2011 Funding Decision.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: 2011 Funding Decision
Date: Monday, September 19, 2016 09:38:37
Attachment 1: Picture (Device Independent Bitmap) 1.jpg

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

Was this contribution rate increase shared by the teachers?

Matthew Colley
Sr. Manager | Audit Advisory
Deloitte LLP
22 Adelaide Street West,
Toronto, Ontario,
M5H 4E3
D: 416-643-8428
mcolley@deloitte.ca | deloitte.ca

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Picture (Device Independent Bitmap) 1.pdf

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A couple of questions.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: A couple of questions
Date: Thursday, December 01, 2016 18:49:46
Attachment 1: PSSRP - valuation allowance v2.docx
Attachment 2: Valuation Allowances for DB Pension Plans v2.pptx

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Hi Lucy.

Just forwarding a couple of docs regarding the NB situation. Having a bit of difficulty following the last slide of the second attachment and how the calculation aligns with my understanding of how the adjusted benefit asset should be computed. (you'll note that the calc begins with a liability vs. asset).

Also, wondering if we can chat regarding the nature of a 7600 Report, just to confirm whether the work being undertaken by the Panel could ever be categorized as such. I don't think so, but would appreciate a chat.

I saw that you called earlier. Talk to you soon.

Nadine

PSSRP - valuation allowance v2.pdf

Public Service Shared Risk Pension Plan – Accounting for Net Pension Assets

Issue

To determine if the Province can record a pension asset for the Public Service Shared Risk Pension Plan.

Relevant PSAS

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

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

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

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

Assessment

Regulation 2012-75 under the *Pension Benefits Act* establishes maximum allowable contribution increases and decreases for shared risk plans. Further, the plan's funding policy has established maximum allowable decreases for this plan, in accordance with the Act, as follows:

Employees currently contribute approximately 8.25% of payroll, which may be reduced by a maximum of 0.50% of payroll in accordance with the plans' funding policy. The Province currently contributes 12.5% of payroll (including temporary contributions), which may be reduced by a maximum of 4.75% (1.25% from elimination of temporary contributions and 3.5% reduction in initial contribution rate). Current period benefit cost (including future indexing) as a percentage of payroll is 14.0% as per the latest actuarial valuation for accounting purposes. Therefore, the minimum employer contribution (7.75%) exceeds the portion of current period benefit cost that is not covered by employees (6.25%).

Illustrated in approximate dollar terms (millions):

Current period benefit cost:	$158.2
Minimum permitted employee contribution:	87.6
Amount not covered by employees:	$ 70.6
Minimum permitted employer contribution:	$ 87.6

Article 3.4 (d) of The Agreement and Declaration of Trust of the PSSRP:

(d) Subject to the *Pension Benefits Act* and the *Income Tax Act*, the following limitations shall apply to the rights to, interests in, or use of, the Fund:

i. No Trustee shall, except when acting as a Trustee and in concert with other Trustees as permitted hereunder, receive or otherwise have control over any of the monies or property which at any time form part of the Fund, except for as described in Section 3.4(b).

ii. Neither the Province, Unions, Employer, Members, nor any other person, association or corporation shall have any right, title or interest in or to the Fund.

iii. Except as otherwise expressly provided herein, no part of the corpus or income of the Fund shall be used for or diverted to purposes other than the exclusive benefit of Members and their beneficiaries.

(note: the reference to section 3.4(b) in paragraph i. refers to administrative and investment management related expenses which are paid by the pension funds)

Conclusion

In accordance with the Plan's funding policy, the Province will always contribute an amount that when added to the minimum employee contribution will sufficiently cover the current period benefit cost. Also, provisions of the Plan's governing documents indicate that the Province can not withdraw excess funds from the Plan. As such, the Province must record a valuation allowance against a net pension asset since no future economic benefit, as contemplated under PS 3250.056, exists.

Valuation Allowances for DB Pension Plans v2.pdf

Valuation Allowances for DB Pension Plans

Analysis of the NB Public Service Shared Risk Pension Plan

PS 3250

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

What is a future economic benefit?

In summary, identified under PS 3250.056 as:

(a) ability to contribute less than employer portion of current period benefit cost, and or

(b) ability to withdraw excess funds.

Contribution reductions

(1) Current period benefit cost = 14% of payroll
(2) Min. employee contribution = 7.75%*
(3) Min. employer contribution = 7.75%*

(3) > [(1)-(2)]

Plan surplus can not be eliminated by contribution decreases alone, therefore, no future economic benefit.

* As specified by the Plan's funding policy (approved by the parties)

Contribution reductions

Illustrated in approximate dollar terms (millions):

Current period benefit cost:	$158.2
Minimum permitted employee contribution:	87.6
Amount not covered by employees:	$ 70.6
Minimum permitted employer contribution:	$ 87.6

Withdrawal of surplus

- Not permitted as per governing documents

- Excerpt from the Agreement and Declaration of Trust :

iii. Except as otherwise expressly provided herein, no part of the corpus or income of the Fund shall be used for or diverted to purposes other than the exclusive benefit of Members and their beneficiaries.

Conclusion

- No future economic benefit under PS 3250.056 (a) or (b)
- The Province recorded a valuation allowance
  - Actuarial Benefit Liability: $ 248.3
  - Unamortized Losses: $(451.0)
  - Net Pension Liability (Asset): $(202.7)
  - Valuation Adjustment: $ 202.7
  - Liability (Asset) recorded: $ ---

Accepted_ Follow-Up Question OPSEUPP.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Shanmugarajah, Ramya (TBS) [Ramya.Shanmugarajah@ontario.ca]; Jack, Shannon (TBS) [SOM3.Shannon.Jack@ontario.ca]; Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]; Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: Accepted: Follow-Up Question OPSEUPP
Date: Tuesday, July 31, 2018 12:06:22

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Accepted_ OTPP - Follow-Up Discussion with EY.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Shanmugarajah, Ramya (TBS) [Ramya.Shanmugarajah@ontario.ca]; Jack, Shannon (TBS) [SOM3.Shannon.Jack@ontario.ca]; Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]; Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: Accepted: OTPP - Follow-Up Discussion with EY
Date: Friday, July 20, 2018 13:50:30

Accepted_ Reference to Deloitte Opinion.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Jack, Shannon (TBS) [Shannon.Jack@ontario.ca]; Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]; Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: Accepted: Reference to Deloitte Opinion
Date: Wednesday, August 30, 2017 17:11:46

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Accepted_ Uros & Cindy Call.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Shanmugarajah, Ramya (TBS) [Ramya.Shanmugarajah@ontario.ca]; Jack, Shannon (TBS) [SOM3.Shannon.Jack@ontario.ca]; Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]; Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: Accepted: Uros & Cindy Call
Date: Thursday, July 26, 2018 10:03:09

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Attachment invite.ics (1418 Bytes) cannot be converted to PDF format.

Cap and Trade accounting.rtf

From: david.c.greenall@pwc.com [david.c.greenall@pwc.com]
To: Virani, Shyrose (TBS) [/o=GOVON/ou=Ontario Public Sector - iSERV EMS/cn=Recipients/cn=viranish03733350]; david.c.greenall@pwc.com [david.c.greenall@pwc.com]
Subject: Cap and Trade accounting
Date:

Upon arrival, please call Shyrose at 416-325-1448 to gain access into our building.

Thanks
Shyrose

Cap and Trade accounting.rtf

From: david.c.greenall@pwc.com [david.c.greenall@pwc.com]
To: Virani, Shyrose (TBS) [/o=GOVON/ou=Ontario Public Sector - iSERV EMS/cn=Recipients/cn=viranish03733350]; david.c.greenall@pwc.com [david.c.greenall@pwc.com]
Subject: Cap and Trade accounting
Date:

Upon arrival, please call Shyrose at 416-325-1448 to gain access into our building.

Thanks
Shyrose

Accepted_ FW_ Pension Planning.rtf

From: Gregory Winston [gregory.winston@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Accepted: FW: Pension Planning
Date: Friday, December 08, 2017 11:06:09

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Attachment invite.ics (1297 Bytes) cannot be converted to PDF format.

Accepted_ OTPP (Legal Opinion) - call with Deloitte (Martin Raymond).rtf

From: Dyczkowski, Marilyn (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Accepted: OTPP (Legal Opinion) - call with Deloitte (Martin Raymond)
Date: Monday, September 12, 2016 07:43:21

Accepted_ OTPP (Legal Opinion) - call with Deloitte (Martin Raymond).rtf

From: Manji, Shemin (MOF) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Accepted: OTPP (Legal Opinion) - call with Deloitte (Martin Raymond)
Date: Saturday, September 10, 2016 10:59:43

Accepted_ OTPP (Legal Opinion) - call with Deloitte (Martin Raymond).rtf

From: Kaufman, Paul (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Accepted: OTPP (Legal Opinion) - call with Deloitte (Martin Raymond)
Date: Saturday, September 10, 2016 10:40:20

Accepted_ PSPP HOOP and CAAT.rtf

From: Gregory Winston [gregory.winston@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Accepted: PSPP HOOP and CAAT
Date: Wednesday, January 17, 2018 12:24:21

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Accepted_ Pension Asset - additional advice.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Accepted: Pension Asset - additional advice
Date: Friday, June 22, 2018 10:48:38

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Access Letters.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Tam, Nelson (TBS) [Nelson.Tam@ontario.ca]
CC: Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]
Subject: Access Letters
Date: Friday, November 18, 2016 10:53:45
Attachment 1: Picture (Device Independent Bitmap) 1.jpg
Attachment 2: Access letter _Uros Karadzic -signed.pdf
Attachment 3: Access letter _Karen Hughes -signed.pdf
Attachment 4: Access letter _Murray Gold -signed.pdf
Attachment 5: Access letter _Paul Martin -signed.pdf
Attachment 6: Access letter _Tricia O'Malley -signed.pdf

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Matthew Colley
Sr. Manager | Audit Advisory
Deloitte LLP
22 Adelaide Street West,
Toronto, Ontario,
M5H 4E3
D: 416-643-8428
mcolley@deloitte.ca | deloitte.ca

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Access letter _Uros Karadzic -signed.pdf

Deloitte.

Deloitte LLP
Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6610
www.deloitte.ca

November 17, 2016

Mr. Uros Karadzic
c/o Nelson Tam
Treasury Board Secretariat,
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Mr. Karadzic

Access to Deloitte report on the application of accounting principles under section 7600 of the CPA Canada Handbook, dated October 2, 2016

The Treasury Board Secretariat of the Province of Ontario (the "Province") has informed Mr. Uros Karadzic, (the "Recipient"), that Deloitte LLP ("Deloitte") has provided a report on the application of accounting principles under section 7600 of the CPA Canada Handbook dated October 2, 2016 as well as Analysis of Pension Asset Ceiling Accounting Considerations for the Office of the Provincial Controller Division re: Ontario Teachers' Pension Plan (OTPP) dated August 19, 2016 (the "Reports"). The Province has requested that the Recipient obtain from Deloitte access to the Reports that was prepared for the Province. This letter sets out the terms on which we are prepared to provide the Recipient with access to the Reports. The August 19 report was prepared to assist management in developing their own analysis; Deloitte was not engaged to and did not provide an opinion in that report.

Recipient acknowledges and agree to the following:

1. The Reports were prepared for the Province in assessing its accounting treatment for the OTPP. Accordingly, Deloitte may not have addressed matters which may be of specific interest or relevance to the Recipient. Deloitte does not warrant or represent that the Report is sufficient or appropriate for the Recipient's purposes.

2. The Reports are subject to the assumptions, qualifications, limitations, and restrictions set out in the Report. The Reports do not address all matters that Deloitte is or may become aware of whether or not such matters might be considered material by the Recipient. Deloitte has no responsibility to advise the Recipient of any additional matters.

3. Deloitte is not responsible to the Recipient, or any other party, if you rely on the Reports. The Recipient is responsible for making its own enquiries and performing its own procedures in connection with the Recipient's work.

4. The Recipient will not acquire any rights in connection with access to the Reports and we have no duty of care to the Recipient for the work we have performed or for the contents of the Reports or any issues referred to in the Reports.

5. The Recipient agrees to release Deloitte and our respective personnel against all actions, claims, suits, demands, claim for cost or expenses or any another proceedings arising in connection with access to the Reports or arising out of a breach of any of the Recipient's obligations hereunder

6. The Reports are confidential information and must be treated as such by the Recipient. The Recipient must not disclose the Reports in whole or in part, to any other person, reproduce the Reports, in whole or in part, for any purpose, or make reference to the Reports in any report or document.

7. The Recipient must not publicly refer to our services in connection with the Reports or name us in any report or document which will be publicly available or lodged or filed with any regulator without our prior written consent, such consent will be granted at our absolute discretion and may be subject to conditions.

8. The Recipient acknowledges that damages may not be a sufficient remedy for any breach of this Agreement and Deloitte may be entitled to specific performance or injunctive relief (as appropriate) as a remedy for any breach or threatened breach by the Recipient, in addition to any other remedies available to Deloitte at law or in equity.

9. This letter shall be governed and construed in accordance with the laws of the Province of Ontario. Each party submits to the courts of this jurisdiction and waives any defence of inconvenient forum to the maintenance of such action or proceeding.

If you have any questions regarding the above, please do not hesitate to contact Kerry Danyluk via e-mail at kdanyluk@deloitte.ca. Please acknowledge that you accept these terms by signing dating and returning the enclosed copy of this letter to us care of Nelson Tam.

Yours very truly

Deloitte LLP.

By: Kerry Danyluk
Partner

Acknowledged and agreed:

_____
Name

_____
Title

_____
Date

Access letter _Karen Hughes -signed.pdf

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Deloitte LLP
Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6610
www.deloitte.ca

November 17, 2016

Ms. Karen Hughes
Associate Deputy Minister
Treasury Board Secretariat
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Ms. Hughes

Access to Deloitte report on the application of accounting principles under section 7600 of the CPA Canada Handbook, dated October 2, 2016

We were engaged of behalf of Treasury Board Secretariat of the Province of Ontario (the "Province"). In connection with that engagement, Deloitte provided a report on the application of accounting principles under section 7600 of the CPA Canada Handbook date October 2, 2016 (the "Report"). Specifically, the Report deals with the application of certain aspects of Canadian public sector accounting standards to the recognition of the accrued benefit asset related to the Ontario Teachers' Pension Plan (OTPP or the Plan) in connection with the March 31, 2016 public accounts. You have requested that we give access to the Report to members of Pension Asset Expert Advisory Panel for information purposes (the "Recipients").

You acknowledge and agree that we shall have no responsibility to you if any of the Recipients misuse any confidential information obtained from their review of the Report.

In consideration of our agreeing to provide such access to the Recipients, you agree not to bring any actions, proceedings or claims against us in any way arising out of or in connection with the grant of access to the Report to the Recipients.

Our agreement to the Report being made available to the Recipients is subject to the prior condition that we obtain from each of the Recipients an agreement that each Recipient acquires no rights against Deloitte as a result of such access and an acknowledgement that they each recognise the basis on which access is provided.

Please confirm your understanding and agreement with the foregoing by signing, dating and returning to us the enclosed copy of this letter.

Yours very truly

Deloitte LLP

By: Kerry Danyluk
Partner

Acknowledged and agreed:

Signature	Position	Date

Access letter _Murray Gold -signed.pdf

Deloitte.

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Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6610
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November 17, 2016

Mr. Murray Gold
c/o Nelson Tam
Treasury Board Secretariat,
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Mr. Gold

Access to Deloitte report on the application of accounting principles under section 7600 of the CPA Canada Handbook, dated October 2, 2016

The Treasury Board Secretariat of the Province of Ontario (the "Province") has informed Mr. Murray Gold, (the "Recipient"), that Deloitte LLP ("Deloitte") has provided a report on the application of accounting principles under section 7600 of the CPA Canada Handbook dated October 2, 2016 as well as Analysis of Pension Asset Ceiling Accounting Considerations for the Office of the Provincial Controller Division re: Ontario Teachers' Pension Plan (OTPP) dated August 19, 2016 (the "Reports"). The Province has requested that the Recipient obtain from Deloitte access to the Reports that was prepared for the Province. This letter sets out the terms on which we are prepared to provide the Recipient with access to the Reports. The August 19 report was prepared to assist management in developing their own analysis; Deloitte was not engaged to and did not provide an opinion in that report.

Recipient acknowledges and agree to the following:

1. The Reports were prepared for the Province in assessing its accounting treatment for the OTPP. Accordingly, Deloitte may not have addressed matters which may be of specific interest or relevance to the Recipient. Deloitte does not warrant or represent that the Report is sufficient or appropriate for the Recipient's purposes.

2. The Reports are subject to the assumptions, qualifications, limitations, and restrictions set out in the Report. The Reports do not address all matters that Deloitte is or may become aware of whether or not such matters might be considered material by the Recipient. Deloitte has no responsibility to advise the Recipient of any additional matters.

3. Deloitte is not responsible to the Recipient, or any other party, if you rely on the Reports. The Recipient is responsible for making its own enquiries and performing its own procedures in connection with the Recipient's work.

4. The Recipient will not acquire any rights in connection with access to the Reports and we have no duty of care to the Recipient for the work we have performed or for the contents of the Reports or any issues referred to in the Reports.

5. The Recipient agrees to release Deloitte and our respective personnel against all actions, claims, suits, demands, claim for cost or expenses or any another proceedings arising in connection with access to the Reports or arising out of a breach of any of the Recipient's obligations hereunder

6. The Reports are confidential information and must be treated as such by the Recipient. The Recipient must not disclose the Reports in whole or in part, to any other person, reproduce the Reports, in whole or in part, for any purpose, or make reference to the Reports in any report or document.

7. The Recipient must not publicly refer to our services in connection with the Reports or name us in any report or document which will be publicly available or lodged or filed with any regulator without our prior written consent, such consent will be granted at our absolute discretion and may be subject to conditions.

8. The Recipient acknowledges that damages may not be a sufficient remedy for any breach of this Agreement and Deloitte may be entitled to specific performance or injunctive relief (as appropriate) as a remedy for any breach or threatened breach by the Recipient, in addition to any other remedies available to Deloitte at law or in equity.

9. This letter shall be governed and construed in accordance with the laws of the Province of Ontario. Each party submits to the courts of this jurisdiction and waives any defence of inconvenient forum to the maintenance of such action or proceeding.

If you have any questions regarding the above, please do not hesitate to contact Kerry Danyluk via e-mail at kdanyluk@deloitte.ca. Please acknowledge that you accept these terms by signing dating and returning the enclosed copy of this letter to us care of Nelson Tam.

Yours very truly

Deloitte LLP

By: Kerry Danyluk
Partner

Acknowledged and agreed:

_____
Name

_____
Title

_____
Date

Access letter _Paul Martin -signed.pdf

Deloitte.

Deloitte LLP
Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6610
www.deloitte.ca

November 17, 2016

Mr. Paul Martin
c/o Nelson Tam
Treasury Board Secretariat,
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Mr. Martin

Access to Deloitte report on the application of accounting principles under section 7600 of the CPA Canada Handbook, dated October 2, 2016

The Treasury Board Secretariat of the Province of Ontario (the "Province") has informed Mr. Paul Martin, (the "Recipient"), that Deloitte LLP ("Deloitte") has provided a report on the application of accounting principles under section 7600 of the CPA Canada Handbook dated October 2, 2016 as well as Analysis of Pension Asset Ceiling Accounting Considerations for the Office of the Provincial Controller Division re: Ontario Teachers' Pension Plan (OTPP) dated August 19, 2016 (the "Reports"). The Province has requested that the Recipient obtain from Deloitte access to the Reports that was prepared for the Province. This letter sets out the terms on which we are prepared to provide the Recipient with access to the Reports. The August 19 report was prepared to assist management in developing their own analysis; Deloitte was not engaged to and did not provide an opinion in that report.

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Yours very truly

Deloitte LLP.

By: Kerry Danyluk
Partner

Acknowledged and agreed:

_____
Name

_____
Title

_____
Date

Access letter _Tricia O’Malley -signed.pdf

Deloitte.

Deloitte LLP
Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6610
www.deloitte.ca

November 17, 2016

Ms. Tricia O'Malley
c/o Nelson Tam
Treasury Board Secretariat,
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Ms. O'Malley

Access to Deloitte report on the application of accounting principles under section 7600 of the CPA Canada Handbook, dated October 2, 2016

The Treasury Board Secretariat of the Province of Ontario (the "Province") has informed Ms. Tricia O'Malley, (the "Recipient"), that Deloitte LLP ("Deloitte") has provided a report on the application of accounting principles under section 7600 of the CPA Canada Handbook dated October 2, 2016 as well as Analysis of Pension Asset Ceiling Accounting Considerations for the Office of the Provincial Controller Division re: Ontario Teachers' Pension Plan (OTPP) dated August 19, 2016 (the "Reports"). The Province has requested that the Recipient obtain from Deloitte access to the Reports that was prepared for the Province. This letter sets out the terms on which we are prepared to provide the Recipient with access to the Reports. The August 19 report was prepared to assist management in developing their own analysis; Deloitte was not engaged to and did not provide an opinion in that report.

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Yours very truly

Deloitte LLP.

By: Kerry Danyluk
Partner

Acknowledged and agreed:

_____
Name

_____
Title

_____
Date

Meeting to review proposed Cap and Trade accounting.rtf

From: david.c.greenall@pwc.com [david.c.greenall@pwc.com]
To: Virani, Shyrose (TBS) [/o=GOVON/ou=Ontario Public Sector - iSERV EMS/cn=Recipients/cn=viranish03733350]; david.c.greenall@pwc.com [david.c.greenall@pwc.com]
Subject: Meeting to review proposed Cap and Trade accounting
Date:

Myra/Doris

Pls extend the invite to appropriate staff.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Meeting with PwC.rtf

From: david.c.greenall@pwc.com [david.c.greenall@pwc.com]
To: Virani, Shyrose (TBS) [/o=GOVON/ou=Ontario Public Sector - iSERV EMS/cn=Recipients/cn=viranish03733350]; david.c.greenall@pwc.com [david.c.greenall@pwc.com]
Subject: Meeting with PwC
Date:

Re_ Availability for a call tomorrow_.rtf

From: lucy.durocher@pwc.com [lucy.durocher@pwc.com]
To: Virani, Shyrose (TBS) [/o=GOVON/ou=Ontario Public Sector - iSERV EMS/cn=Recipients/cn=viranish03733350]; lucy.durocher@pwc.com [lucy.durocher@pwc.com]
Subject: Re: Availability for a call tomorrow?
Date:

From: lucy.durocher@ca.pwc.com<mailto:lucy.durocher@ca.pwc.com>
Sent: June 5, 2017 9:26 PM
To: Petsche, Nadine (TBS)
Cc: Virani, Shyrose (TBS)
Subject: Re: Availability for a call tomorrow?

Hi Nadine,

It's good to hear from you. We can definitely arrange a call for tomorrow. I have good availability after 11:30- let me know what time works for you.
I may have to do some digging re: TTC so may not have all the answers on that tomorrow, but we can set up a call anyway on cap and trade and I'll see what I can find out on the pensions prior.

Lucy

Sent from my iPhone

On Jun 5, 2017, at 9:01 PM, Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca<mailto:Nadine.Petsche@ontario.ca>> wrote:

Hi Lucy.

I hope that this note finds you well. I was hoping that you might have some insights on a couple of items, or alternatively that you might be able to direct me in the right direction on a couple of items:

1. We were wondering if you might have some info on how companies are accounting for cap & trade when they are the buyer of the EAs. Specifically, if a company chooses not to purchases anything at the auction, are they recognizing an expense and an accrual? If they buy the EA, how are they accounting for it – e.g. setting it up as a prepaid and expensing it when they pay the amount or amortizing it?

2. Secondly, we understand that the TTC is taking a valuation allowance on its net pension assets but we haven't been able to locate details on the rational for the allowance in the notes to the TTC's f/s. We noticed that PwC is the organization's auditor, and we wondered if you might be able to provide some additional context.

If you have some availability tomorrow, perhaps we can touch base.

Take care,

Nadine

_____

This e-mail is intended only for the person to whom it is addressed (the "addressee") and may contain confidential and/or privileged material. Any review, retransmission, dissemination or other use that a person other than the addressee makes of this communication is prohibited and any reliance or decisions made based on it, are the responsibility of such person. We accept no responsibility for any loss or damages suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

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Additional doc.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Additional doc
Date: Friday, September 16, 2016 19:29:09
Attachment 1: MOF letter 2_appendix.pdf

Hi Lucy.

We just received the attached letter this afternoon. I understand that we can expect to receive the external legal opinion sometime this weekend. I will forward it to you when I receive it.

Nadine

MOF letter 2_appendix.pdf

ONTARIO TEACHERS' PENSION PLAN

5650 Yonge Street
Toronto, Ontario, Canada
M2M 4H5

tel: 416-228-5900 or 1 877-812-7989
fax: 416-730-5349
www.otpp.com

September 16, 2016

Alex Killoch, Director
BPS Pensions Branch
Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto, Ontario
M7A 1Y7

Dear Alex:

Re: Ontario Teachers' Pension Plan (Plan) Financial Statement Results

As requested - and further to our correspondence dated September 15, 2016 - we are providing information related to the financial statement valuation results as at December 31, 2015 published in our 2015 Annual Report.

The Plan is subject to several valuations which serve different purposes and produce results that vary due to actuarial cost methods and the underlying actuarial assumptions. First, the Plan's funding valuation assesses the long-term financial health of the Plan to facilitate determinations of future contribution rates and benefit levels. Second, the Plan's financial statement valuation is a mark-to-market, current snap shot view of the financial position of the plan at a point in time where assumptions and methodology are outlined by the Chartered Professional Accountants (CPA) Handbook. Lastly, on annual basis, we receive a request from the Ontario Ministry of Finance to produce results, based on their assumptions, used to prepare the Ontario Budget as outlined in the Chartered Professional Accountants of Canada Public Sector Accounting Board Handbook.

Financial Statement Reporting

The CPA Handbook allows two approaches for multi-employer pension plans in the creation of their financial statement reporting. They may use their funding valuation or valuation results prepared in accordance with Section 4600 of the CPA Handbook. Teachers' has chosen the latter approach for the following two reasons:

- An important feature of the Plan is Conditional Inflation Protection (CIP). To properly reflect the nature of CIP, the cost method used for funding purposes is the aggregate method which allows the Plan to address surpluses and deficits through future benefit changes. This cost method differs from that required by the accounting standards (i.e. the projected benefit cost method, prorated on services). So the funding valuation would not be appropriate for financial statement reporting.

- The funding valuation of the Plan employs an asset smoothing method to mitigate volatility in the market value of assets. Asset smoothing is no longer permitted under Section 4600 of the CPA Handbook.

Discount Rates

A key assumption in actuarial valuations is the discount rate. The methodology for determining the discount rate is different for each valuation. For the funding valuation, the rate is based on the expected return on assets with margins. The actuary must confirm that the assumptions used within a funding valuation are independently reasonable and are appropriate in aggregate in accordance with the Canadian Institute of Actuaries Standards of Practice. For the financial statement valuation, the rate is based on current market rates in accordance with the CPA Handbook. For the Ontario Budget, the best estimates are used in accordance with the Public Sector Accounting Board standards. In particular:

- The annual valuation performed for funding purposes determines the discount rate by reference to what the Plan's assets can reasonably be expected to earn over the long run less expenses and less provisions for adverse deviation (PFAD). For the January 1, 2016 funding valuation (which will be filed with the regulatory authorities by September 30th), the nominal discount rate is 4.8% with an underlying real return of 2.75%. This real return takes into account PFADs of approximately 1.5%.

- As described in Note 4. of the 2015 Annual Report, the discount rate used to determine liabilities on a financial statement valuation basis (3.25% nominal, 1.70% real) is based on market rates, as at the valuation date, of bonds issued by the Province of Ontario, which have characteristics similar to the Plan's liabilities. The discount rate was determined by applying a weighted average discount rate that reflects the estimated timing and amount of benefit payments. Please see further detail below on Section 4600 of the CPA Canada Handbook requirements related to discount rate determination.

- As noted in the December 11, 2015 correspondence from the Ontario Ministry of Finance, the Province uses best estimate assumptions as required by the Public Sector Accounting Standards (i.e. without PFADs). The December letter provided the specific assumptions to be used in the valuation (to be performed by the external Plan actuary – Mercer) including return on investment, inflation, real rate of return and anticipated salary growth. Public Sector Accounting Standards provide for determination of discount rates by reference to the expected return on the pension plan's assets.

Please do not hesitate to call if you have any questions or require further information.

Sincerely,

Barbara Zvan, FSA, FCIA, CERA
SVP, Strategy & Risk and Chief Investment Risk Officer
(416) 730-6364
Barbara_zvan@otpp.com

cc: Ross Peebles
Joshua Paul
Rob Pomykacz
Allan Shapira
David McGraw
Mary Cover

Appendix A

Discount Rate Determination under Section 4600 of the CPA Canada Handbook

Section 4600 of the CPA Canada Handbook specifies that defined benefit obligation guidance can be found in the Employee Future Benefits Section 3462 (Part II of the CPA Canada Handbook) and in IAS 19 Employee Benefits (Part I of the Handbook).

- Section 3462 indicates that the discount rate should be determined with reference to market interest rates on high-quality debt instruments.
- Both Section 3462 and IAS 19 provide that when rates on high-quality corporate bonds are available, they are used to determine the discount rate and that when the market for corporate bonds is not deep or they do not extend far enough into the future to match the cash flows inherent in the defined benefit obligation, the rates on government bonds may be used to determine the discount rate.
- Both Section 3462 and IAS 19 provide that the rates used should reflect the estimated timing of benefit payments.

Agenda.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Agenda
Date: Monday, December 05, 2016 00:03:50
Attachment 1: Dec. 5 Agenda.docx

Hi Lucy.

Attached is a copy of the agenda.

Nadine

Dec. 5 Agenda.pdf

AGENDA

Pension Asset Expert Panel

December 5, 2016

Attendees

Patricia O'Malley – Chair

Murray Gold

Uros Karadzic

Paul Martin

Nelson Tam – Project Manager

Topic	Lead	
1. November 18 Meeting Minutes Approval, Report Writer Update, Timelines, Briefings on Other Pension Plans	Chair/Nelson	8:45 – 9:00
2. Auditor General a. Invitation b. Annual Report	Chair	9:00 – 9:30
3. Report Outline	Chair	9:30 – 10:30
4. Break		10:30 – 10:45
5. Confirmation of the Questions to be Answered	Chair	10:45– 12:00
6. Lunch		12:00 – 1:00
7. Discussion on Recognition – Viewpoints and Pros and Cons	Chair	1:00 – 3:00
8. Break	Chair	3:00 – 3:15
9. Discussion on Measurement – Viewpoints and Pros and Cons		3:15 – 4:45
10. Next Steps	Chair	4:45 – 5:00

Amendment document from Lucy Durocher, PwC.rtf

From: tracey.whelan@ca.pwc.com [tracey.whelan@ca.pwc.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Amendment document from Lucy Durocher, PwC
Date: Thursday, October 20, 2016 10:43:37
Attachment 1: NuanceScanDoc_10_20_16_10_22.pdf

Tracey Whelan
PwC, Audit and Assurance Group
T: +1 416 941 8383 ext. 14223 | F: +1 416 941 8481
Email: tracey.whelan@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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NuanceScanDoc_10_20_16_10_22.pdf

AMENDMENT
To Add an Additional Resource to a Project

Agreement Number and Description of Project:	OPCD-PWC-01 Accounting Advisory Services
Original SOW Date:	September 16, 2016
Name of Vendor:	PricewaterhouseCoopers LLP
Date of Amendment:	October 18, 2016
Amendment Number:	001

1) Amendment Details:

1.1 This amendment hereby exercises the Ministry's right to add an additional resource to support this project. The additional resource is:

Names, Roles and Per Diem Rates:

Individual's Legal Name	Individual's Role (& level)	Per Diem Rate
Mario Chassé	General Consultant (Actuarial), Level 2 Service Category 2	The per diem rate shall be equal to the per diem rates stipulated in the SOW for each deliverable (ie Accounting Advisory and Accounting Opinion).

1.2 The additional resource does not change the scope, deliverables, or ceiling value of the project.

1.3 This amendment is subject to the terms and conditions of the Master Agreement.

1.4 All other terms and conditions of the Statement of Work OPCD-PWC-01 between PricewaterhouseCoopers LLP and the Ministry are unchanged.

HER MAJESTY THE QUEEN in right of Ontario
as represented by the Minister of the Treasury Board
Secretariat

Per: D. Petsche

Print Name: Dorina Petsche

Title: Director, Accounting Policy and Financial Reporting

PricewaterhouseCoopers LLP

Acknowledged: PricewaterhouseCoopers LLP

Print Name: PRICEWATERHOUSE COOPERS LLP

Title: pp. LUCY DURCHER, PARTNER

Another Q.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Another Q
Date: Friday, September 23, 2016 12:17:18
Attachment 1: 2007 Teachers Survey Apendix.pdf
Attachment 2: 2007 Teachers Survey.pdf

Hi Lucy

Attached pls find above documents from Nadine. The docs reflect member expectations on future rates.

Thanks

Shyrose

2007 Teachers Survey Apendix.pdf

Appendix A: Study interview schedule

POLLARA

Interview Schedule

A. Introduction

Good morning/afternoon/evening. May I please speak with (MEMBER NAME)?

IF AVAILABLE- CONTINUE
IF NOT AVAILABLE - SCHEDULE APPOINTMENT TO CALL BACK (IF NECESSARY, READ FIRST 2 SENTENCES OF PREAMBLE BELOW AND SCHEDULE CALL-BACK)

(WHEN MEMBER IS ON LINE) Good morning/afternoon/evening. My name is ( ) and I am calling on behalf of the Ontario Teachers' Pension Plan, the Ontario Teachers' Federation and the Ontario Government, from POLLARA, a national research firm. We are conducting a survey of pension plan members, which will provide these groups with information about members' preferences. Would you mind if I asked you some questions? All of your responses will be kept completely confidential. (IF ASKED: On average, the survey takes about 10 minutes to complete.)

(IF YES) Thank you (PROCEED TO QUESTION 1)
(IF NO) When is a better time for me to call back? (SCHEDULE APPOINTMENT UP TO AND INCLUDING May 2; MONDAY-FRIDAY 5pm-9pm; SATURDAY 9am-5pm; NO SUNDAY CALLS.)

B. Objective 1: To determine the level of awareness and understanding among Plan members about the current level of benefits and contributions.

To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF BENEFITS)

1. Members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (95%)
   Unaware ..... (4%)
   Don't know ..... (<1%)
   Refused ..... (<1%)

2. The monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (87%)
   Unaware ..... (12%)
   Don't know ..... (1%)
   Refused ..... (<1%)

3. The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made. (IF NECESSARY: Were you aware or unaware of this?)

Aware	(74%)
Unaware	(25%)
Don't know	(1%)
Refused	(<1%)

(END RANDOMIZATION OF STATEMENTS)

Now I'd like to ask you about some other pension issues.

4. Prior to my call, were you aware or unaware that the pension plan does not provide dental and other health benefit coverage to retirees?

Aware	(68%)
Unaware	(31%)
Don't know	(1%)
Refused	(<1%)

5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?

Aware	(63%)
Unaware	(36%)
Don't know	(1%)
Refused	(<1%)

6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible? (IF REQUIRED: Similar to an RRSP, you can deduct your total pension contributions from your net income on page 3 of your tax return.)

Aware	(66%)
Unaware	(32%)
Don't know	(1%)
Refused	(<1%)

7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?

Higher	(23%)
Lower	(10%)
About the same amount	(38%)
Don't know	(29%)
Refused	(<1%)

8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan? (READ LIST - STOP AFTER ANSWER IS GIVEN)

Less than 5%	(5%)
5% to less than 7%	(10%)
7% to less than 9%	(17%)
9% to less than 12%	(24%)
12% to less than 15%	(4%)
15% or more	(5%)
Don't know (DO NOT READ)	(35%)
Refused (DO NOT READ)	(<1%)

9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

Up	(77%)
Down	(1%)
Stay the same	(13%)
Don't know	(9%)
Refused	(<1%)

C. Objective 2: To measure plan members' preferences in terms of increased contributions vs. decreased benefits, if a future valuation shows an increased shortfall.

Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These increases are required to keep pension provisions for future service at current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

10. (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

Higher	(27%)
Lower	(3%)
Same	(64%)
Don't know	(6%)
Refused	(<1%)

11. (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

Yes	(47%)
No	(49%)
Don't know	(4%)
Refused	(<1%)

Although all members are guaranteed pensions, the Ontario Teachers' Pension Plan, like many other pension plans, is facing funding challenges. Decisions may need to be made about whether to further increase members' contributions beyond the increases we have just discussed. The alternative to increasing contributions is reducing the level of pension provisions that will be earned from the time the change is made until members retire.

(IF RESPONDENT ASKS: By law, such changes could not affect the pensions provided to those who have already retired. Likewise, pension provisions that have already been earned by working members could not be reduced. Such changes could only be applied into the future.)

12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(5%)
10.0%	(15%)
10.1%-11.0%	(7%)
11.1%-12.0%	(20%)
12.1%-13.0%	(8%)
13.1%-14.0%	(2%)
14.1%-15.0%	(27%)
Greater than 15.0%	(3%)
Don't know	(12%)
Refused	(1%)
Mean (%):	12.34
Median (%):	12.0
Mode (%):	15.0

13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12. EXCLUDE IF Q12 = "Don't know" or "Refused") If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than (INSERT RESPONSE FROM Q12) of your salary in order to keep all pension provisions at current levels?

(IF ASKED: Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These changes are required to keep the pension provisions for future service at their current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

In favour	(36%)
Not in favour	(53%)
Don't know	(10%)
Refused	(<1%)

Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level. Please tell me whether you would be in favour or not in favour of each of the following changes. How about: (READ - RANDOMIZE ORDER OF PROVISIONS)

(IF REQUIRED, READ: Please keep in mind that by law, these changes could not affect the pensions provided to those who have already retired. Likewise, current pension provisions that have already been earned by working members could not be reduced.)

14. Increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it. (IF ASKED: Members can currently retire with unreduced monthly pension payments when their age plus years of service equals eighty-five, or when they reach the age of 65.) (IF ASKED: Discussions would take place between the OTF and the government to decide on a transition period.)

In favour	(41%)
Not in favour	(57%)
Don't know	(2%)
Refused	(<1%)

15. Reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

In favour	(32%)
Not in favour	(57%)
Don't know	(11%)
Refused	(<1%)

16. Making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

In favour	(51%)
Not in favour	(43%)
Don't know	(5%)
Refused	(<1%)

(END OF QUESTION RANDOMIZATION)

17. We've just discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. When I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan. (RANDOMIZE ORDER OF CHANGES)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

Decreasing your monthly pension for future service by 10%	(11%)
Increasing the eighty-five factor to a ninety factor	(37%)
Providing flexibility for the cost-of-living adjustment	(44%)
Don't know (DO NOT READ OR RANDOMIZE)	(3%)
Refused (DO NOT READ OR RANDOMIZE)	(4%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

18. Which potential change are you least willing to have made? (REPEAT REMAINING CHANGES AS REQUIRED)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act)

Decreasing your monthly pension for future service by 10%	(37%)
Increasing the eighty-five factor to a ninety factor	(41%)
Providing flexibility to the cost-of-living adjustment	(16%)
Don't know (DO NOT READ OR RANDOMIZE)	(3%)
Refused (DO NOT READ OR RANDOMIZE)	(2%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(6%)
10.0%	(11%)
10.1%-11.0%	(8%)
11.1%-12.0%	(22%)
12.1%-13.0%	(8%)
13.1%-14.0%	(3%)
14.1%-15.0%	(29%)
Greater than 15.0%	(5%)
Don't know	(8%)
Refused	(1%)
Mean (%):	12.55
Median (%):	12.0
Mode (%):	15.0

D. Objective 3: To identify the views of sub-groups of members who may have different perspectives based on their circumstances.

20. (ASK IF AGE + YEARS OF CREDIT = >74) Which one of the following three statements best represents your own viewpoint: (RANDOMIZE ORDER OF STATEMENTS - REPEAT AS REQUIRED)

    If pension contributions increase to more than about eleven percent of your salary, you will consider retiring earlier than planned, even if your pension provisions remain the same ..... (13%)

    If the pension provisions you will earn in future years are reduced you will consider retiring earlier than planned, even if your contribution rates remain the same ..... (19%)

    You are unlikely to consider retiring earlier than planned as a result of changes to your future pension provisions and contribution rates. .. (55%)

    Don't know (DO NOT READ OR RANDOMIZE) ..... (10%)
    Refused (DO NOT READ OR RANDOMIZE) ..... (4%)

21. Do you work at an elementary school, a secondary school, or at another organization?

    Elementary ..... (63%)
    Secondary ..... (33%)
    Other ..... (4%)
    Refused ..... (<1%)

We have come to the end of our survey. Thank you very much for your time, we appreciate your participation. (IF RESPONDENT WANTS TO LEARN MORE ABOUT THE ISSUES DISCUSSED IN THE SURVEY: Would you like me to give you some web site addresses that provide further detail on the pension plan issues discussed in this survey? (IF YES): www.otpp.com; www.otffeo.on.ca)

22. Gender (INTERVIEWER-RECORDED)

    Male ..... (26%)
    Female ..... (74%)

23. Employment type (SAMPLE)

    Full-time ..... (83%)
    Part-time ..... (7%)
    Occasional ..... (10%)

24. Employer type (SAMPLE)

English School Board	(94%)
French School Board	(5%)
Other	(1%)

25. Years of credit (SAMPLE)

0-4.9	(26%)
5-9.9	(28%)
10-14.9	(15%)
15-19.9	(14%)
20-24.9	(8%)
25 And Over	(9%)

26. Career Status Grouping (SAMPLE)

Newer members (0-4.9 years)	(26%)
Newer members (5-9.9 years)	(26%)
Mid-career members (10-14.9 years)	(12%)
Mid-career members (15-21.9 years)	(7%)
Older members (within 10 years of an unreduced pension)	(14%)
Older members (within 5 years of an unreduced pension)	(12%)
Older members (eligible for unreduced pension)	(5%)

27. Other years of credit collapse (SAMPLE)

0-6.9 years of actual credit	(36%)
7-14.9 years of actual credit	(27%)
15-21.9 years of actual credit	(7%)
Within 10 years or less of an unreduced pension	(14%)
Within 5 years of unreduced pension	(12%)
Already eligible unreduced pension	(5%)

29. Age (SAMPLE)

Under 35 Yrs	(24%)
35-44	(32%)
45-54	(31%)
55-64	(13%)
65 And Over	(<1%)

30. Urban/Rural (SAMPLE)

Urban	(86%)
Rural	(14%)

31. Administration (SAMPLE)

Administration	(6%)
Non-Administration	(94%)

Appendix B: LTIP interview schedule

LTIP interview schedule

- Some individuals contained in member records were receiving long-term income protection (LTIP) through their employer. A total of 21 individuals on LTIP completed this survey. These results have been excluded from the findings presented in other sections of this report because the mandate of the study was to understand contribution and benefit issues among active, *contributing* pension plan members.
- A total of 21 individuals on LTIP completed the survey, the results of which are presented in the following interview schedule. Due to the extremely small sample size, results should not be generalized to all individuals on LTIP.

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Interview Schedule

A. Introduction

Good morning/afternoon/evening. May I please speak with (MEMBER NAME)?

IF AVAILABLE- CONTINUE
IF NOT AVAILABLE - SCHEDULE APPOINTMENT TO CALL BACK (IF NECESSARY, READ FIRST 2 SENTENCES OF PREAMBLE BELOW AND SCHEDULE CALL-BACK)

(WHEN MEMBER IS ON LINE) Good morning/afternoon/evening. My name is ( ) and I am calling on behalf of the Ontario Teachers' Pension Plan, the Ontario Teachers' Federation and the Ontario Government, from POLLARA, a national research firm. We are conducting a survey of pension plan members, which will provide these groups with information about members' preferences. Would you mind if I asked you some questions? All of your responses will be kept completely confidential. (IF ASKED: On average, the survey takes about 10 minutes to complete.)

(IF YES) Thank you (PROCEED TO QUESTION 1)
(IF NO) When is a better time for me to call back? (SCHEDULE APPOINTMENT UP TO AND INCLUDING May 2; MONDAY-FRIDAY 5pm-9pm; SATURDAY 9am-5pm; NO SUNDAY CALLS.)

LTIP Plan
(n=21)

B. Objective 1: To determine the level of awareness and understanding among Plan members about the current level of benefits and contributions.

To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF BENEFITS)

1. Members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (100%)

2. The monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (86%)
   Unaware ..... (10%)
   Don't know ..... (5%)

	LTIP Plan (n=21)
3. The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made. (IF NECESSARY: Were you aware or unaware of this?)	
Aware	(76%)
Unaware	(24%)

(END RANDOMIZATION OF STATEMENTS)

Now I'd like to ask you about some other pension issues.

4. Prior to my call, were you aware or unaware that the pension plan does not provide dental and other health benefit coverage to retirees?	
Aware	(71%)
Unaware	(24%)
Don't know	(5%)
5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?	
Aware	(48%)
Unaware	(38%)
Don't know	(14%)
6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible? (IF REQUIRED: Similar to an RRSP, you can deduct your total pension contributions from your net income on page 3 of your tax return.)	
Aware	(67%)
Unaware	(29%)
Don't know	(5%)
7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?	
Higher	(29%)
Lower	(5%)
About the same amount	(24%)
Don't know	(43%)

	LTIP Plan (n=21)

8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan? (READ LIST - STOP AFTER ANSWER IS GIVEN)

Less than 5%	(5%)
5% to less than 7%	(<1%)
7% to less than 9%	(14%)
9% to less than 12%	(24%)
12% to less than 15%	(<1%)
15% or more	(<1%)
Don't know (DO NOT READ)	(52%)
Refused (DO NOT READ)	(5%)

9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

Up	(43%)
Down	(10%)
Stay the same	(24%)
Don't know	(24%)

C. Objective 2: To measure plan members' preferences in terms of increased contributions vs. decreased benefits, if a future valuation shows an increased shortfall.

Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These increases are required to keep pension provisions for future service at current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

10. (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

Higher	(22%)
Lower	(11%)
Same	(56%)
Don't know	(11%)

	LTIP Plan (n=21)

11. (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

Yes	(42%)
No	(42%)
Don't know	(17%)

Although all members are guaranteed pensions, the Ontario Teachers' Pension Plan, like many other pension plans, is facing funding challenges. Decisions may need to be made about whether to further increase members' contributions beyond the increases we have just discussed. The alternative to increasing contributions is reducing the level of pension provisions that will be earned from the time the change is made until members retire.

(IF RESPONDENT ASKS: By law, such changes could not affect the pensions provided to those who have already retired. Likewise, pension provisions that have already been earned by working members could not be reduced. Such changes could only be applied into the future.)

12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't Know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(14%)
10.0%	(14%)
10.1%-11.0%	(10%)
11.1%-12.0%	(10%)
12.1%-13.0%	(10%)
13.1%-14.0%	(<1%)
14.1%-15.0%	(14%)
Greater than 15.0%	(5%)
Don't know	(14%)
Refused	(10%)
Mean (%):	11.03
Median (%):	11.50
Mode (%):	10.00

	LTIP Plan (n=21)

13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12. EXCLUDE IF Q12 = "Don't know" or "Refused") If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than (INSERT RESPONSE FROM Q12) of your salary in order to keep all pension provisions at current levels?

(IF ASKED: Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These changes are required to keep the pension provisions for future service at their current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

In favour	(62%)
Not in favour	(31%)
Don't know	(8%)

Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level. Please tell me whether you would be in favour or not in favour of each of the following changes. How about: (READ - RANDOMIZE ORDER OF PROVISIONS)

(IF REQUIRED, READ: Please keep in mind that by law, these changes could not affect the pensions provided to those who have already retired. Likewise, current pension provisions that have already been earned by working members could not be reduced.)

14. Increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it. (IF ASKED: Members can currently retire with unreduced monthly pension payments when their age plus years of service equals eighty-five, or when they reach the age of 65.) (IF ASKED: Discussions would take place between the OTF and the government to decide on a transition period.)

In favour	(48%)
Not in favour	(48%)
Refused	(5%)

	LTIP Plan (n=21)

15. Reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

In favour	(19%)
Not in favour	(43%)
Don't know	(33%)
Refused	(5%)

16. Making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

In favour	(62%)
Not in favour	(29%)
Don't know	(5%)
Refused	(5%)

(END OF QUESTION RANDOMIZATION)

17. We've just discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. When I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan. (RANDOMIZE ORDER OF CHANGES)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

Decreasing your monthly pension for future service by 10%	(14%)
Increasing the eighty-five factor to a ninety factor	(33%)
Providing flexibility for the cost-of-living adjustment	(33%)
Don't know (DO NOT READ OR RANDOMIZE)	(10%)
Refused (DO NOT READ OR RANDOMIZE)	(10%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

LTIP Plan (n=21)

18. Which potential change are you least willing to have made? (REPEAT REMAINING CHANGES AS REQUIRED)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act)

Decreasing your monthly pension for future service by 10%	(53%)
Increasing the eighty-five factor to a ninety factor	(21%)
Providing flexibility to the cost-of-living adjustment	(21%)
Don't know (DO NOT READ OR RANDOMIZE)	(5%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't Know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(10%)
10.0%	(5%)
10.1%-11.0%	(14%)
11.1%-12.0%	(14%)
12.1%-13.0%	(10%)
14.1%-15.0%	(10%)
Greater than 15.0%	(10%)
Don't know	(24%)
Refused	(5%)
Mean (%):	11.51
Median (%):	12.00
Mode (%):	12.00

LTIP Plan (n=21)

D. Objective 3: To identify the views of sub-groups of members who may have different perspectives based on their circumstances.

20. (ASK IF AGE + YEARS OF CREDIT = >74) Which one of the following three statements best represents your own viewpoint: (RANDOMIZE ORDER OF STATEMENTS - REPEAT AS REQUIRED)

    If pension contributions increase to more than about eleven percent of your salary, you will consider retiring earlier than planned, even if your pension provisions remain the same ..... (21%)
    If the pension provisions you will earn in future years are reduced you will consider retiring earlier than planned, even if your contribution rates remain the same ..... (7%)
    You are unlikely to consider retiring earlier than planned as a result of changes to your future pension provisions and contribution rates. .. (36%)
    Don't know (DO NOT READ OR RANDOMIZE) ..... (21%)
    Refused (DO NOT READ OR RANDOMIZE) ..... (14%)

21. Do you work at an elementary school, a secondary school, or at another organization?

    Elementary ..... (43%)
    Secondary ..... (33%)
    Other ..... (14%)
    Refused ..... (10%)

We have come to the end of our survey. Thank you very much for your time, we appreciate your participation. (IF RESPONDENT WANTS TO LEARN MORE ABOUT THE ISSUES DISCUSSED IN THE SURVEY: Would you like me to give you some web site addresses that provide further detail on the pension plan issues discussed in this survey? (IF YES): www.otpp.com; www.otffeo.on.ca)

22. Gender (INTERVIEWER-RECORDED)

    Male ..... (29%)
    Female ..... (71%)

23. Employment type (SAMPLE)

    Full-time ..... (100%)

	LTIP Plan (n=21)
24. Employer type (SAMPLE)	
English School Board	(71%)
French School Board	(24%)
Other	(5%)
25. Years of credit (SAMPLE)	
5-9.9	(10%)
10-14.9	(14%)
15-19.9	(19%)
20-24.9	(29%)
25 And Over	(29%)
26. Career Status Grouping (SAMPLE)	
Newer members (5-9.9 years)	(5%)
Mid-career members (10-14.9 years)	(5%)
Mid-career members (15-21.9 years)	(10%)
Older members (within 10 years of an unreduced pension)	(10%)
Older members (within 5 years of an unreduced pension)	(29%)
Older members (eligible for unreduced pension)	(43%)
27. Other years of credit collapse (SAMPLE)	
7-14.9 years of actual credit	(10%)
15-21.9 years of actual credit	(10%)
Within 10 years or less of an unreduced pension	(10%)
Within 5 years of unreduced pension	(29%)
Already eligible unreduced pension	(43%)
29. Age (SAMPLE)	
Under 35 Years	(5%)
35-44	(10%)
45-54	(19%)
55-64	(62%)
65 And Over	(5%)
30. Urban/Rural (SAMPLE)	
Urban	(67%)
Rural	(33%)
31. Administration (SAMPLE)	
Non-Adminsitration	(100%)

About POLLARA

- POLLARA Inc., a leading-edge Canadian public opinion and marketing research firm, helps its clients improve their performance through strategic research designed and analyzed by consultants who are experts in their fields. Drawing on the talents of employees located in six Canadian cities, POLLARA provides a full range of research services to leading global, national and local companies and to public and non-profit sector organizations. These services include quantitative and qualitative research and counsel in the areas of public affairs/public policy, employee satisfaction, customer value/satisfaction, new product development, advertising testing and tracking, branding, and consumer demand and pricing models.

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2007 Teachers Survey.pdf

The contribution and benefit preferences of active members of the Ontario Teachers' Pension Plan

Prepared for:

OTF/FEO ONTARIO TEACHERS' PENSION PLAN Ontario

by:

POLLARA

June 2007

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I. Objectives

- The goals of this survey of active, contributing members of the Ontario Teachers' Pension Plan are:
  - → To determine the level of awareness and understanding among plan members about the current level of benefits and contributions.
  - → To measure plan members' preferences in terms of increased contributions and decreased benefits, if a future valuation shows an increased shortfall.
  - → To identify the views of sub-groups of members who may have a different perspective based on their circumstances (i.e., years from retirement).
- In order to achieve these objectives, the study required a sound research methodology that would accurately measure member preferences. This methodology is detailed in the following pages.

II. Methodology

- A total of 2,820 telephone interviews were conducted with OTPP members between April 11th and May 2nd, 2007.

A. Questionnaire development

- The survey questionnaire and methodology were developed by POLLARA in conjunction with the Ontario Teachers' Pension Plan (OTPP), the Ontario Teachers' Federation (OTF), and the Ontario Government, through a series of meetings held between September 11th and December 11th, 2006.

- In addition, six focus groups, four English (Brampton & Toronto) and two French (Ottawa), were conducted in October 2006 with early, mid, and late career members to facilitate the overall design of the questionnaire. An important goal of the focus groups was to identify pension terminology and explanations that members do or do not understand to determine the appropriate level of communication for the questionnaire. A draft copy of *Let's talk about the future of your pension*, a primer created by the OTPP, OTF, and Ontario Government, was also assessed during these sessions, and member feedback was used to refine the document in a way that would make it most easily understood.

II. Methodology, continued

A. Questionnaire development, continued

- As well, using a draft questionnaire, POLLARA conducted 17 pre-test interviews with OTPP members in November, 2006. After further questionnaire refinement, a second pre-test of 46 English and French members was conducted in March, 2007. A stratified sample was used for both pre-tests, to ensure a good mix of members. The questionnaire tested well in both cases and after each pre-test modifications were made to facilitate respondent comprehension of survey topics.

B. Member communications

- *Let's talk about the future of your pension*, a primer created by the OTPP, OTF, and Ontario Government was mailed to all pension plan members the week of March 19th, 2007. The primer informed members that they may be called to participate in a survey and encouraged them to familiarize themselves with the document and to keep it available for reference in case they were contacted. The resource was also included on OTPP's website.

- In addition to the primer, in December, 2006, the Ontario Teachers' Federation released, *What About My Teachers' Pension?*, a multi-media educational resource that was sent to local presidents for distribution to schools. The resource was also included on OTF's website, and was included as a link on OTPP's website.

II. Methodology, continued

B. Member communications, continued

- Members were also informed about the survey through OTPP's 2006 Annual Report, its 2006 Report to Members, its 2007 Annual Meeting, detailed Q&As on its website, and its Pensionwise newsletter.

C. Interviewing

- Pension plan members were telephoned by POLLARA weekdays between 5 p.m. and 9 p.m. and on Saturday between 9 a.m. and 5 p.m. If the time of the initial call was deemed inconvenient or if members wanted additional time to review reference material on the survey topics, the researcher offered to schedule an appointment to call back.
- Of the 3,636 eligible members POLLARA spoke with, 78% completed the survey and 22% declined to participate. The survey response rate, calculated according to the Marketing Research and Intelligence Association (MRIA) formula, was 40%.
- All interviewers were briefed on the project's background and questionnaire. 100% of interviews were supervised, and 10% were monitored, as per MRIA guidelines.

II. Methodology, continued

D. Sampling and data weighting

- The source of the survey sample was OTPP current member records.
- Additional interviews were conducted among member sub-groups in order to accurately understand the views of these segments. Specific groups to be oversampled were selected in consultation with POLLARA, by OTPP, OTF, and the Ontario Government.
- The overall results of the survey were weighted to reflect the actual distribution of members within these sub-groups.

POLLARA

II. Methodology, continued

D. Sampling and data weighting, continued

- The following table shows the distribution of interviews and the corresponding margins of error. Overall results are accurate to within ±1.8%, nineteen times out of twenty. Sub-sample results have a larger margin of error.

		Actual # of interviews	Weighted # of interviews	Margin of error (%)
Career groupings	Newer members (0 – 4.9 years credit)	481	255	±4.4
	Newer members (5 – 9.9 years credit)	398	259	±4.9
	Mid-career members (10 – 14.9 years credit)	361	120	±5.1
	Mid-career members (15 – 21.9 years credit)	353	65	±5.1
	Older members (within 10 years of an unreduced pension)	431	137	±4.7
	Older members (within 5 years of an unreduced pension)	392	117	±4..9
	Older members (eligible for unreduced pension)	404	47	±4.7
Gender	Female	2077	736	±2.1
	Male	743	264	±3.6
Employment type	Full-time	2082	829	±2.1
	Part-time	354	73	±5.1
	Occasional	384	98	±4.9
Employer type	District school board – English	2345	938	±2.0
	District school board – French	429	48	±4.6
	Other	46	14	±14.3
TOTAL		**2,820***	**1,000***	**±1.8**

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*Sub-group interviews do not add up to the total due to overlap.

III. Key findings

Key findings

In summary, the study indicates that members would be willing to contribute an average maximum of 12.3% in order to preserve their current level of benefits. This amount is 1.3 percentage points above the increase scheduled to take effect in 2009 that will bring contributions to an average of 11%. Six-in-ten members say they would be willing to contribute *more* than 11% of their before-tax income to preserve their current level of benefits, while 27% would be willing to contribute *up to* 11%. If members were contributing their maximum, the benefit change they would be most willing to support is making cost-of-living increases to future retirees' pensions flexible (supported by 51%). They would be least supportive of reducing monthly pension for future service by about 10% (supported by 32%).

A. Awareness of current level of benefits and contributions

- Overall, the majority of pension plan members have a high level of aided awareness of all pension plan provisions and issues tested in this study. Almost all are aware of the 85 factor and that their monthly pension amount is based on a formula. Another three-quarters are aware of the inflation protection provision. Of the other pension plan issues tested, the majority of members are aware of the lack of dental and health coverage, tax deductibility of contributions, and government matching of pension plan contributions.
  - → Awareness is widespread among all career groupings. Understandably, newer members are less aware of all provisions/issues than those approaching retirement.

Key findings, continued

- Almost two-fifths of members say that the $750,000 value of the average teacher's pension at retirement, in today's dollars, is about the same as they expected. Almost one-quarter say that this amount is more than they expected, and one-in-ten report that they thought the value was higher than $750,000. Three-in-ten are unsure.
  - → Almost two-fifths of members in all career groupings report that this amount is about what they expected.
- Members' awareness of the amount they currently contribute to their pension plan is not very widespread. Specifically, only one-quarter of members correctly name 9% to 11.9% as the amount of their before-tax salary they contribute to the pension plan. In addition, more than one-third of all members say they do not know how much they contribute.
  - → Interestingly, members who are already eligible for retirement are as likely as newer members to say they don't know how much they contribute to their pension plan.
- Awareness of scheduled contribution increases is widespread, with over three-quarters of members understanding that their contributions will increase over the next two years.
  - → Newer members are least likely to be aware of these increases, whereas members already eligible for unreduced pension are most likely to be aware.
- When scheduled contribution increases are outlined for members who expect an increase, almost two-thirds see the amounts as in line with their expectations, whereas, about a quarter feel they are higher than expected. Only 3% say that the increases are less than expected.

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Key findings, continued

- When prompted, half of those who had *not* expected a contribution increase recall hearing or seeing information about the change.

B. Preferences in terms of increased contributions and decreased benefits

Increased contributions

- If a future valuation shows an increased shortfall, pension plan members would be willing to contribute a maximum of 12.3% in order to maintain current pension provisions. Six-in-ten members are willing to have contributions *exceed* 11%, while 27% are willing to contribute *up to* 11%.
  - → Average maximum pension plan contributions are very consistent across career groupings, ranging from 11.9% to 12.8%.
  - → Part-time workers (13.0%) are willing to contribute the most in order to maintain their current pension provisions, whereas French school board members are willing to contribute slightly less (10.7%) than average.

Key findings, continued

- Members whose maximum contribution is 8.1% or higher were asked if they would be willing to contribute more than their maximum if a commitment was made to reduce contributions to eight percent if the pension plan shows a surplus in future. More than half do not support such a move. However, over one-third of members would increase their maximum contribution under this circumstance.
- After three potential benefit changes are reviewed with members, the average maximum contribution increases by 0.3 (to total 12.6%) and the proportion of members willing to contribute more than 11% increases by seven percentage points (to total 67%). Average maximum pension plan contributions are again very consistent across career groupings (12.1% to 13.0%).

Decreased benefits

- Respondents were asked to imagine that their contributions are at the maximum amount they would be willing to contribute in order to keep all pension provisions at current levels. They were then read a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level.

Key findings, continued

- The most popular option is making cost-of-living adjustments flexible, which is supported by more than one-half of pension plan members.
  - → Newer members are more likely than older members to be in favour of this choice. Occasional workers and French school board members are also more likely to favour this option.
- Two-fifths of all members are in favour of increasing the 85 factor to 90.
  - → Unlike the cost-of-living option, those already eligible for an unreduced pension are more likely to be in favour of this plan than newer members.
- One-third of plan members are in favour of reducing monthly pension for future service by about 10%.
  - → Newer members are more likely to be in favour of this option than older members, as are occasional workers, and French school board members.
- When asked to identify the one potential benefit change they prefer, the most popular response (provided by more than two-fifths) is making cost-of-living adjustment flexible.
  - → This is the preferred option for five of seven career groupings and rural residents.
- The second most preferred benefit change is increasing the 85 factor to 90, chosen by almost four-in-ten members.
  - → Only members within five years of unreduced pension and those already eligible for unreduced pension name this change as their top option.

Key findings, continued

- Reducing monthly pension for future service by 10% is preferred by just over one-in-ten members, ranking this option third.
  - → Preference for this option is consistently low among all career groupings, with no more than 13% naming this change as their preferred option.
- When members are asked for their least preferred option amongst all three, increasing the 85 factor to 90 comes out on top, with two-fifths saying is it the least desirable option.
  - → This option is the least favourite choice for five of the seven career groupings.
  - → Reducing monthly pension for future service by 10% ranks as the second least preferred option overall (chosen by 37%). This is the number one least preferred option among members within five years of unreduced pension and those already eligible to retire.
  - → Less than one-fifth of members rank flexible cost-of-living adjustments as their third least preferred option. Only those already eligible for unreduced pension rank this option as their second least preferred option.

All of the findings in this summary are analyzed in greater detail within the remaining sections of this report.

IV. Level of awareness and understanding among plan members about the current level of benefits and contributions

Awareness and understanding of pension plan benefits and contributions

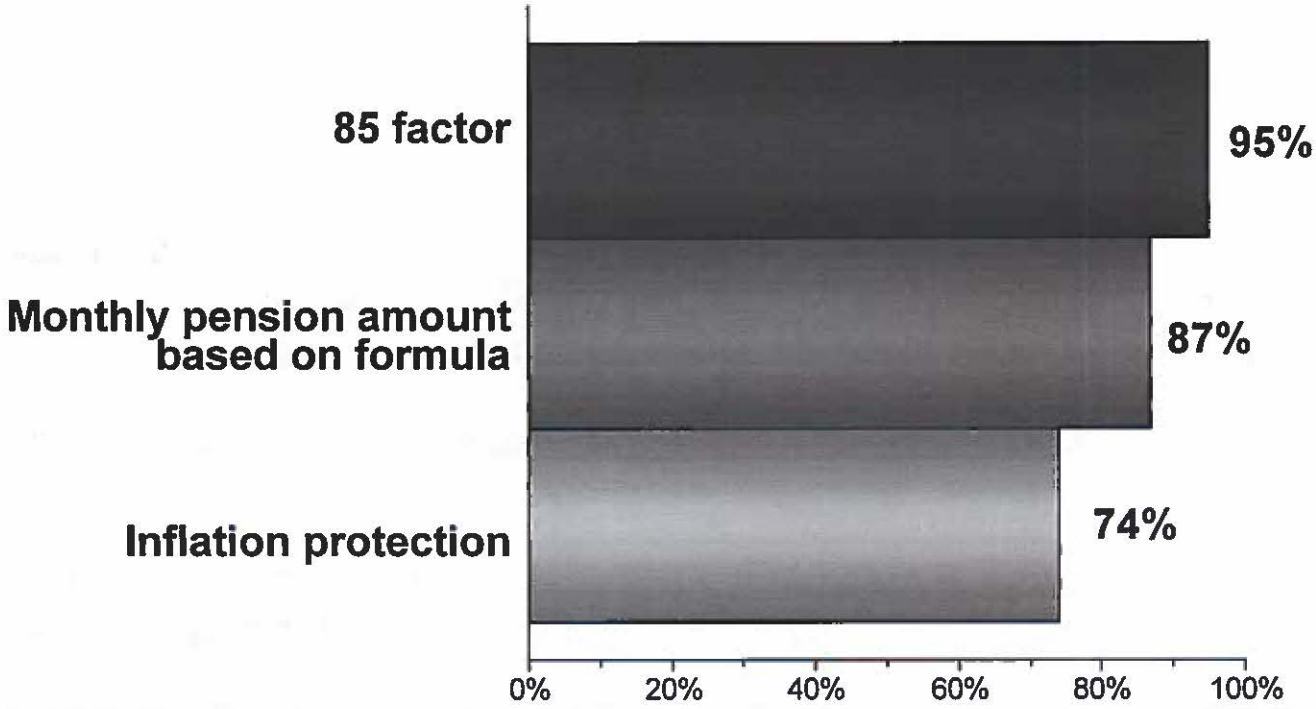
- Prior to delving into pension plan members' preferences in terms of contributions and benefits, a number of questions were asked of members at the onset of the questionnaire, the goals of which were:

  → To understand members' aided awareness of their pension provisions.

  → To ensure that survey respondents were aware of current provisions before they answered more detailed questions concerning their benefit and contribution preferences.

Majority of pension plan members aware of each current pension plan provision tested

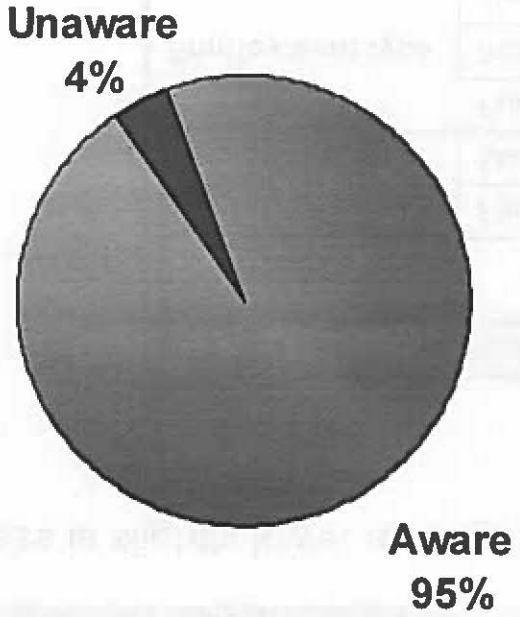
- Of the three pension plan provisions tested, members are most likely to be aware of the 85 factor, followed by the use of a formula to determine the amount of their pension, and inflation protection.



Qs 1-3. To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF PROVISIONS)

Almost all pension plan members aware of 85 factor

- Almost all pension plan members (95%) are aware that they can retire with unreduced monthly pension payments when their age plus number of teaching years equals 85, or when they reach the age of 65.
- Awareness is slightly lower among newer members (90%) and close to unanimous among older members, those within 10 years of unreduced pension eligibility, and those already eligible for unreduced pension.



Career groupings	Aware (%)
Newer members (0 – 4.9)	90%
Newer members (5 – 9.9)	95%
Mid-career members (10 – 14.9)	98%
Mid-career members (15 – 21.9)	99%
Older members (within 10 yrs unreduced pension)	98%
Older members (within 5 yrs unreduced pension)	99%
Older members (eligible for unreduced pension)	99%

Q1. Please tell me whether or not you were aware of each provision prior to my call. How about: members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65.

POLLARA

Large majorities of all member segments aware of 85 factor

- Awareness is slightly lower among occasionally employed pension plan members (85%).

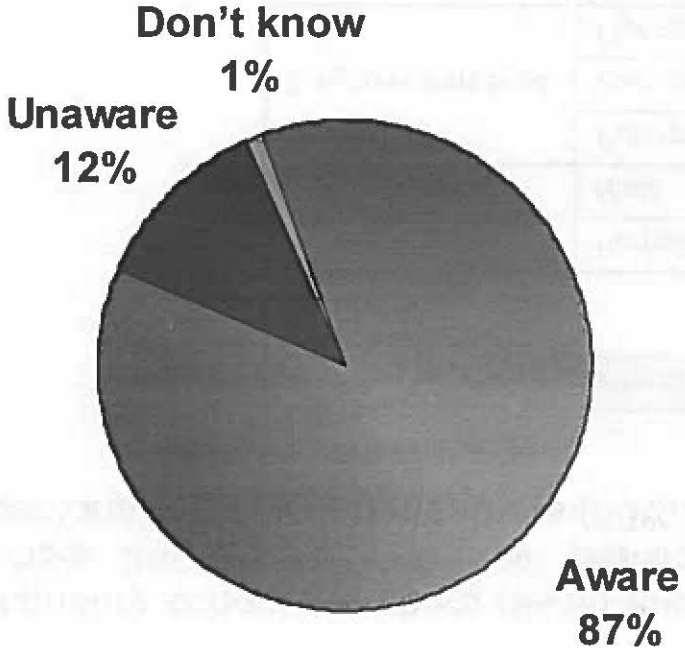
Member segment		Aware (%)
OVERALL		95%
Gender	Female	96%
	Male	95%
Employment type	Full-time	97%
	Part-time	95%
	Occasional	85%
Employer type	District school board – English	96%
	District school board – French	92%
Place of work	Elementary	95%
	Secondary	96%
Urban/Rural	Urban	95%
	Rural	97%

Less likely

POLLARA

Large majority of pension plan members aware of how their monthly pension is determined

- Almost nine-in-ten pension plan members (87%) are aware that their basic annual pension is determined through a formula.
- Awareness increases as members approach retirement, with almost three-quarters (71%) of newer members (0-4.9 years) to almost all (99%) unreduced pension eligible members being aware.



Career groupings	Aware (%)
Newer members (0 – 4.9)	71%
Newer members (5 – 9.9)	89%
Mid-career members (10 – 14.9)	93%
Mid-career members (15 – 21.9)	94%
Older members (within 10 yrs unreduced pension)	96%
Older members (within 5 yrs unreduced pension)	95%
Older members (eligible for unreduced pension)	99%

POLLARA

Q2. Please tell me whether or not you were aware of each provision prior to my call. How about: the monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries.

Awareness that pension amount based on formula widespread among all member segments

- Secondary school members (94%) and men (93%) are slightly more aware than average of how the amount of their pension is determined. Awareness is lowest among occasionally employed members (66%).

Member segment		Aware (%)
OVERALL		87%
Gender	Female	85%
	Male	93%
Employment type	Full-time	90%
	Part-time	84%
	Occasional	66%
Employer type	District school board – English	87%
	District school board – French	83%
Place of work	Elementary	84%
	Secondary	94%
Urban/Rural	Urban	87%
	Rural	91%

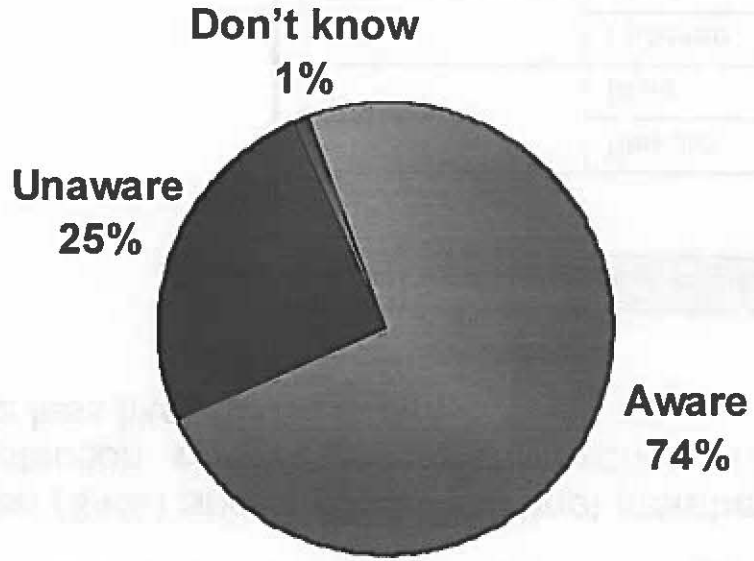
More likely

Less likely

POLLARA

Almost three-quarters of pension plan members aware that monthly payments are protected against inflation

- Almost three-quarters of pension plan members (74%) are aware that monthly pension payments are protected against inflation.
- Again, awareness is higher among members approaching retirement. Just over half (52%) of newer members (0-4.9 years of credit) are aware of inflation protection, compared to 85% of mid-career members (15-21.9 years). Unreduced pension eligible members are almost unanimously aware that a guaranteed cost-of-living adjustment is made (97%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	52%
Newer members (5 – 9.9)	68%
Mid-career members (10 – 14.9)	80%
Mid-career members (15 – 21.9)	85%
Older members (within 10yrs unreduced pension)	92%
Older members (within 5 yrs unreduced pension)	93%
Older members (eligible for unreduced pension)	97%

POLLARA

Q3. Please tell me whether or not you were aware of each provision prior to my call. How about: The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made.

Inflation protection awareness widespread among most member segments

- Men (84%) and secondary school members (81%) are more likely to be aware of inflation protection, whereas occasional workers (55%) and French school board members (61%) are less likely to be aware.

Member segment		Aware (%)
OVERALL		74%
Gender	Female	70%
	Male	84%
Employment type	Full-time	76%
	Part-time	71%
	Occasional	55%
Employer type	District school board – English	75%
	District school board – French	61%
Place of work	Elementary	70%
	Secondary	81%
Urban/Rural	Urban	73%
	Rural	78%

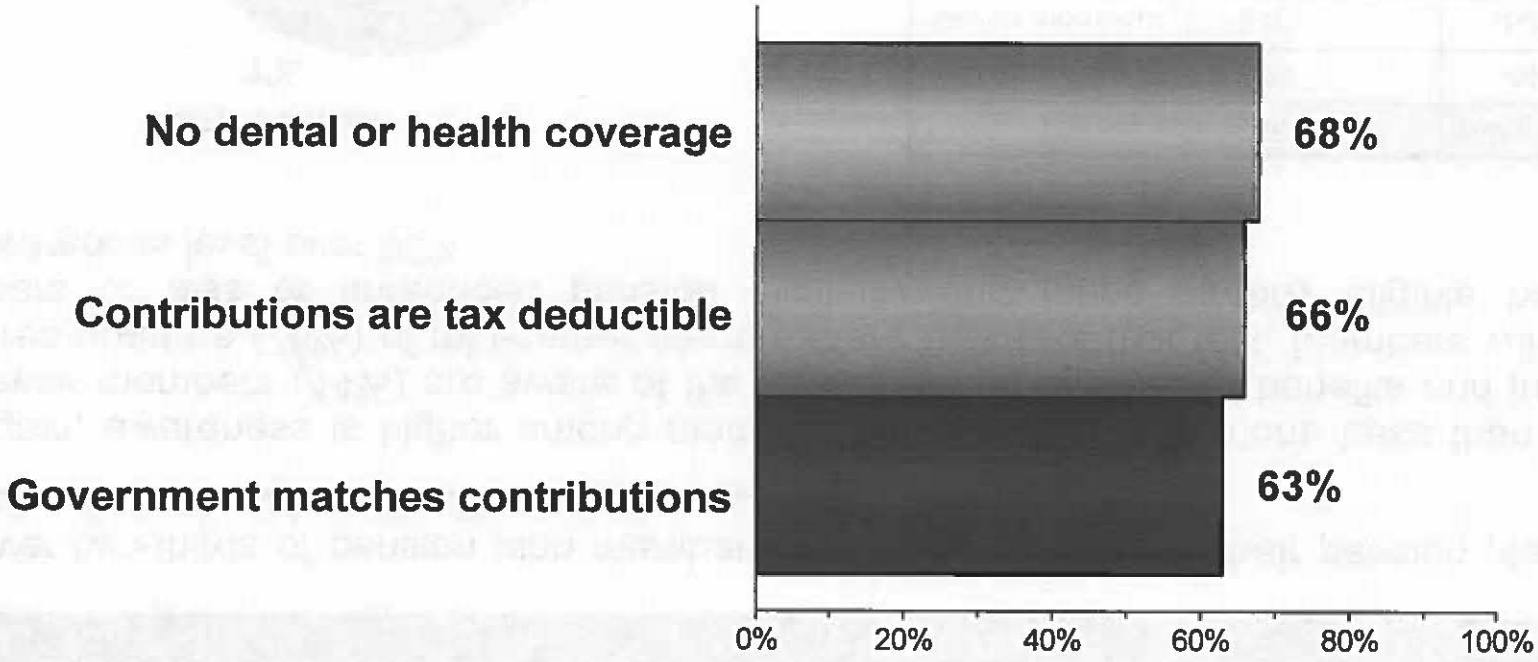
More likely

Less likely

POLLARA

Majority of pension plan members are aware of other aspects of their pension plan

- In addition to testing awareness of plan provisions, members' aided awareness of three other aspects of their plan were explored.
- More than six-in-ten members are aware of the lack of dental and health coverage in the plan, followed by the tax deductibility of their contributions, and contribution matching by the Ontario government.

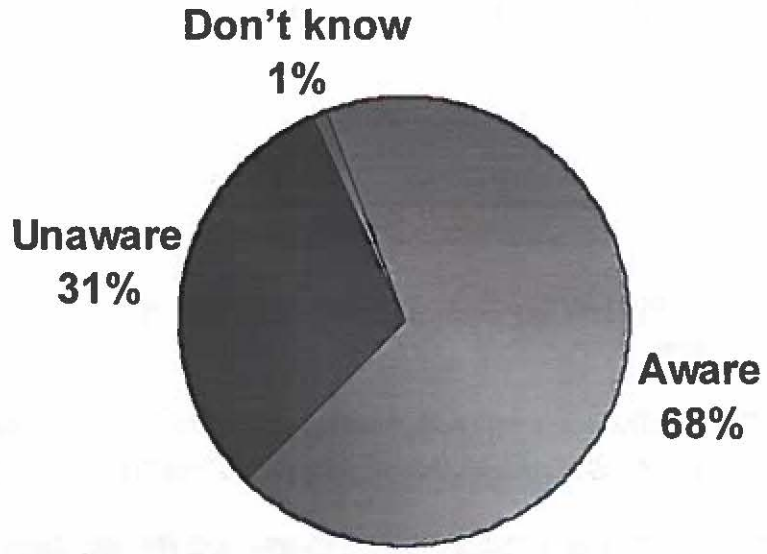


POLLARA

Qs 4-6. Now I'd like to ask you about some other pension issues. Prior to my call, were you aware or unaware…

More than two-thirds of members aware that pension plan does not provide dental and health benefit coverage

- Over two-thirds of pension plan members (68%) are aware that their pension plan does not include dental and health benefit coverage.
- Again, awareness is higher among members approaching retirement. Less than half of newer members (44%) are aware of the lack of dental and health benefits and just over three-quarters (76%) of mid-career members are aware of that fact. Members within five years or less of unreduced pension eligibility and those already eligible have an awareness level over 90%.



Career groupings	Aware (%)
Newer members (0 – 4.9)	44%
Newer members (5 – 9.9)	62%
Mid-career members (10 – 14.9)	75%
Mid-career members (15 – 21.9)	76%
Older members (within 10 yrs unreduced pension)	82%
Older members (within 5 yrs unreduced pension)	92%
Older members (eligible for unreduced pension)	98%

Q4. Prior to my call, were you aware or unaware that the pension plan <u>does not</u> provide dental and other health benefit coverage to retirees?

POLLARA

Majority of all member segments aware of lack of dental and health benefits

- Occasional workers (52%), French school board members (56%), and part-time workers (60%) are less likely to be aware that their pension plan lacks dental and health coverage.

Member segment		Aware (%)
OVERALL		68%
Gender	Female	68%
	Male	69%
Employment type	Full-time	71%
	Part-time	60%
	Occasional	52%
Employer type	District school board – English	69%
	District school board – French	56%
Place of work	Elementary	67%
	Secondary	71%
Urban/Rural	Urban	68%
	Rural	68%

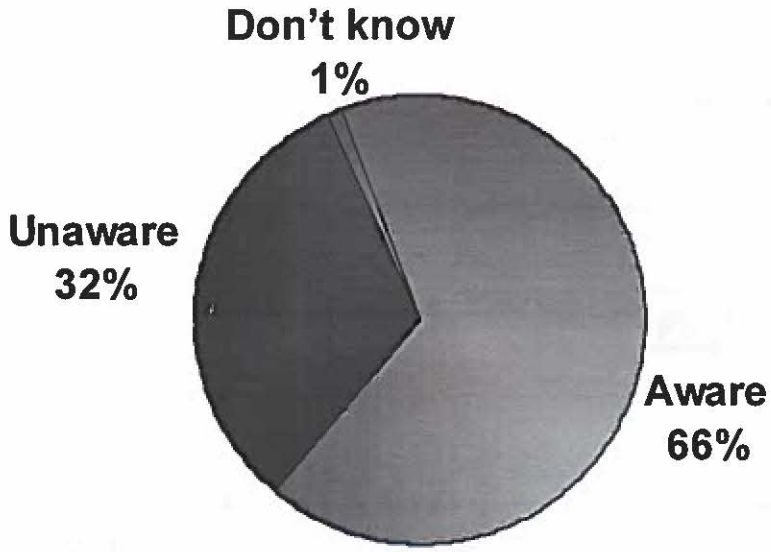
More likely

Less likely

POLLARA

Two-thirds of pension plan members aware that money contributed to pension plan is tax deductible

- Two-thirds of pension plan members (66%) are aware that their pension plan contributions are tax deductible.
- Newer members, once again, are least aware (55%), whereas members already eligible for unreduced pension score the highest (81%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	55%
Newer members (5 – 9.9)	65%
Mid-career members (10 – 14.9)	71%
Mid-career members (15 – 21.9)	76%
Older members (within 10 yrs unreduced pension)	73%
Older members (within 5 yrs unreduced pension)	71%
Older members (eligible for unreduced pension)	81%

Q6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible?

POLLARA

Majority of all member segments aware of tax deductibility of contributions

- Awareness of tax deductibility is higher among men (73%) and secondary school workers (73%), and lower among occasional workers (56%) and French school board members (59%).

Member segment		Aware (%)
OVERALL		66%
Gender	Female	64%
	Male	73%
Employment type	Full-time	68%
	Part-time	64%
	Occasional	56%
Employer type	District school board – English	66%
	District school board – French	59%
Place of work	Elementary	63%
	Secondary	73%
Urban/Rural	Urban	66%
	Rural	66%

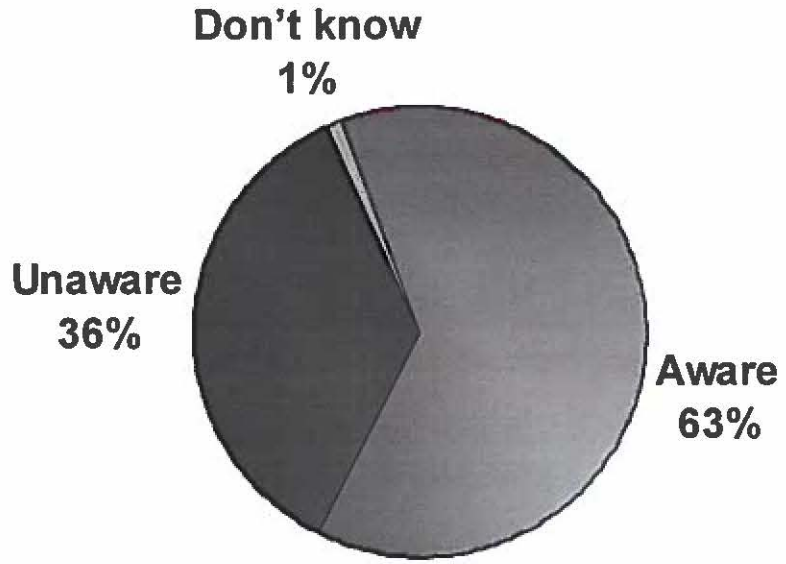
More likely

Less likely

POLLARA

Majority of pension plan members aware that the Ontario government matches members' contributions to the pension plan

- Almost two-thirds of pension plan members (63%) are aware that the Ontario government matches members' contributions to their pension plan.
- Again, awareness is lowest among newer members (45%) and highest among those who are eligible for an unreduced pension (81%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	45%
Newer members (5 – 9.9)	60%
Mid-career members (10 – 14.9)	70%
Mid-career members (15 – 21.9)	78%
Older members (within 10 yrs unreduced pension)	73%
Older members (within 5 yrs unreduced pension)	78%
Older members (eligible for unreduced pension)	81%

Q5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?

POLLARA

Majority of most member segments aware government matches contributions

- Men (77%) and secondary school members (73%) are more likely to be aware of contribution matching. French school board members (41%), occasional (44%) and part-time (53%) workers, women (58%), and elementary school members (58%) are all less likely to be aware of contribution matching.

Member segment		Aware (%)
OVERALL		63%
Gender	Female	58%
	Male	77%
Employment type	Full-time	66%
	Part-time	53%
	Occasional	44%
Employer type	District school board – English	65%
	District school board – French	41%
Place of work	Elementary	58%
	Secondary	73%
Urban/Rural	Urban	63%
	Rural	67%

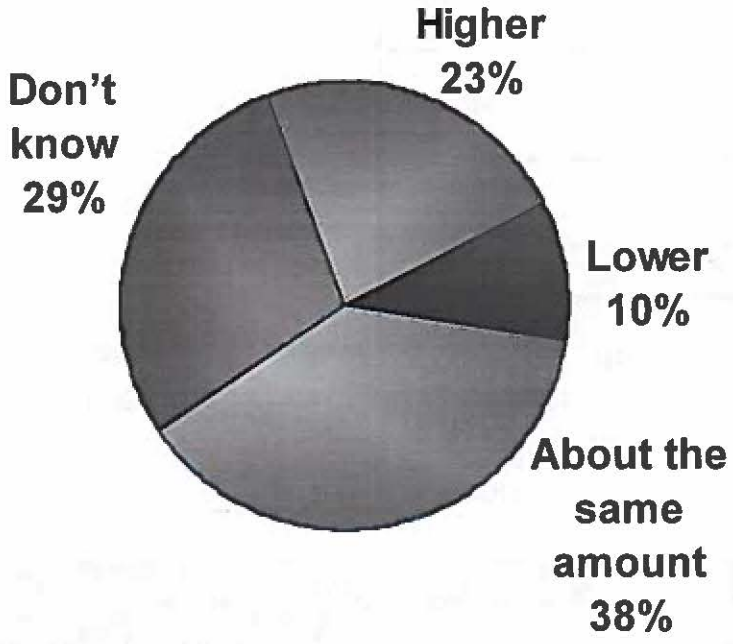
More likely

Less likely

POLLARA

More than six-in-ten members expect the value of the average teacher's pension to be $750,000 or less

- Members were told that the average teacher's pension at retirement, in today's dollars, is valued at $750,000. Almost two-fifths (38%) of pension plan members say this is about what they expected, whereas, 23% think it is higher than expected. Only one-in-ten (10%) say it is lower than expected and almost three-in-ten (29%) don't know.
- Expectations are very consistent between career groups. Between 21% and 24% of each group say the $750,000 is higher than expected, 9%-15% say lower, and 36%-42% say about the same as expected.



Career groupings	Higher (%)	Lower (%)	Same (%)	DK (%)
Newer members (0 – 4.9)	24%	9%	36%	31%
Newer members (5 – 9.9)	22%	9%	39%	29%
Mid-career members (10 – 14.9)	24%	9%	38%	30%
Mid-career members (15 – 21.9)	21%	10%	41%	28%
Older members (within 10 yrs unreduced pension)	21%	15%	37%	28%
Older members (within 5 yrs unreduced pension)	22%	8%	42%	28%
Older members (eligible for unreduced pension)	22%	9%	40%	29%

POLLARA

Q7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?

Majority of all member segments say pension value same or higher than they expected

- Part-time (30%) and occasional (31%) workers are more likely than average to say that the $750,000 value of the average teachers' pension is higher than they expected. Men (47%) are more likely to say that $750,000 is about the same as expected.

Member segment		Higher	Lower	Same	DK
OVERALL		23%	10%	38%	29%
Gender	Female	25%	8%	35%	32%
	Male	16%	13%	47%	23%
Employment type	Full-time	21%	10%	40%	29%
	Part-time	30%	5%	30%	34%
	Occasional	31%	11%	30%	28%
Employer type	District school board – English	23%	9%	39%	29%
	District school board – French	19%	12%	35%	35%
Place of work	Elementary	25%	9%	36%	30%
	Secondary	19%	10%	41%	29%
Urban/Rural	Urban	23%	9%	38%	29%
	Rural	20%	13%	37%	30%

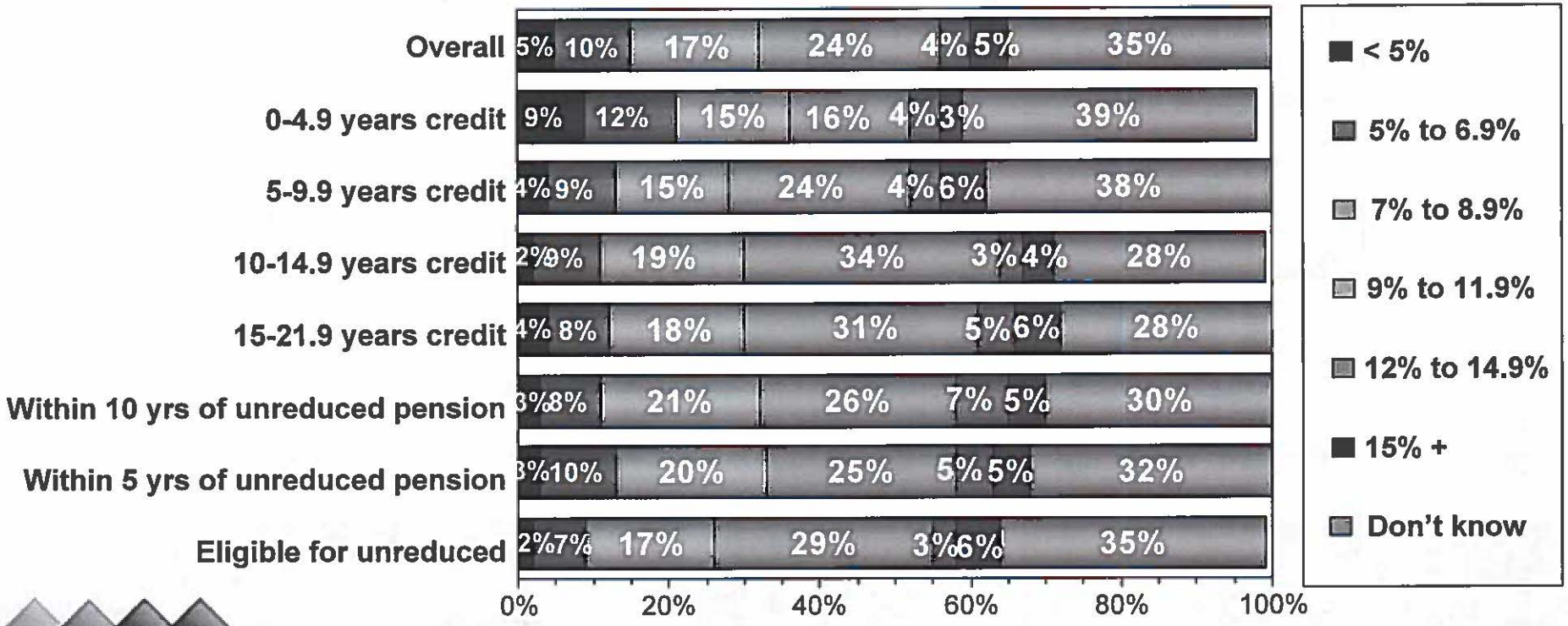
More likely

Less likely

POLLARA

Almost one-quarter of members believe they contribute 9% to less than 12% of their before-tax salary to their pension plan

- Almost one-quarter (24%) of members correctly believe that they contribute 9% to less than 12% of their before-tax salary to their pension plan. Over one-third (35%) do not know how much they are contributing.
- Interestingly, members who are already eligible for an unreduced pension (35%) are almost as likely to say they don't know how much they contribute to their pension plan as newer members (39%). However, newer members are less likely to have chosen the correct percentage range (16% vs. 29%) than their older counterparts.



Q8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan?

Men more likely then women to know their contribution amounts

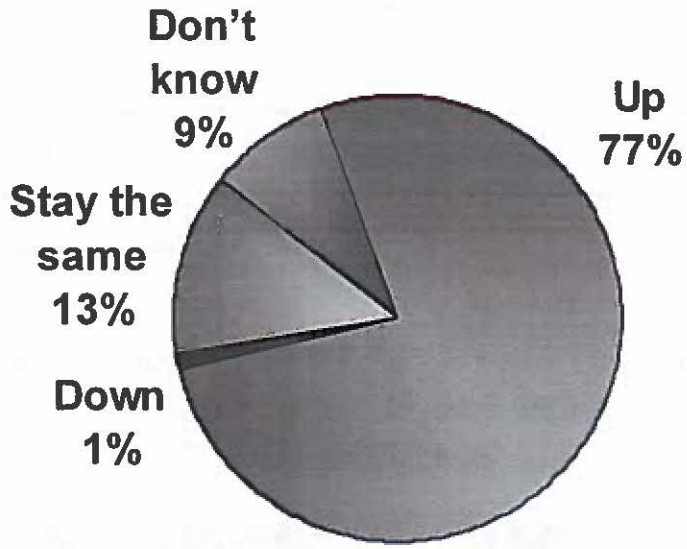
- Men (32%) are more likely than women (21%) to be aware of current contribution levels. An additional 40% of women say they do not know how much they contribute, while occasional workers (43%) are most likely to provide this response.

Member segment		<5%	5-6.9%	7-8.9%	9-11.9%	12-14.9%	15%+	DK
OVERALL		5%	10%	17%	24%	4%	5%	35%
Gender	Female	5%	9%	15%	21%	4%	5%	40%
	Male	5%	11%	23%	32%	5%	3%	21%
Employment type	Full-time	4%	9%	18%	25%	5%	5%	33%
	Part-time	4%	10%	17%	23%	3%	4%	39%
	Occasional	12%	12%	15%	14%	3%	1%	43%
Employer type	District school board – English	5%	10%	17%	25%	4%	5%	35%
	District school board – French	5%	13%	19%	19%	6%	4%	32%
Place of work	Elementary	5%	10%	16%	20%	4%	5%	39%
	Secondary	4%	9%	20%	32%	5%	4%	26%

More likely Less likely

More than three-quarters of members understand that pension plan contributions are scheduled to increase over the next two years

- Three-quarters (77%) of pension plan members understand that contributions are scheduled to increase over the next two years. Only 1% believe that contributions are scheduled to decrease, and another 13% believe they will stay the same. One-in-ten (9%) do not know.
- Newer members (69%) are least likely to know that contributions are scheduled to increase. Members already eligible for unreduced pension are most likely to know that contributions are increasing (85%).



Career groupings	Up (%)	Down (%)	Same (%)
Newer members (0 – 4.9)	69%	1%	16%
Newer members (5 – 9.9)	77%	2%	13%
Mid-career members (10 – 14.9)	80%	1%	13%
Mid-career members (15 – 21.9)	82%	<1%	11%
Older members (within 10 yrs unreduced pension)	81%	<1%	10%
Older members (within 5 yrs unreduced pension)	77%	2%	14%
Older members (eligible for unreduced pension)	85%	1%	9%

Q9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

POLLARA

Majority of every member segment believes contributions scheduled to increase

- Occasional and part-time workers are less likely than average to believe that contributions are scheduled to increase (59% and 72%) over the next two years and occasional workers are also more likely to say they don't know (21%).

Member segment		Up (%)	Down (%)	Same (%)	DK (%)
OVERALL		77%	1%	13%	9%
Gender	Female	76%	1%	13%	9%
	Male	78%	1%	13%	8%
Employment type	Full-time	79%	1%	12%	7%
	Part-time	72%	1%	14%	13%
	Occasional	59%	1%	19%	21%
Employer type	District school board – English	77%	1%	13%	9%
	District school board – French	74%	2%	21%	4%
Place of work	Elementary	76%	1%	13%	10%
	Secondary	78%	1%	14%	7%
Urban/Rural	Urban	76%	1%	13%	10%
	Rural	79%	2%	13%	6%

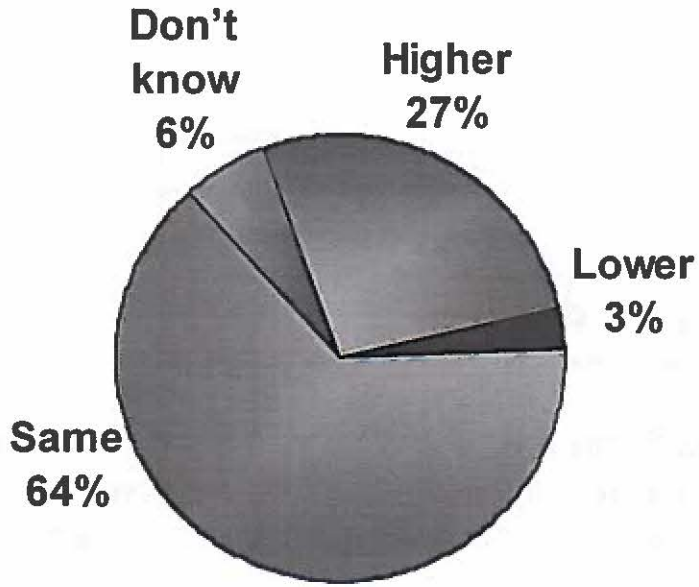
More likely

Less likely

POLLARA

Scheduled contribution increases are in line with expectations of the majority of members who are expecting an increase

- Among the 77% of members who expect an increase, almost two-thirds (64%) say the amount of future increases is what they expected. A further 27% feel that the future increases are higher than expected and only 3% expected smaller increases in the next two years.
- In most cases about two-thirds of members in each career grouping feel that the future increases are as they expected.



Career groupings	Higher (%)	Lower (%)	Same (%)	DK (%)
Newer members (0 – 4.9)	26%	3%	64%	8%
Newer members (5 – 9.9)	29%	4%	59%	8%
Mid-career members (10 – 14.9)	29%	1%	66%	4%
Mid-career members (15 – 21.9)	24%	3%	70%	4%
Older members (within 10 yrs unreduced pension)	23%	4%	67%	5%
Older members (within 5 yrs unreduced pension)	27%	3%	62%	7%
Older members (eligible for unreduced pension)	26%	3%	67%	4%

Q10. Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate… (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

POLLARA

Majority of all member segments say amount of scheduled increases is same as expected

- Rural residents (70%) are most likely to report that the proposed increases are as expected.

Member segment		Higher (%)	Lower (%)	Same (%)
OVERALL		27%	3%	64%
Gender	Female	27%	3%	63%
	Male	27%	4%	66%
Employment type	Full-time	27%	3%	63%
	Part-time	22%	5%	66%
	Occasional	23%	2%	66%
Employer type	District school board – English	27%	3%	64%
	District school board – French	24%	6%	63%
Place of work	Elementary	26%	3%	63%
	Secondary	27%	3%	66%
Urban/Rural	Urban	28%	3%	63%
	Rural	20%	3%	70%

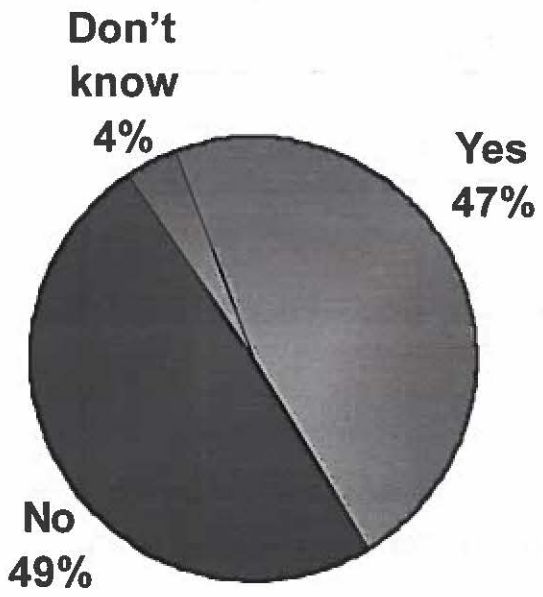
More likely

Less likely

POLLARA

Of those who do not expect contributions to increase, almost half recall seeing or hearing about increases when prompted

- Among the 23% of members who believe that contributions are going down (1%), staying the same (13%), or who are unsure (9%), almost one-half (47%) remember hearing or seeing about contribution increases, when prompted.
- Less than two-in-five newer members (38%) recall seeing or hearing such information, whereas, two-thirds (67%) of those approaching unreduced pension eligibility or those already eligible (67%) recall hearing or seeing about contribution increases.



Career groupings	Yes (%)
Newer members (0 – 4.9)	38%
Newer members (5 – 9.9)	38%
Mid-career members (10 – 14.9)	53%
Mid-career members (15 – 21.9)	57%
Older members (within 10 yrs unreduced pension)	58%
Older members (within 5 yrs unreduced pension)	67%
Older members (eligible for unreduced pension)	67%

Q11. Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate… (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

POLLARA

French school board members and men are more likely to recall seeing or hearing about increases

- Of those who do not expect contributions to increase, French school board members (58%), men (52%), and rural members (52%) are all more likely to recall hearing or seeing information about contribution increases, when prompted. Occasional workers (35%) are less likely.

Member segment		'Yes' (%)
OVERALL		47%
Gender	Female	45%
	Male	52%
Employment type	Full-time	50%
	Part-time	44%
	Occasional	35%
Employer type	District school board – English	47%
	District school board – French	58%
Place of work	Elementary	45%
	Secondary	51%
Urban/Rural	Urban	46%
	Rural	52%

More likely

Less likely

POLLARA

V. Pension plan members' preferences in terms of increased contributions and decreased benefits, if a future valuation shows an increased shortfall

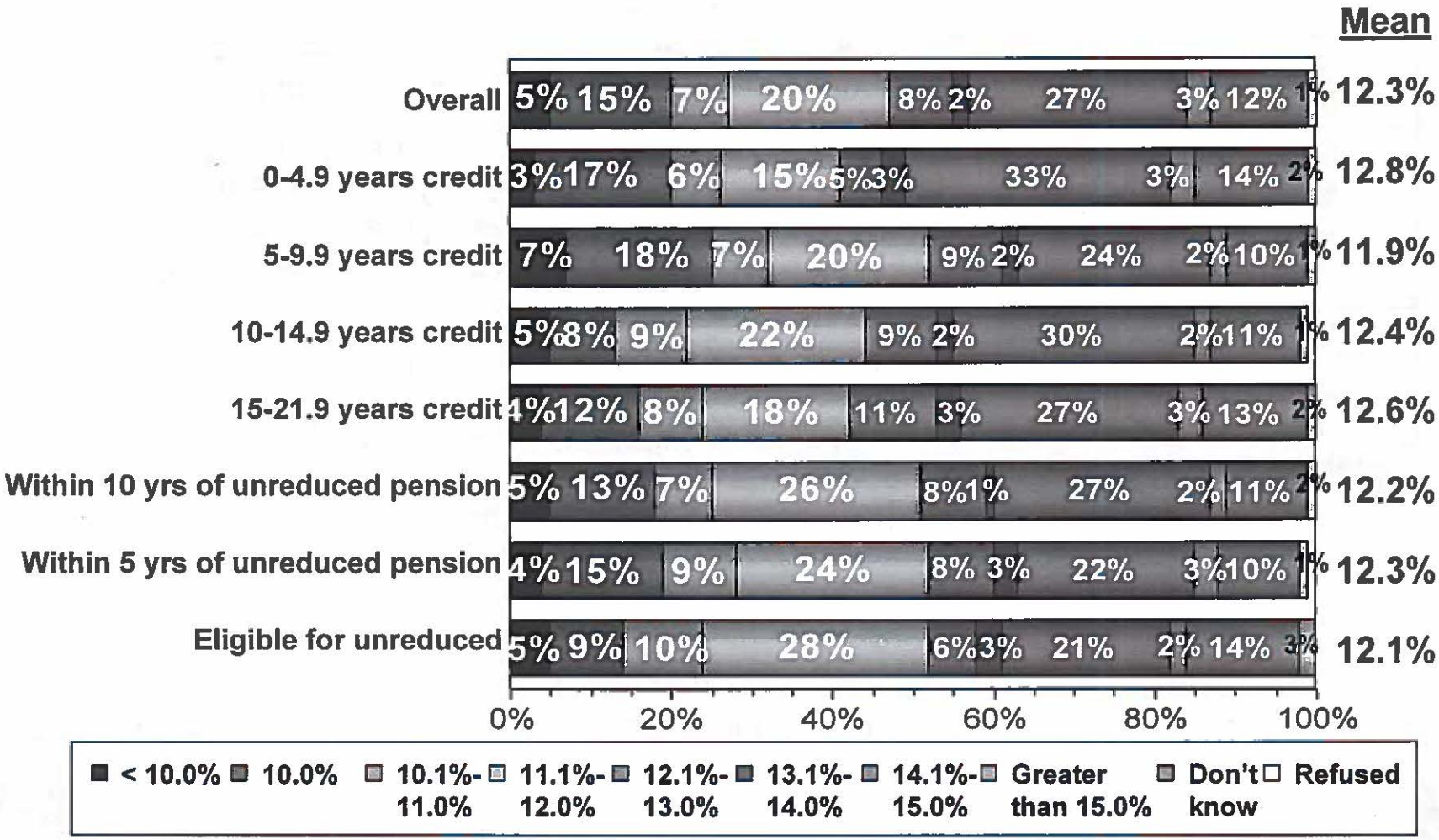
Members willing to contribute average maximum of 12.3% to maintain current pension provisions

- Prior to reviewing potential benefit changes, members were asked to identify the maximum contribution they would be willing to make in order to maintain current pension provisions.
  - → Members are willing to contribute an average (mean) maximum of 12.3% in order to maintain current pension provisions. Six-in-ten (60%) members are willing to have contributions exceed 11%, while more than one-quarter (27%) are willing to contribute up to 11%. The median for this result is 12%.
  - → Interestingly, maximum contribution rates are similar across career groupings (mean of 11.9%-12.8%), as detailed on the next page.
  - → Members were asked the same question after reviewing potential benefit changes and their mean response was 0.3 points higher (12.6%). This result is discussed in greater detail on page 58.

Contribution	Members (%)
Less than 10.0%	5%
10.0%	15%
10.1%-11.0%	7%
11.1%-12.0%	20%
12.1%-13.0%	8%
13.1%-14.0%	2%
14.1%-15.0%	27%
Greater than 15.0%	3%
Don't know	12%

POLLARA

Average maximum contribution, in order to maintain current pension provisions, is remarkably similar across career groupings



Q12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

Maximum contributions fairly consistent among all member segments

- Part-time workers (13%) have a slightly higher average maximum contribution rate, whereas French school board members are willing to contribute slightly less than average (10.7%).

Member segment		Mean
OVERALL		12.3%
Gender	Female	12.4%
	Male	12.2%
Employment type	Full-time	12.3%
	Part-time	13.0%
	Occasional	12.6%
Employer type	District school board – English	12.4%
	District school board – French	10.7%
Place of work	Elementary	12.4%
	Secondary	12.2%
Urban/Rural	Urban	12.3%
	Rural	12.6%

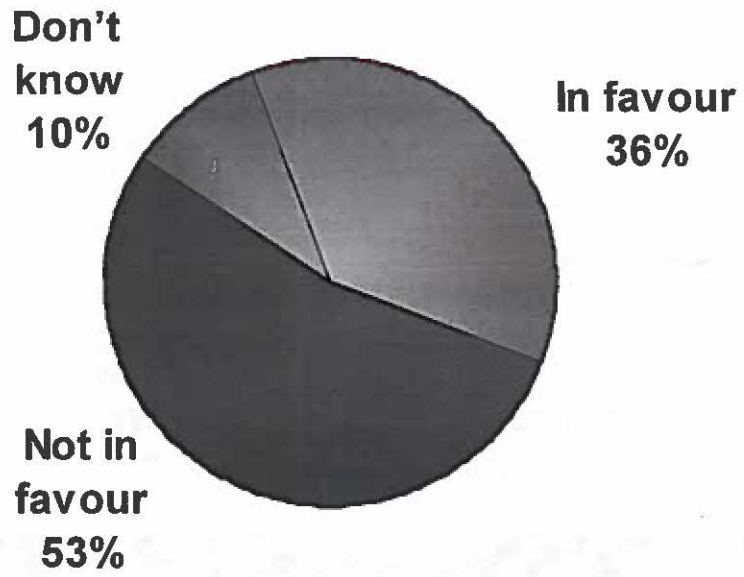
More likely

Less likely

POLLARA

More than one-third would increase their maximum contribution if reduced to 8% with future surplus; 53% opposed

- Members whose maximum contribution was 8.1% or higher (79% of members) were asked if they would be willing to contribute more if a commitment was made to reduce contributions to eight percent if the pension plan shows a surplus in future. Over one-third of members (36%) would increase their maximum contribution under this circumstance, including 45% of those already eligible for unreduced pension. More than half (53%) do not support such a move.
- There is a greater willingness to exceed one's maximum contribution among those approaching retirement.



Career groupings	In favour (%)	Not In favour (%)
Newer members (0 – 4.9)	32%	53%
Newer members (5 – 9.9)	38%	54%
Mid-career members (10 – 14.9)	36%	56%
Mid-career members (15 – 21.9)	36%	51%
Older members (within 10 yrs unreduced pension)	38%	55%
Older members (within 5 yrs unreduced pension)	39%	52%
Older members (eligible for unreduced pension)	45%	46%

Q13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12.) If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than [RESPONSE FROM Q12] of your salary in order to keep all pension provisions at current levels?

POLLARA

Support and opposition to increasing maximum contribution for future reduction is fairly consistent across member segments

- Rural members (30%) are slightly less likely to be in favour of increasing their maximum contribution with a reduction to eight percent in the event of a surplus.

Member segment		In favour (%)	Not in favour (%)
OVERALL		36%	53%
Gender	Female	36%	53%
	Male	37%	55%
Employment type	Full-time	36%	52%
	Part-time	32%	57%
	Occasional	38%	57%
Employer type	District school board – English	36%	53%
	District school board – French	39%	50%
Place of work	Elementary	37%	53%
	Secondary	34%	54%
Urban/Rural	Urban	37%	53%
	Rural	30%	55%

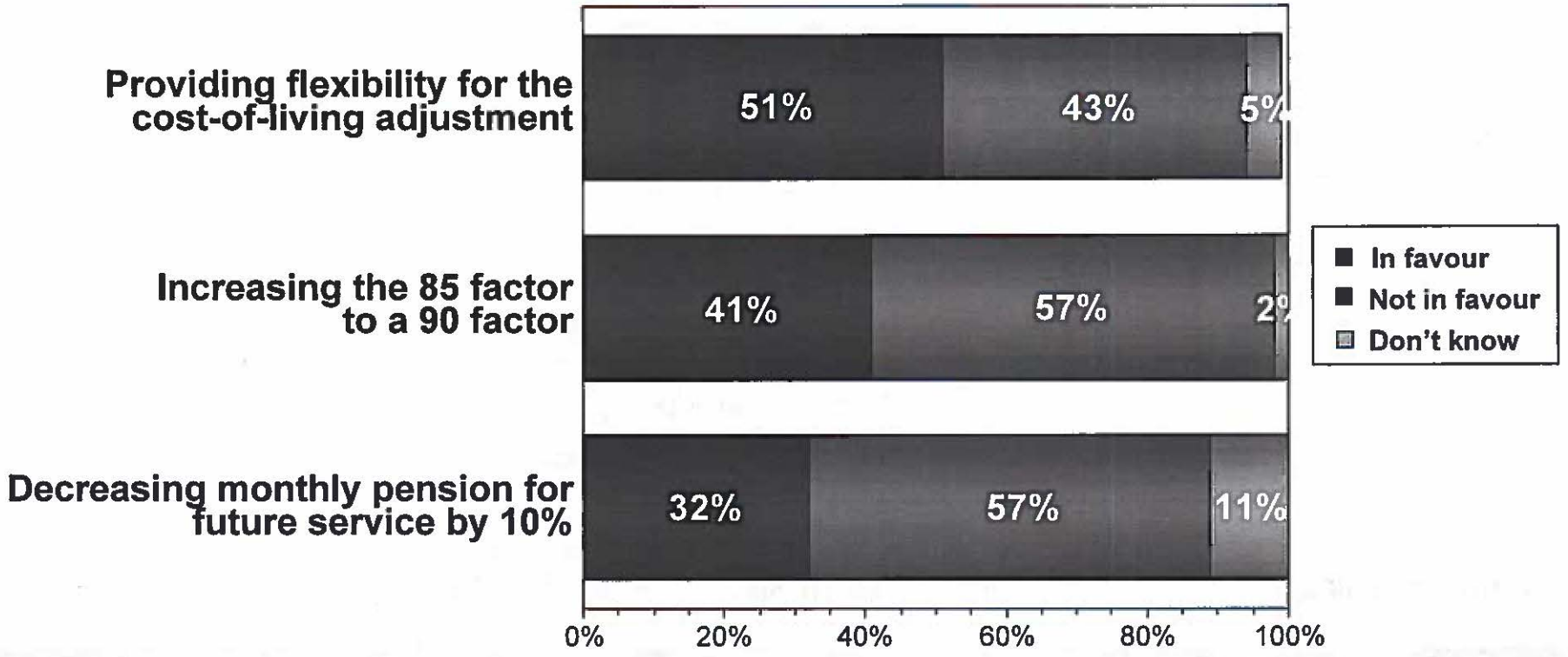
More likely

Less likely

POLLARA

Support for benefit changes to keep contributions from rising beyond maximum ranges from 32% to 51%

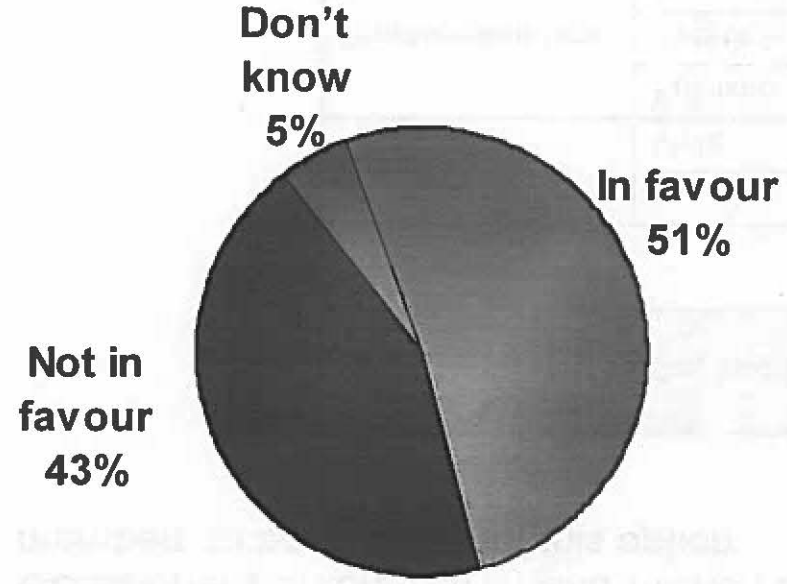
- If members were contributing their maximum, support for potential benefit changes would range from 32% (for reducing pensions by 10%) to 51% (for making the cost-of-living adjustment flexible).



Qs 14-16.Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about… (RANDOMIZE ORDER)

One-half of pension plan members would be in favour of making cost-of-living increases to future retirees' pension flexible

- One-half (51%) of pension plan members are in favour of making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible.
- This option is the favourite among newer members, with 59% being in favour. Support decreases as members approach retirement.



Career groupings	In favour (%)	Not in favour (%)
Newer members (0 – 4.9)	59%	33%
Newer members (5 – 9.9)	59%	37%
Mid-career members (10 – 14.9)	51%	45%
Mid-career members (15 – 21.9)	45%	49%
Older members (within 10 yrs unreduced pension)	43%	53%
Older members (within 5 yrs unreduced pension)	38%	57%
Older members (eligible for unreduced pension)	37%	61%

Q16. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

POLLARA

Support for flexible cost-of-living adjustment fairly consistent among member segments

- Occasional workers (66%) and French board members (56%) are more likely than other members to be in favour of this option.

Member segment		In favour (%)	Not in favour (%)
OVERALL		51%	43%
Gender	Female	51%	43%
	Male	51%	45%
Employment type	Full-time	50%	46%
	Part-time	52%	40%
	Occasional	66%	27%
Employer type	District school board – English	51%	44%
	District school board – French	56%	29%
Place of work	Elementary	53%	42%
	Secondary	48%	47%
Urban/Rural	Urban	51%	43%
	Rural	53%	43%

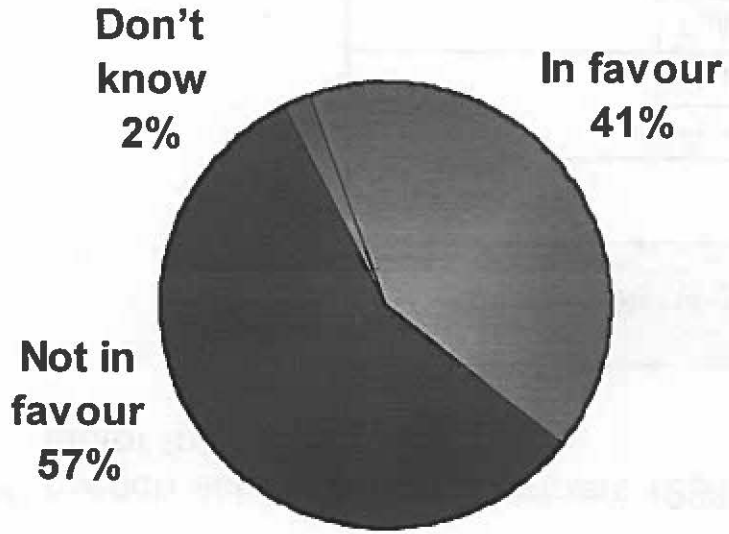
More likely

Less likely

POLLARA

Two-fifths of members support increasing 85 factor to 90 to keep contributions from rising beyond their maximum; more than half disagree

- Over two-fifths (41%) of pension plan members are in favour of increasing the 85 factor to 90, meaning that in the future members would work an extra two and a half years to quality for unreduced pension in order to retire before age 65.
- Members who are already eligible for unreduced pension are significantly more likely to be in favour of switching to a 90 factor (74%). Newer members are second most likely to be in favour (44%), followed by older members within 5 years of unreduced pension (42%). No more than 38% of members are in favour of switching to a 90 factor among the other groupings.



Career groupings	In favour (%)	Not In favour (%)
Newer members (0 – 4.9)	44%	52%
Newer members (5 – 9.9)	38%	59%
Mid-career members (10 – 14.9)	36%	64%
Mid-career members (15 – 21.9)	34%	63%
Older members (within 10 yrs unreduced pension)	36%	62%
Older members (within 5 yrs unreduced pension)	42%	56%
Older members (eligible for unreduced pension)	74%	22%

Q14. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it.

POLLARA

More than half of every member segment not in favour of changing 85 factor to 90

- French school board members (29%) are least likely to be in favour of increasing the 85 factor to 90.

Member segment		In favour (%)	Not in favour (%)
OVERALL		41%	57%
Gender	Female	41%	56%
	Male	41%	58%
Employment type	Full-time	40%	57%
	Part-time	43%	55%
	Occasional	44%	51%
Employer type	District school board – English	41%	56%
	District school board – French	29%	70%
Place of work	Elementary	42%	55%
	Secondary	38%	60%
Urban/Rural	Urban	41%	57%
	Rural	43%	54%

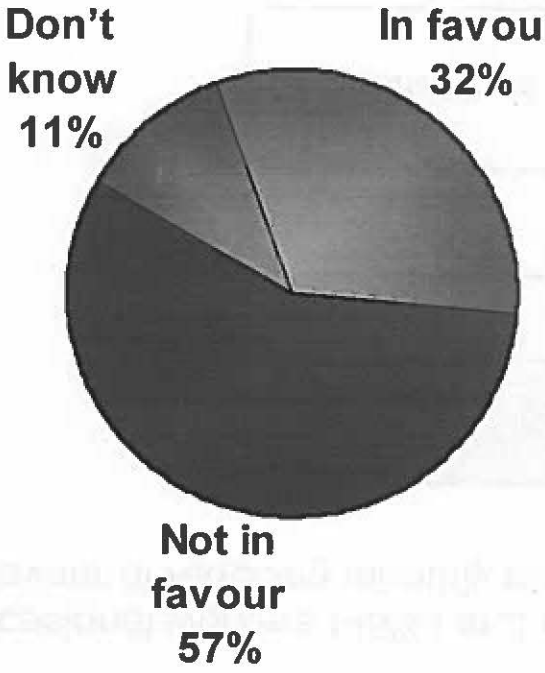
More likely

Less likely

POLLARA

Almost one-third of pension plan members are in favour of reducing monthly pension for future service by about 10%; more than half disagree

- Almost one-third (32%) of pension plan members are in favour of reducing monthly pension for future service by about 10%.
- Newer members (41% and 34%) are more supportive than other career groupings of reducing monthly pension for future service by about 10%.



Career groupings	In favour (%)	Not in favour (%)
Newer members (0 – 4.9)	41%	47%
Newer members (5 – 9.9)	34%	54%
Mid-career members (10 – 14.9)	29%	60%
Mid-career members (15 – 21.9)	24%	62%
Older members (within 10 yrs unreduced pension)	26%	65%
Older members (within 5 yrs unreduced pension)	27%	64%
Older members (eligible for unreduced pension)	24%	63%

Q15. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

POLLARA

Reduction to monthly pension by about 10% opposed by more than half of most member segments

- Occasional workers (45%) and French school board members (45%) are more likely to be in favour of reducing monthly pension for future service by 10%.

Member segment		In favour (%)	Not in favour (%)
OVERALL		32%	57%
Gender	Female	32%	57%
	Male	34%	57%
Employment type	Full-time	31%	59%
	Part-time	33%	53%
	Occasional	45%	44%
Employer type	District school board – English	32%	57%
	District school board – French	45%	41%
Place of work	Elementary	34%	55%
	Secondary	28%	61%
Urban/Rural	Urban	32%	58%
	Rural	35%	52%

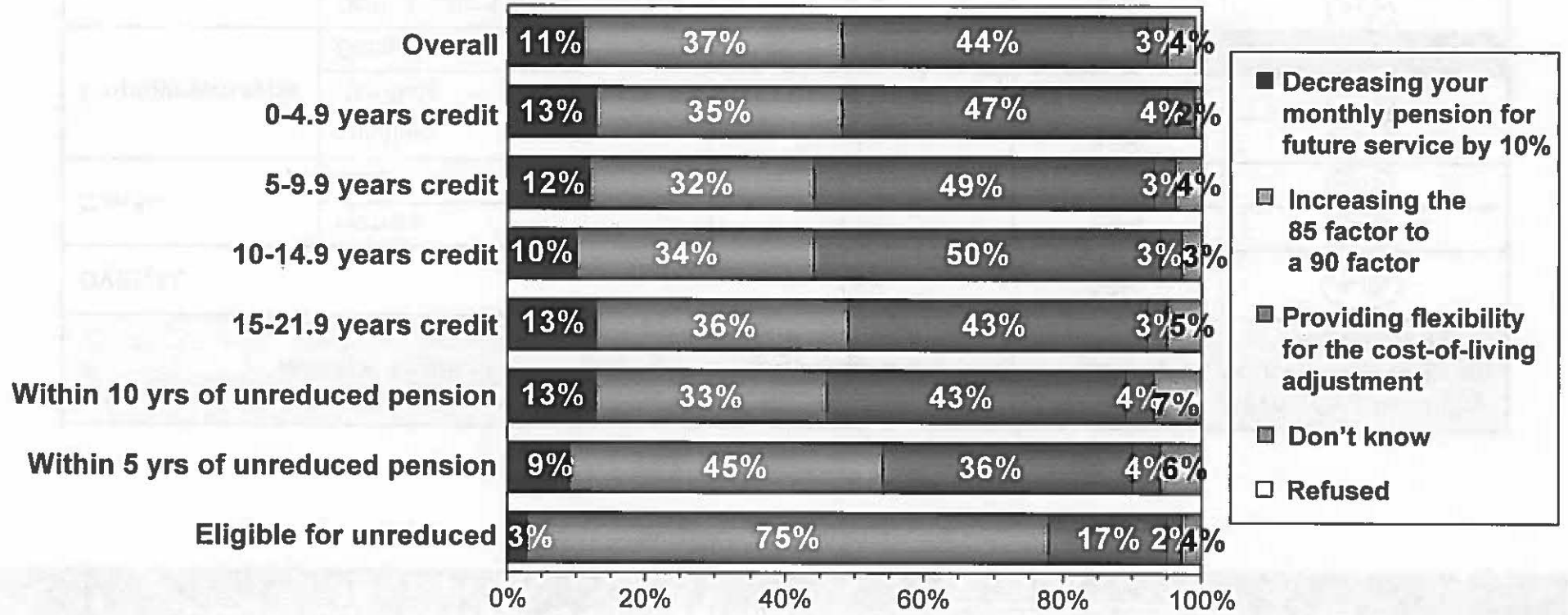
More likely

Less likely

POLLARA

Providing flexibility for the cost-of-living adjustment is the preferred potential change to members' pension plan

- When asked which of the three potential plan changes they preferred, 44% of pension plan members opt for the flexible cost-of-living adjustment.
- This change is the top choice for five of the seven career groupings. Only members within five years of unreduced pension and those already eligible for unreduced pension prefer increasing the 85 factor to 90.



Q17. We've discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. when' I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan.

Plurality of all member segments name flexible cost-of-living adjustment as preferred change

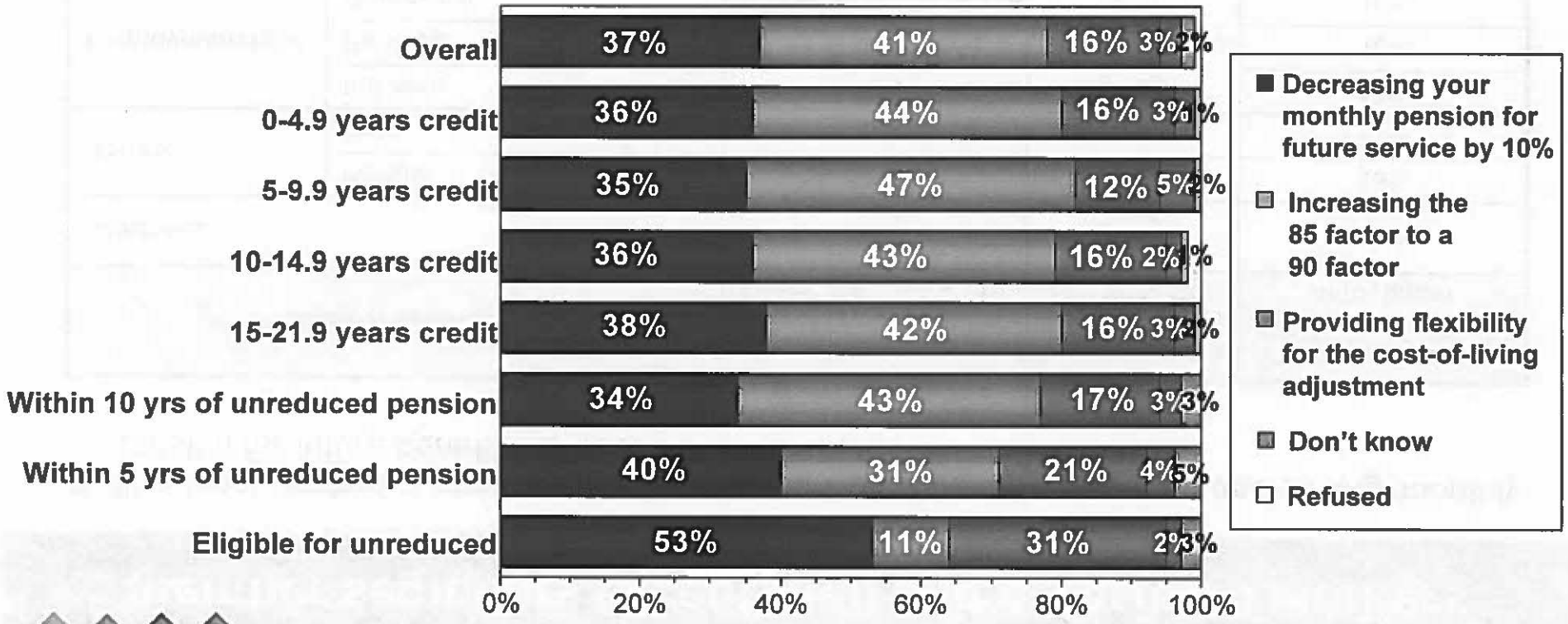
Member segment		Decreasing your monthly pension for future service by 10%	Increasing the 85 factor to a 90 factor	Providing flexibility for the cost-of-living adjustment
OVERALL		11%	37%	44%
Gender	Female	11%	36%	45%
	Male	11%	38%	43%
Employment type	Full-time	11%	37%	44%
	Part-time	12%	38%	42%
	Occasional	13%	31%	52%
Employer type	District school board – English	11%	37%	44%
	District school board – French	25%	20%	46%
Place of work	Elementary	12%	36%	45%
	Secondary	10%	38%	44%
Urban/Rural	Urban	12%	37%	43%
	Rural	8%	35%	50%

More likely Less likely

POLLARA

Increasing 85 factor to 90 is the least preferred potential change to the pension plan

- When asked which of the three potential plan changes they are least willing to have made, a plurality (41%) name increasing the 85 factor to a 90 factor.
- This option is the least favourite choice for five of the seven career groupings. Again, only members within five years of unreduced pension and those already eligible for unreduced pension have different least favourite options.



Q18. Which potential change are you least willing to have made?

Increasing 85 factor to 90 is the least preferred change for all member segments except men and occasional workers

- The least preferred change among men and occasional workers is decreasing monthly pension for future benefits by 10%.

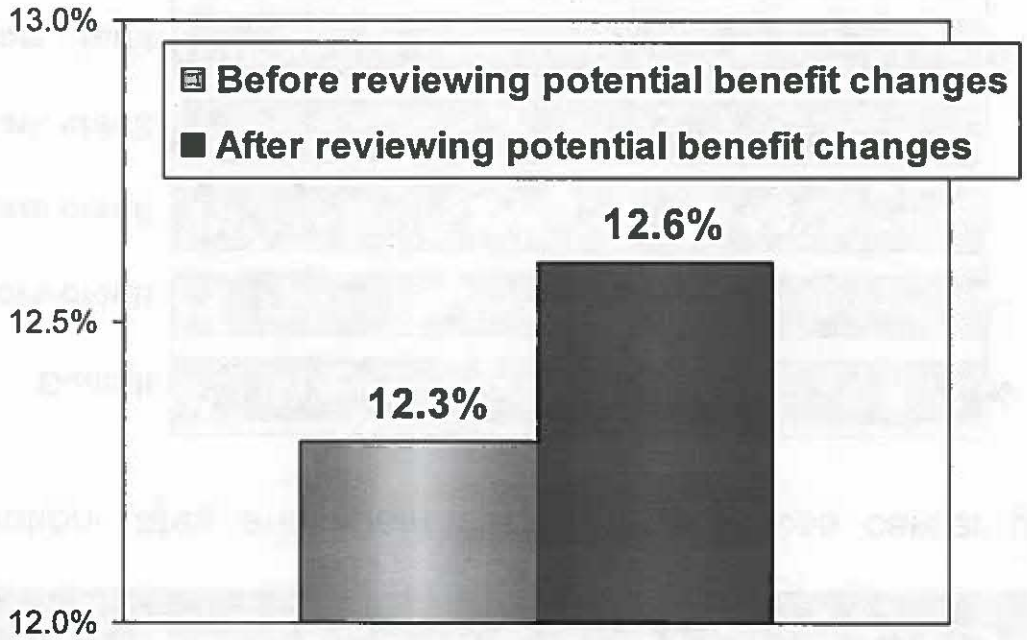
Member segment		Decreasing your monthly pension for future service by 10%	Increasing the 85 factor to a 90 factor	Providing flexibility for the cost-of-living adjustment
OVERALL		37%	(41%)	16%
Gender	Female	36%	(42%)	16%
	Male	40%	38%	17%
Employment type	Full-time	36%	(41%)	17%
	Part-time	38%	(42%)	15%
	Occasional	(42%)	40%	15%
Employer type	District school board – English	38%	(40%)	16%
	District school board – French	23%	(58%)	15%
Place of work	Elementary	38%	(42%)	15%
	Secondary	35%	(39%)	19%
Urban/Rural	Urban	37%	(41%)	17%
	Rural	38%	(42%)	13%

More likely **Less likely**

POLLARA

After reviewing potential benefit changes, members increase their maximum contribution from 12.3% to 12.6%

- After reviewing potential changes to their pension provisions, members were asked to identify the maximum contribution they would be willing to make in order to maintain their current provisions.
- Members' maximum contribution increased to an average maximum of 12.6% (up 0.3 points). A quarter (25%, down 2 percentage points) of members became willing to contribute up to 11%. More than two-thirds (67%, up 7 points) of members became willing to have contributions exceed 11%.

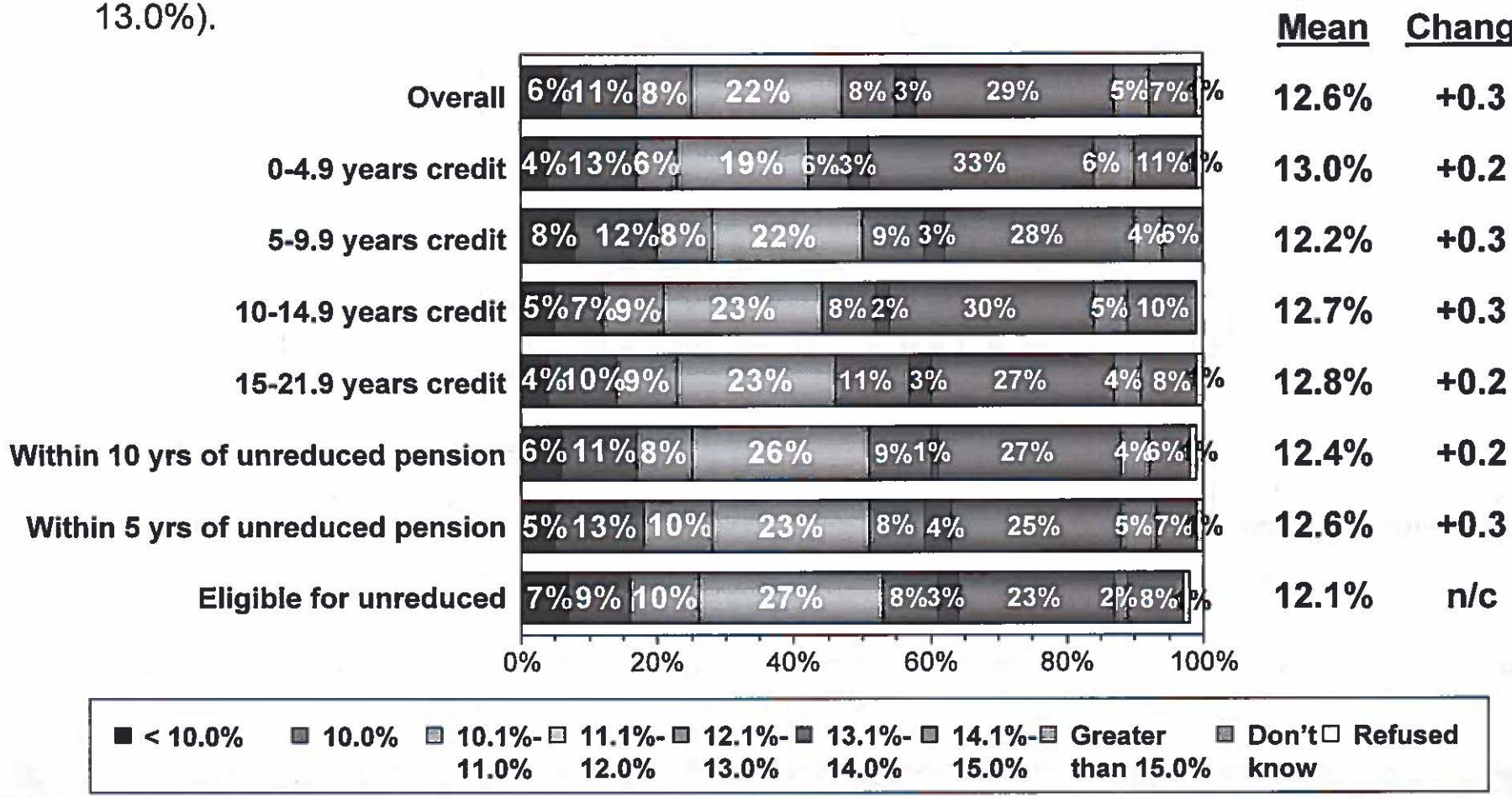


Q19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

POLLARA

Maximum pension contributions fairly consistent among different career groupings

- Maximum contribution rates are again very similar across career groupings (12.1%-13.0%).



Q19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

POLLARA

Maximum contributions fairly consistent among different member segments

- Part-time workers (13%) once again are willing to contribute slightly more, whereas French school board members are willing to contribute the least (10.7%).

Member segment		Mean	Change
OVERALL		12.6%	+0.3
Gender	Female	12.6%	+0.2
	Male	12.3%	+0.1
Employment type	Full-time	12.5%	+0.2
	Part-time	13.0%	n/c
	Occasional	12.7%	+0.1
Employer type	District school board – English	12.6%	+0.2
	District school board – French	10.7%	n/c
Place of work	Elementary	12.6%	+0.2
	Secondary	12.4%	+0.2
Urban/Rural	Urban	12.5%	+0.2
	Rural	12.8%	+0.2

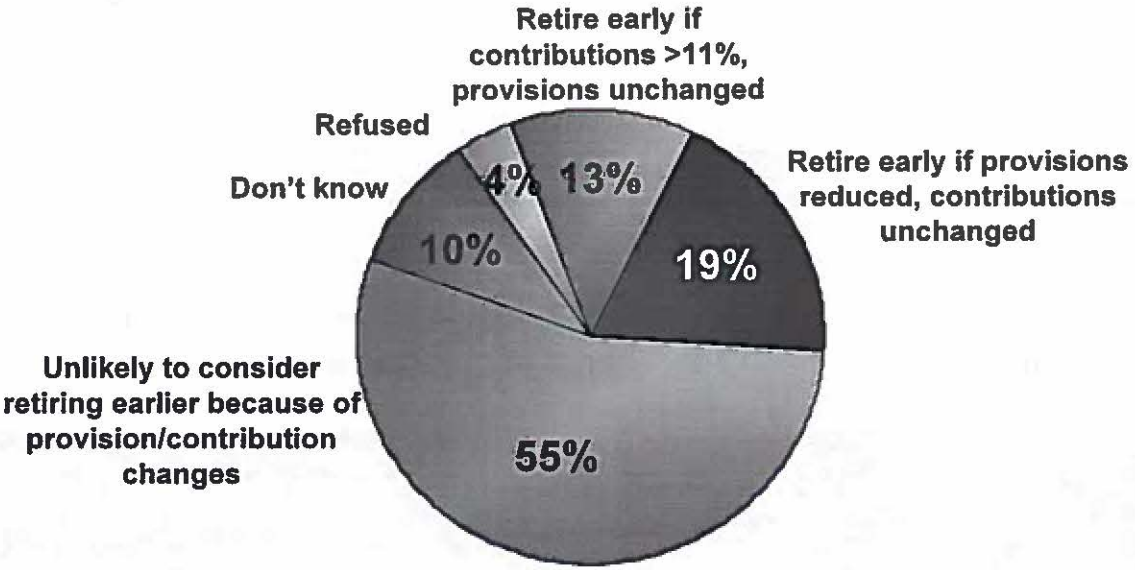
More likely

Less likely

POLLARA

Early retirement slightly more likely if provisions reduced rather than contributions increased; more than half say intentions unchanged

- More than half (55%) of members approaching retirement (age plus years of credit ≥ 74) say they are unlikely to consider retiring earlier than planned as a result of changes to their future pension provisions and contribution rates.
- A further 19% would consider retiring earlier than planned if the pension provisions they will earn in future years are reduced, even if their contributions rates remain the same. If contributions increase to more than about 11% of their salary, 13% would consider retiring earlier than planned, even if their provisions are unchanged.
- Overall results are mirrored by members within five years of unreduced pension and those who are already eligible. Men (17%) are slightly more likely than women (10%) to retire if contributions increase to more than 11%.



Q20. (ASK IF AGE + YEARS OF CREDIT ≥ 74) Which ONE of the following three statements best represents you own viewpoint: (RANDOMIZE ORDER OF STATEMENTS)

Approval Notification, PDF version of PO 225606 .rtf

From: OSS-iProcurement (MGCS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: OSS-iProcurement (MGCS) [OSS-iProcurement@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; martin.boucher@ca.pwc.com [martin.boucher@ca.pwc.com]
Subject: Approval Notification, PDF version of PO 225606
Date: Monday, September 26, 2016 10:55:45
Attachment 1: image003.png
Attachment 2: OSS-225606.pdf

****Please note:** do not email or reply to this message. This mailbox is not monitored for incoming emails and is used for outgoing iProcurement emails only.

Hi,

Just a quick message to confirm that your **Requisition # 305048** has been posted to **Purchase Order # 225606**.

The Purchase Order has been approved and attached is a PDF version for your records. A copy is also being forwarded to the Supplier.

For any Ministry questions or concerns, please contact the OSS Contact Centre at (416) 326-9300 or toll free at (866) 979-9300.

For any Customer questions or concerns, please contact the OSS Contact Centre at (416) 212-2345 or toll free at (866) 320-1756.

Thank you and have a great day,

i-Procurement

Enterprise Financial Services and Systems

Financial Processing Operations Branch

Ontario Shared Services | Ministry of Government and Consumer Services

Visit the OSS Services Listing

vi_logo_xsmall

Ontario Shared Services

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M
G
C
S

OSS-225606.pdf

Ontario

Ontario Shared Services
OSS Contact Centre: (416) 212−2345
Toll Free: 1−866−320−1756

Purchase Order

Purchase Order No.	Release	Revision	Page
OSS 225606		0	1/1

IMPORTANT: Suppliers must show the Purchase Order Number and Purchase Order Line Number on all invoices, packing slips, labels, etc.

PRICEWATERHOUSECOOPERS LLP
2600−18 YORK ST
PWC CENTRAL ACCOUNTING
TORONTO, ON M5J 0B2
CANADA

Supplier No.		Contract No.	
2642		OPCD−PWC−01	
Date Issued		**Date Revised**	
September 26, 2016			
Supplier's Phone	**Supplier's Fax**		**Ship Via**
Freight Terms	**F.O.B**		**Terms of Payment**
NO CHARGE	Not Applicable		NET 30

Ship To	**Bill to**
7 Queen's Park Cres, 1st Floor Toronto 7 Queen's Park Cres Toronto Toronto,ON M7A 1Y7 CANADA	Email to: OSSAPNBPOInvoice@ontario.ca Or Mail to: OSS, FINANCIAL PROCESSING OPERATIONS 200 FIRST AVE W 3RD FLOOR NORTH BAY,ON P1B 3B9 CANADA

NOTES TO SUPPLIER:

SUBJECT TO ALL STANDARD TERMS AND CONDITIONS ESTABLISHED/ATTACHED TO THIS ORDER. PLEASE SUPPLY THE FOLLOWING GOODS AND/ OR SERVICES

Line No.	Catalogue/Part Number and Description	Delivery Date	Tax	Quantity	UOM	Unit Cost $	Total Amount $
1	FY 16/17 PWC − Pensions TREASURY BOARD SECRETARIAT Requestor: VIRANI, SHYROSE	26−SEP−16	13% HST	**100,000.00** 100,000.00	Dollars		100,000.00

GIBSON−SMITH, C

TOTAL CAD $ **100,000.00**

The property and/or services ordered/purchased hereby are purchased for the use of the Crown in right of Ontario, and are subject to the Harmonized Sales Tax (HST) at the stated rate for each line. Prices quoted above do not include tax.
The quoted HST rate is a guideline only as the appropriate tax is to be determined, by the supplier, at the time of billing.

PURCHASE ORDER (PO) TERMS AND CONDITIONS

Interpretation

1. A reference to the Ontario Government ("Ontario") will hereinafter mean a reference to Her Majesty the Queen in right of Ontario.
2. This PO is to be construed according to the laws of the Province of Ontario.

Entire Agreement

3. The goods and services described in the Purchase Order (the "PO") are provided by Supplier subject to the following terms and conditions. Supplier agrees to be bound by and to comply with all such conditions. Unless expressly accepted by Ontario, in writing, or as otherwise set out herein, no other terms shall be binding on Ontario. All exhibits, attachments, technical specifications, drawings, notes, instructions, or information referenced in the PO are incorporated herein by reference.
4. Where terms and conditions are not otherwise expressly provided for in a previously signed agreement related to the goods or services referenced by this PO, this PO, upon acceptance by the Supplier or his duly authorized Agent, serve as a written memorandum of the complete contract between the Supplier and Ontario and, upon acceptance by the Supplier, the Supplier shall be deemed to covenant to comply with the conditions herein. Where there is a previously signed agreement and a conflict arises between the provisions of the PO and the agreement, the terms and conditions of the previously signed agreement shall govern.

Time

5. Time shall be of the essence.

Force Majeure

6. Supplier shall not be liable for default or delay due to causes beyond Supplier's reasonable control and without fault or negligence on the part of Supplier. The Supplier gives Ontario prompt notice in writing when any such cause appears likely to delay delivering and /or performing of services and takes appropriate action to avoid or minimize such delay. If any such default or delay threatens to impair Supplier's ability to meet delivery requirements for its material, supplies and services, Ontario shall have the right, without any liability to Supplier, to cancel the portion or portions of this PO so affected. Ontario shall not be liable for default or delay in the performance of its obligations due to cause beyond its reasonable control.

Waiver

7. The failure of Ontario to insist in any instance upon the strict performance of any provision of this PO, or to exercise any right or privilege granted to Ontario hereunder shall not constitute or be construed as a waiver of any such provision or right and the same shall continue in force.

Sale of Goods Act

8. Subject to the provisions herein, The Sale of Goods Act of the Province of Ontario applies to this contract insofar as any part of this contract relates to goods.

Supplier's Warranties

9. In addition to any other express or implied warranties, the Supplier warrants that the Goods or Services furnished pursuant to this PO will be: (a) free from defects in title, workmanship and material; (b) free from defects in design except to the extent that such items comply with detailed designs provided by Ontario; (c) of merchantable quality and suitable for the purposes intended, specifications and free from liens or encumbrances on title. All services are performed in accordance with current, sound and generally accepted industry practices by qualified personnel trained and experienced in the appropriate fields.
10. In addition to the warranties and conditions implied by The Sale of Goods Act of the Province of Ontario, the Supplier warrants that there are no patents, trademarks or other rights restricting the use, repair or replacement of the goods furnished or any part thereof.
11. All products supplied against this PO must comply with WHIMIS regulations.

Indemnity and Insurance

12. The Supplier agrees to defend, indemnify and hold harmless Ontario from and against all claims, demands, losses, costs, damages, actions, suits or other proceedings by whomever made, filed, or prosecuted in any manner arising from the provision of the goods or services under this PO.
13. Supplier and any Subcontractor used by Supplier in connection with this PO shall carry Comprehensive General Liability and adequate Comprehensive Automobile Liability Insurance. At Ontario's request, Supplier shall provide to Ontario certificates from Supplier's insurers showing that such coverage is in effect and agreeing to give Ontario thirty (30) days' prior notice of cancellation of the coverage. Ontario may require minimum liability coverage depending on circumstances.

Freedom of Information and Protection of Privacy Act

14. Suppliers are advised that this PO is governed by the Freedom of Information and Protection of Privacy Act and that all information submitted pursuant to this PO is subject to that Act.

Confidentiality

15. The supplier shall treat as confidential and shall safeguard all knowledge or information acquired by it under this contract.

Assignment

16. The Supplier shall not assign this contract in whole or in part or any monies due under it without obtaining the prior written consent of Ontario.

Changes and Amendments

17. Ontario shall have the right at any time, by written notice, in the form of a Change Order, to the Supplier, to make any changes it deems necessary, including, but not limited to, changes in specifications, design, delivery, testing methods, packing or destination. If any such required changes cause an increase or decrease in the cost of or the time required for performance, an equitable adjustment shall be made in the contract price or delivery schedule, or both. Any claim by the Supplier for adjustment under this clause shall be deemed waived unless asserted in writing within ten (10) days from receipt by the Supplier of notice of change. Price increases, extensions of time for delivery and change in quantity shall not be binding on Ontario unless evidenced by a form of Change Order issued and signed by Ontario.

The Goods

18. Any goods that are not in accordance with this PO will be returned at the Supplier's expense.
19. Substitutions are not permitted without the written approval of Ontario.
20. Subject to the provisions of the section, property and risk in the goods passes upon examination and acceptance by Ontario. In the event that any apparent defects are discovered in any goods under this PO within six (6) months after acceptance, such goods will be rejected and the Supplier shall promptly replace the defective goods at his expense.

Delivery

21. All goods ordered in quantities specified shall be delivered to the specified destination in the Province of Ontario, in good order and free from any extra expense to Ontario.
22. Unless otherwise specified, all deliveries shall be made on a normal working day.
23. The Supplier shall ensure strict adherence to any specified delivery schedule.
24. If the Supplier fails to deliver the goods on the date specified, Ontario may terminate this PO upon seven (7) days notice to the Supplier.
25. Any request for extension or lead times due to circumstances beyond the control of the Supplier must be made to Ontario which will then inform the Supplier if the requested extension is acceptable.
26. In the event that unauthorized deliveries are made in advance of date(s) specified, Ontario has the option to return any such items or goods delivered at the cost of the supplier.
27. Where goods are shipped F.O.B., Supplier's dock via a common carrier, the Supplier must make a reasonable contract with the carrier and must give immediate notice of shipment to Ontario.
28. If the Supplier fails or refuses to make deliveries on the dates herein specified (as such dates may be extended by any cause of excusable delay), Ontario may at its option terminate this contract as to any goods not then delivered hereunder and recover any amounts therefore paid on account thereof and may purchase other goods of a similar description, charging the Supplier with any excess cost incurred by Ontario by reason of such purchase.
29. The Supplier must communicate immediately upon receipt of the PO from the Purchasing Officer for further instruction if he is unable to supply/deliver the order as specified.
30. Ontario will accept neither responsibility nor charges for quantities or goods delivered/supplied by the Supplier in excess of the quantities shown on the PO without prior written authorization of Ontario by amendment to the PO. In the event that additional quantities are agreed to by Ontario they will be subject to renegotiations of the contract price which negotiations shall take into consideration possible volume discounts resulting from the total quantity of goods received.
31. A detailed packing slip must accompany each shipment. The PO number and requisition number must be shown on all packages, bills of lading, invoices and relevant documents.
32. It is the Supplier's responsibility, at its cost, to provide the necessary facilities and manpower to accomplish unloading from whatever means of transport is employed.

Payment and Invoicing

33. Payment shall be made within thirty (30) days of the invoice date upon receipt and approval of a fully valid/complete invoice or through terms established otherwise in a related contract.
34. All prices quoted shall be in CAD or USD as indicated on the PO.
35. Invoices must be typed or printed in ink.
36. All invoices must show:
    - (i) full particulars, description of goods, quantity, rate and charge for each item;
    - (ii) the name and postal address of the person or firm (Supplier) to whom the account is payable;
    - (iii) any applicable taxes and import duty separate from the basic cost of goods and services, including Federal Sales Tax credits, Goods and Services Tax, Provincial Sales Tax and Harmonized Sales Tax charges;
    - (iv) when transportation charges have been prepaid on orders shipped F.O.B. Supplier's dock, the original freight, cartage or express receipt must accompany the invoice and the freight charge must be shown as a separate item on the invoice. Invoice for labour and materials must give details of quantities and prices of materials and the number of hours worked with the rates per hour;
    - (v) where equipment has been rented, the commencement date of rental, the duration of rental and the rental rates; and
    - (vi) all applicable transportation charges, shown separately.
37. For all invoices, Ontario reserves the right to seek further details as necessary.
38. Ontario shall have right at any time to set-off any amounts due to the Supplier, (or any of its associated or affiliated companies) against any amounts owed by Ontario with respect to this PO or any subsequent PO or any other contractual agreement between the parties hereto.

Termination

39. Ontario reserves the right to terminate this contract:
    - (i) immediately upon giving written notice in the event of the Supplier being adjudged a bankrupt or making a general assignment for the benefit of creditors or a receiver being appointed on account of the Supplier's insolvency; and
    - (ii) without cause or liability upon giving the Supplier thirty (30) days prior written notice.
40. Ontario will not, by virtue of any of the above instances of termination, waive any rights or remedies it may have in this PO or otherwise at law. Ontario shall only be responsible for the payment for goods or services received in connection with this PO up to and including the effective date of any such termination. Termination shall not relieve the Supplier from the supplier's warranties and other responsibilities relating to the goods or services provided or money paid, or both, up to and including the date of termination.

As discussed.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: As discussed
Date: Thursday, September 15, 2016 20:47:35

Hi Lucy.

Further to our discussion, below is an outline of the work we discussed. The work relates to the jointly sponsored pension plans (OTPP and OPSEUPP) as reported in the Province's consolidated financial statements.

I'll look forward to hearing back from you.

Best regards,

Nadine

416 562 9509

The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following

· Taking into account public sector accounting principles, advice and guidance on complex accounting and reporting matters related to accounting for pensions on the Province's consolidated financial statements.

· The Vendor will participate in meetings as necessary to support the engagement objectives:

· Working with management of OPCD's Accounting Policy and Financial Reporting Branch (APFR), the provider of complex accounting services related to the following possible areas:

· Develop discussion and analysis material

· Develop draft input/briefing materials/option papers

· Provide accounting advice and guidance related to the accounting for pensions on the Province's financial statements

· Participate in discussions with internal and external stakeholders, as required

As part of this engagement, the consultant(s) would be expected to provide professional accounting expertise in assessing actuarial assessments for specified plans in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250 (3250.050 to PS3250.059).

As previously referenced.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: As previously referenced
Date: Thursday, September 22, 2016 10:24:36
Attachment 1: FMP_Temporary Plan Improvement Zone Discussion Deck.pdf

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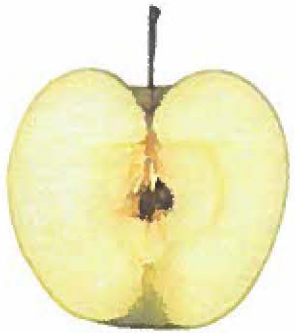
Hi Matt.

Please see last page**

Nadine

FMP_Temporary Plan Improvement Zone Discussion Deck.pdf



TEMPORARY PLAN IMPROVEMENTS

Draft for Discussion

March 19, 2014 (Sponsor's Task Force Meeting)

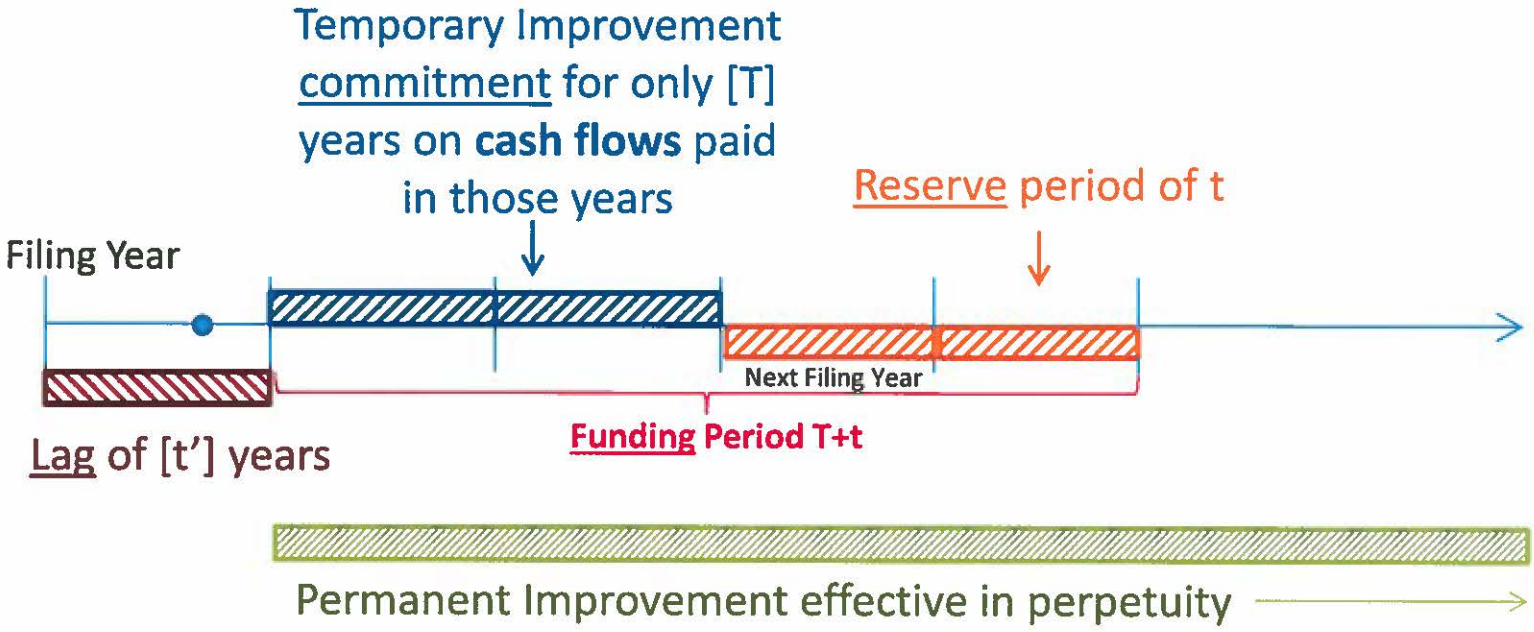
Funding Management Policy - Framework Description

TEMPORARY PLAN IMPROVEMENTS INCLUDE:

- Decrease to cash contribution paid
- Increase to benefits paid to pensioners in pay
- a combination of both

Temporary plan improvements are determined in a filed funding valuation. They are effective with a **lag** of [t'] years with a **commitment** of [T] years, **reserve** over t years and **funded** over a period of T+t. They impact only affected cash flows paid in years [t'] through [T].

Filing in temporary zone occurs if new temporary benefits schedule better than the current temporary benefits schedule.



Funding Management Policy - Framework Description

Valuation Basis

Assets = 110% of Liabilities valued at interest rates + 0.5%

Zone:	**Permanent Plan Improvements**
Mechanism:	Improve benefits as negotiated
Funding Risk:	Plan is essentially fully funded at Government of Canada long bond rates. Funding security is desired to ensure the Plan can support these benefits continually in the future. The impact of new teachers is important as they will create losses.

That is, Assets ~ 133% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1%

Zone:	**Temporary Plan Improvements**
Mechanism:	Improve benefits or lower contributions as negotiated[1]
Funding Risk:	Plan is well funded and can afford changes that temporarily provide a benefit enhancement (as long as it does not create a long term cost) and/or lower the contributions being paid into the plan.

[1] A funding reserve will be created to help support the temporary benefits

That is, Assets ~ 116% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.55%

Zone:	**Fully Funded**
Mechanism:	Maintain Base Benefits and Contributions
Funding Risk:	Plan is adequately funded to provide base benefits supported by the base contributions. Given the volatility of market factors and the numerous assumptions in the funding valuation, "fully funded" is considered a range.

Zone:	**Additional Support Required From Current FMP Levers**
Mechanism:	Raise Contribution Rates and/or Invoke Conditional Inflation Protection as negotiated
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions. An increase to the contribution rate (within FMP maximum) and/or a decrease to the level of indexing being provided are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Zone:	**Additional Support Required From New/Additional Changes**
Mechanism:	Negotiate other plan changes
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions and CIP is fully invoked and contribution rates are increased to maximum outlined in FMP. Plan changes are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Next step is to review simulation results

TEMPORARY IMPROVEMENTS – Baseline FMP for Simulations

	Distribution Surplus	Surplus/Deficit split
Step 1:	Benefit Improvement (unlimited)	100%

	Distribution Deficit	Surplus/Deficit split
Step 1:	Raise Regular contribution up to 11%	100%

	Temporary Surplus	Surplus/Deficit split
Step 1:	Temporary Regular Contribution Reduction (regular CR no lower than 0%)	100%

Lag: 1 year, Commitment: 3 years, Reserve: 7 years, Funding Period: 10 years, Spread: 1.00%

	Restoration Surplus	Surplus/Deficit split
Step 1:	Lower Special to **1%**	100%
Step 2:	Restore Future Indexation Level to 100%	100%
Step 3:	Catch Up to 50% (both Post 2009-Pre 2014 and Post 2013 at 50%)	100%
Step 4:	Catch Up to 100% (both Post 2009-Pre 2014 and Post 2013 at 100%)	100%
Step 5:	Lower Special to 0%	100%

	Restoration Deficit	Surplus/Deficit split
Step 1:	Raise Special to **1%**	100%
Step 2:	Reduce Indexation Level (Post 2009-Pre 2014: 50%, Post 2013: 0%)	100%
Step 3:	Raise Special no threshold	100%

Note: FMP CR = 12%, Usable Surplus in Temporary zone is based on smooth assets and smooth liabilities

Brief Explanation of Metrics for Analysis

TEMPORARY PLAN IMPROVEMENTS METRICS for ANALYSIS:

- Probability in FMP Zone: Probability that OTPP will be in a particular FMP zone in the future
- Probability Temporary Benefits in pay: Probability that temporary benefits will be paid in the future and in which FMP Zone that will occur
- Probability Temporary Benefits in pay while in FMP Zone: What is the percentage of times a temporary benefits is in pay while in a particular FMP Zone

TEMPORARY IMPROVEMENT ZONE – POTENTIAL METRICS

# observations in each zone	Restoration Zone (Sp CR +CIP+add'l Sp CR)	Restoration Zone (Special CR)	Do Nothing Zone	Temporary Improvement Zone	Distribution Zone, usable surplus
Current (Starting FR 100%)	30%	2%	38%	0%	30%
Metrics					
Probability in FMP Zone (rounded)					
Baseline	32%	2%	27%	33%	6%
Probability in Temporary Benefits in pay (rounded)					
Baseline	0%	0%	9%	21%	3%
Probability Temporary Benefits in pay while in FMP Zone (rounded)					
Baseline	0%	0%	34%	63%	56%

Note: Starting FR= 100%

Asset Ceiling Reports.rtf

From: Petsche, Nadine (TBS) []
To: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]
CC: Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]; uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]
Subject: Asset Ceiling Reports
Date: Tuesday, May 16, 2017 11:30:53

Shayan,

Cindy would like to share the results of the Asset Ceiling analysis with the OAG prior to completion of the work related to pension adjustments. We would like to include appropriate language/caveat regarding pending adjs and plan to update once complete.

Can you please insert the appropriate caveat in the draft report and resend.

Thanks in advance.

Nadine

Automatic reply_ OTPP - Follow-Up Discussion with EY.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]
Subject: Automatic reply: OTPP - Follow-Up Discussion with EY
Date: Friday, July 20, 2018 09:11:27

I am out of the office with periodic access to email and voicemail until 26 July 2018. If you need immediate assistance please contact my assistant Sarah Anderton at 416 943 3143 or sarah.anderton@ca.ey.com

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Automatic reply_ potential conflict.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]
Subject: Automatic reply: potential conflict
Date: Friday, August 10, 2018 12:05:28

I am out of the office with periodic access to email and voicemail until 14 August 2018. If you need immediate assistance please contact my assistant Sarah Anderton at 416 943 3143 or sarah.anderton@ca.ey.com

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Automatic reply_ tax declaration form.docx and confidentiality agreement.rtf

From: Raymond, Martin (CA - Montreal) [maraymond@deloitte.ca]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Automatic reply: tax declaration form.docx and confidentiality agreement
Date: Wednesday, October 19, 2016 09:34:41

Prendre note que je suis à l'extérieur du 17 au 20 octobre avec accès limité à mes courriels. Pour toute urgence veuillez contacter Guillaume Bellavance ou Tina Magloe Francis.

Take note that I am out of the office on October 17 to 20 with limited access to emails. For any urgent matter please contact Max Bazile or Trevor Gary.

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additional info.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: additional info
Date: Sunday, September 18, 2016 12:39:58
Attachment 1: Report on Funding.pdf

Report on Funding.pdf

Teachers' Pension Plan Board

Ontario

REPORT ON FUNDING

April 2002

This is a report on the financial health of the Teachers' pension plan and on the progress of the development of a funding management policy.

The responsibility to ensure a defined benefit pension plan is fully funded lies with the sponsor of the plan, usually the employer. In the case of the Teachers' pension plan, however, there are two sponsors: the Ontario government and the Ontario Teachers' Federation, representing the plan members.

The co-sponsors negotiate the use of surplus and, when there is a deficiency, they both make additional contributions to ensure the plan is fully funded within a specified time period.

To assess the financial health of the plan, we hire an independent actuary to conduct a valuation at least once every three years. This valuation determines if the plan has a funding surplus or deficit.

Funding Valuation Results

On January 1, 2002, the Teachers' pension plan had a funding surplus of $1.9 billion, including a $3-billion smoothing adjustment. Without smoothing, the plan had a $1.1-billion deficit.

($ billions) (at January 1)	**02**	01	00	99	98	96	93**
Net assets	**$ 69.5**	73.1	68.3	59.1	54.5	40.1	29.4
Smoothing	**3.0**	(4.3)	(7.3)	(5.1)	(6.0)	(1.8)	---
Value of assets	**72.5**	68.8	61.0	54.0	48.5	38.3	29.4
Future contributions	**13.7**	14.4	13.4	12.0	12.6	14.5	14.3
Special payments*	---	---	---	3.7	8.5	8.4	8.4
Actuarial assets	**86.2**	83.2	74.4	69.7	69.6	61.2	52.1
Future accrued benefits	**84.3**	76.4	69.8	66.2	62.8	60.5	50.6
Surplus (deficit)	**$ 1.9**	6.8	4.6	3.5	6.8	0.7	1.5

* Payments committed by the government toward the pre-1990 unfunded liability

** Valuation dates determined by co-sponsors

Assumptions

Valuations use many estimates, or assumptions. Among them are: how long will a teacher teach? What will inflation be in the future? What salary increases are teachers likely to receive? How long will the average teacher live?

These assumptions are used to estimate the value of the future benefits owed to teachers. In addition, an assumption of the long-term rate of return is used to determine if today's assets plus future contributions will be sufficient to pay promised pensions.

Valuation Assumptions

(percent)	2002	2001
Discount rate	6.30	6.25
Salary escalation rate	2.90	3.20
Inflation rate	1.90	2.20

The discount rate is the long-term market rate of return used to determine the present value of all future pension benefits and assets.

The assumptions are intended to be accurate over a long horizon. While actual experience mirrors some assumptions closely, annual equity returns fluctuate greatly compared to our assumption (6% plus inflation).

It would be impractical to adjust contribution rates frequently because of investment swings. So, to reduce short-term fluctuations in the funding surplus, equity returns compared to our long-term assumptions are 'smoothed.'

WHAT'S INSIDE...

- Understanding Smoothing pg 2
- Funding Management Policy pg 2
- Use of Surplus pg 4

Questions? www.otpp.com or 1-800-668-0105

Understanding Smoothing

Gains and losses from equities are smoothed over five years, a practice accepted by the actuarial profession and pension regulators.

Smoothing defers gains when actual equity returns exceed the 6% plus inflation assumption. On the other hand, when returns are below the assumption, smoothing defers losses (as is the case this year). This practice is simply used to soften the impact of annual volatility in equity markets.

How Smoothing is Calculated

($ billions)

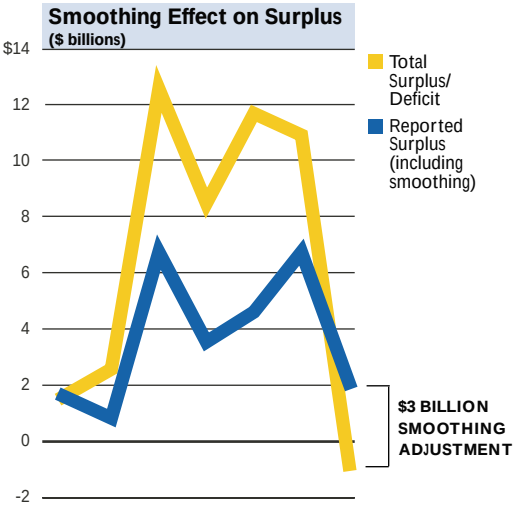
Year	Gain/ (loss)	to be recognized in 2006	2005	2004	2003	Held back in 2002
1997	$3.5					
1998	$1.3				0.3	**0.3**
1999	$6.7			1.34	1.34	**2.7**
2000	($1.2)		(0.24)	(0.24)	(0.24)	**(0.7)**
2001	($6.6)	(1.32)	(1.32)	(1.32)	(1.32)	**(5.3)**
Smoothing						**(3.0)**

Each year, we recognize 20% of equity gains or losses. Smoothing consists of the remaining portions that will be recognized in the future. For the last two years, equity returns have fallen short of our assumption, causing losses held back by smoothing.

At its peak, smoothing held $7.3 billion in reserve. In 2002, smoothing increased actuarial assets by $3 billion to show a $1.9 billion surplus, instead of a $1.1 billion deficit.

However, smoothing is only capable of absorbing short-term fluctuations in returns and will not sustain a funding surplus in a long period of poor market performance.

The funding surplus is the more important number for plan members. It is used to determine benefit improvements or changes to the contribution rate.



Without the $3-billion smoothing adjustment, the plan would have had a funding deficiency of $1.1-billion this year. We are concerned about the downward trend.

Comparing Valuations

We also report a financial valuation in our annual report. The two surpluses are different because the funding surplus includes two projections: future contributions and future benefits for all current teachers.

Comparing the valuations shows a $5.1-billion difference. In other words, there is a $5.1-billion cost to provide future benefits for plan members that are not funded by the current contribution rate. We expect this gap to grow as new teachers enter the plan.

($ billions)	**Financial** (at Dec. 31/01)	**Funding** (at Jan. 1/02)
Net assets	$ 69.5	$ 69.5
Smoothing adjustment	3.0	3.0
Future contributions	---	13.7
Actuarial assets	72.5	86.2
Accrued benefits	65.5	65.5
Future benefits	---	18.8
Surplus	**$ 7.0**	**$ 1.9**

The Role of a Funding Management Policy

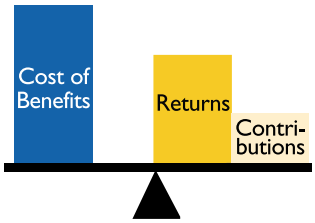
Within certain legislated limits, the co-sponsors negotiate benefit and contribution levels. For 2002, the co-sponsors have decided not to make any changes to contributions or benefits and to concentrate on developing the funding management policy. The pension board fully supports their decision and efforts.

In light of our outlook for equity markets, new benefit costs present a challenge to us and a cautionary note to plan members and the co-sponsors. Over the next decade, we expect modest real rates of return from stock and bond markets compared with the past 10 years.

Despite what the 1990s suggested, 2000 and 2001 have proven that markets are not one-way streets. In fact, historically they have only produced returns equal to the plan's 4.5% long-term funding requirement about 60% of the time.

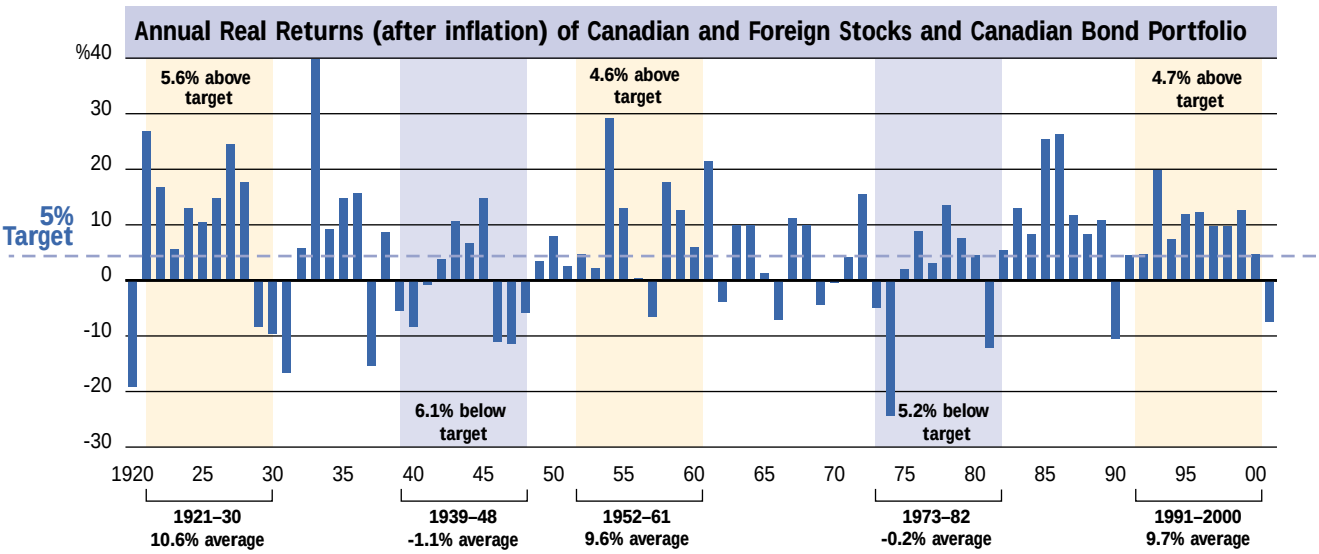
To sustain improved benefit levels for young and future teachers, without the need for contribution increases, we will need to generate a minimum real rate of return of 5% over the long term. That may be very difficult over the next decade.

Over the long term, benefits must balance with contributions plus investment returns or there will be a deficit. If the fund has a deficit when the funding valuation is filed, the law will automatically trigger a contribution rate increase. The only alternative for the co-sponsors would be to reduce future benefits.



The objective of a funding management policy is to provide a framework for improved long-term governance of the fund by determining when it is prudent to increase benefits, change contributions, or conserve assets. This policy will guide the co-sponsors in making these complex decisions, and help address the risks of poor market performance borne by both working teachers and the government. It is also important from an investment perspective, as it will change the risk profile of the fund and affect the pension board's investment policies.

Teachers have told us in focus groups that they would prefer contribution rates to remain stable. A funding management policy will help to ensure this occurs. Development of a workable policy will put the plan's co-sponsors at the forefront of exercising solid pension plan governance that balances the interests of all plan members – working or retired teachers – and the government.



This graph shows how a hypothetical portfolio, based on a similar asset mix as our own, would have performed over the last 80 years. One of the best decades in history was the 1990s. The portfolio includes two-thirds stocks (28% Canadian, 17% U.S., 22% foreign), and one-third Canadian bonds. The plan will need to earn a minimum of 5% over the long term to fund benefits at current levels.

Use of Surplus

In 1990, the plan had a $7.8 billion unfunded liability. The Ontario government agreed to pay the initial unfunded liability through a series of special payments over 40 years.

The pension plan has enjoyed a series of funding surpluses, primarily due to above-average investment growth brought on by strong equity markets throughout the 1990s and lower than expected increases in wages and inflation.

Since 1993, $18.6 billion in surplus was used by co-sponsors to improve benefits and eliminate special payments.

Valuation date	Surplus/ (Deficit)	OTF	Ontario government	Surplus remaining
1990	($7.8) 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	$325 million to offset social contract days	Eliminated special payments for $1.2 billion saving	$0
1996	$0.7	$0.6 for benefit improvements and RCA contributions[2]		$0.1
1998[3]	$6.8	$2.2 for benefit improvements[4]	$4.6 to reduce the value of remaining special payments	$0
1999	$3.5		$3.5 to reduce the value of remaining special payments[5]	$0
2001	$6.8	$6.2 for benefit improvements[6]		$0.6
2002	$1.9	Co-sponsors agreed not to make any changes to benefits or contributions		$1.9
Total		$9.3 billion	$9.3 billion	

[1] Savings offset cuts that would have been made in the education sector as part of the government's overall cost-cutting program.

[2] Benefit improvements: reduced early retirement penalty to 2.5% from 5% for each point short of 90 factor, making it easier to retire early; lower CPP reduction after age 65 (to 6.8% from 0.7%).

[3] In 1998, the co-sponsors agreed future surplus would first be used to eliminate the remaining special payments, and the next $6.2 billion would be available exclusively to the OTF.

[4] Benefit improvements: 85-factor window from 1998 to 2002; lower CPP reduction after age 65 (to 0.6%)

[5] The government paid off its remaining special payments by the end of 1999.

[6] Benefit improvements: permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average YMPE to calculate CPP reduction; pension recalculation based on approximate best-5 salary for older pensioners; and top-up waived for LTIP contributions.

amendment form attached.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: amendment form attached
Date: Tuesday, October 18, 2016 12:16:47
Attachment 1: Scanned from a Xerox multifunction device.pdf

Hi Lucy

Attached, please find an amendment form. Kindly sign and send it back to me.

Thanks
shyrose

Scanned from a Xerox multifunction device.pdf

AMENDMENT
To Add an Additional Resource to a Project

Agreement Number and Description of Project:	OPCD-PWC-01 Accounting Advisory Services
Original SOW Date:	September 16, 2016
Name of Vendor:	PricewaterhouseCoopers LLP
Date of Amendment:	October 18, 2016
Amendment Number:	001

1) Amendment Details:

1.1 This amendment hereby exercises the Ministry's right to add an additional resource to support this project. The additional resource is:

Names, Roles and Per Diem Rates:

Individual's Legal Name	Individual's Role (& level)	Per Diem Rate
Mario Chassé	General Consultant (Actuarial), Level 2 Service Category 2	The per diem rate shall be equal to the per diem rates stipulated in the SOW for each deliverable (ie Accounting Advisory and Accounting Opinion).

1.2 The additional resource does not change the scope, deliverables, or ceiling value of the project.

1.3 This amendment is subject to the terms and conditions of the Master Agreement.

1.4 All other terms and conditions of the Statement of Work OPCD-PWC-01 between PricewaterhouseCoopers LLP and the Ministry are unchanged.

HER MAJESTY THE QUEEN in right of Ontario
as represented by the Minister of the Treasury Board
Secretariat

Per: D. Petsche

Print Name: Nadine Petsche

Title: Director, Accounting Policy and Financial Reporting

PricewaterhouseCoopers LLP

Acknowledged: _____

Print Name: _____

Title: _____

assumption of teachers wanting to see contribution reductions at some point....rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]
Subject: assumption of teachers wanting to see contribution reductions at some point...
Date: Saturday, September 24, 2016 07:41:25
Attachment 1: 2007 Teachers Survey Apendix.pdf
Attachment 2: 2007 Teachers Survey.pdf

Matt/Kerry,

Sharing some additional background relevant to informing assumptions w.r.t. teachers wanting to see contribution reductions at some point.

N

We have been able to locate the member's survey that was conducted in 2007. I would think that is relatively old, with the plan having experienced a lot of changes since then.

The scanned survey and its appendix is attached. The key finding that members would support contribution rates of 12.3% is on page 10 of the PDF.

2007 Teachers Survey Apendix.pdf

Appendix A: Study interview schedule

POLLARA

Interview Schedule

A. Introduction

Good morning/afternoon/evening. May I please speak with (MEMBER NAME)?

IF AVAILABLE- CONTINUE
IF NOT AVAILABLE - SCHEDULE APPOINTMENT TO CALL BACK (IF NECESSARY, READ FIRST 2 SENTENCES OF PREAMBLE BELOW AND SCHEDULE CALL-BACK)

(WHEN MEMBER IS ON LINE) Good morning/afternoon/evening. My name is ( ) and I am calling on behalf of the Ontario Teachers' Pension Plan, the Ontario Teachers' Federation and the Ontario Government, from POLLARA, a national research firm. We are conducting a survey of pension plan members, which will provide these groups with information about members' preferences. Would you mind if I asked you some questions? All of your responses will be kept completely confidential. (IF ASKED: On average, the survey takes about 10 minutes to complete.)

(IF YES) Thank you (PROCEED TO QUESTION 1)
(IF NO) When is a better time for me to call back? (SCHEDULE APPOINTMENT UP TO AND INCLUDING May 2; MONDAY-FRIDAY 5pm-9pm; SATURDAY 9am-5pm; NO SUNDAY CALLS.)

B. Objective 1: To determine the level of awareness and understanding among Plan members about the current level of benefits and contributions.

To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF BENEFITS)

1. Members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (95%)
   Unaware ..... (4%)
   Don't know ..... (<1%)
   Refused ..... (<1%)

2. The monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (87%)
   Unaware ..... (12%)
   Don't know ..... (1%)
   Refused ..... (<1%)

3. The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made. (IF NECESSARY: Were you aware or unaware of this?)

Aware	(74%)
Unaware	(25%)
Don't know	(1%)
Refused	(<1%)

(END RANDOMIZATION OF STATEMENTS)

Now I'd like to ask you about some other pension issues.

4. Prior to my call, were you aware or unaware that the pension plan does not provide dental and other health benefit coverage to retirees?

Aware	(68%)
Unaware	(31%)
Don't know	(1%)
Refused	(<1%)

5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?

Aware	(63%)
Unaware	(36%)
Don't know	(1%)
Refused	(<1%)

6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible? (IF REQUIRED: Similar to an RRSP, you can deduct your total pension contributions from your net income on page 3 of your tax return.)

Aware	(66%)
Unaware	(32%)
Don't know	(1%)
Refused	(<1%)

7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?

Higher	(23%)
Lower	(10%)
About the same amount	(38%)
Don't know	(29%)
Refused	(<1%)

8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan? (READ LIST - STOP AFTER ANSWER IS GIVEN)

Less than 5%	(5%)
5% to less than 7%	(10%)
7% to less than 9%	(17%)
9% to less than 12%	(24%)
12% to less than 15%	(4%)
15% or more	(5%)
Don't know (DO NOT READ)	(35%)
Refused (DO NOT READ)	(<1%)

9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

Up	(77%)
Down	(1%)
Stay the same	(13%)
Don't know	(9%)
Refused	(<1%)

C. Objective 2: To measure plan members' preferences in terms of increased contributions vs. decreased benefits, if a future valuation shows an increased shortfall.

Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These increases are required to keep pension provisions for future service at current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

10. (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

Higher	(27%)
Lower	(3%)
Same	(64%)
Don't know	(6%)
Refused	(<1%)

11. (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

Yes	(47%)
No	(49%)
Don't know	(4%)
Refused	(<1%)

Although all members are guaranteed pensions, the Ontario Teachers' Pension Plan, like many other pension plans, is facing funding challenges. Decisions may need to be made about whether to further increase members' contributions beyond the increases we have just discussed. The alternative to increasing contributions is reducing the level of pension provisions that will be earned from the time the change is made until members retire.

(IF RESPONDENT ASKS: By law, such changes could not affect the pensions provided to those who have already retired. Likewise, pension provisions that have already been earned by working members could not be reduced. Such changes could only be applied into the future.)

12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(5%)
10.0%	(15%)
10.1%-11.0%	(7%)
11.1%-12.0%	(20%)
12.1%-13.0%	(8%)
13.1%-14.0%	(2%)
14.1%-15.0%	(27%)
Greater than 15.0%	(3%)
Don't know	(12%)
Refused	(1%)
Mean (%):	12.34
Median (%):	12.0
Mode (%):	15.0

13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12. EXCLUDE IF Q12 = "Don't know" or "Refused") If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than (INSERT RESPONSE FROM Q12) of your salary in order to keep all pension provisions at current levels?

(IF ASKED: Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These changes are required to keep the pension provisions for future service at their current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

In favour	(36%)
Not in favour	(53%)
Don't know	(10%)
Refused	(<1%)

Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level. Please tell me whether you would be in favour or not in favour of each of the following changes. How about: (READ - RANDOMIZE ORDER OF PROVISIONS)

(IF REQUIRED, READ: Please keep in mind that by law, these changes could not affect the pensions provided to those who have already retired. Likewise, current pension provisions that have already been earned by working members could not be reduced.)

14. Increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it. (IF ASKED: Members can currently retire with unreduced monthly pension payments when their age plus years of service equals eighty-five, or when they reach the age of 65.) (IF ASKED: Discussions would take place between the OTF and the government to decide on a transition period.)

In favour	(41%)
Not in favour	(57%)
Don't know	(2%)
Refused	(<1%)

15. Reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

In favour	(32%)
Not in favour	(57%)
Don't know	(11%)
Refused	(<1%)

16. Making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

In favour	(51%)
Not in favour	(43%)
Don't know	(5%)
Refused	(<1%)

(END OF QUESTION RANDOMIZATION)

17. We've just discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. When I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan. (RANDOMIZE ORDER OF CHANGES)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

Decreasing your monthly pension for future service by 10%	(11%)
Increasing the eighty-five factor to a ninety factor	(37%)
Providing flexibility for the cost-of-living adjustment	(44%)
Don't know (DO NOT READ OR RANDOMIZE)	(3%)
Refused (DO NOT READ OR RANDOMIZE)	(4%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

18. Which potential change are you least willing to have made? (REPEAT REMAINING CHANGES AS REQUIRED)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act)

Decreasing your monthly pension for future service by 10%	(37%)
Increasing the eighty-five factor to a ninety factor	(41%)
Providing flexibility to the cost-of-living adjustment	(16%)
Don't know (DO NOT READ OR RANDOMIZE)	(3%)
Refused (DO NOT READ OR RANDOMIZE)	(2%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(6%)
10.0%	(11%)
10.1%-11.0%	(8%)
11.1%-12.0%	(22%)
12.1%-13.0%	(8%)
13.1%-14.0%	(3%)
14.1%-15.0%	(29%)
Greater than 15.0%	(5%)
Don't know	(8%)
Refused	(1%)
Mean (%):	12.55
Median (%):	12.0
Mode (%):	15.0

D. Objective 3: To identify the views of sub-groups of members who may have different perspectives based on their circumstances.

20. (ASK IF AGE + YEARS OF CREDIT = >74) Which one of the following three statements best represents your own viewpoint: (RANDOMIZE ORDER OF STATEMENTS - REPEAT AS REQUIRED)

    If pension contributions increase to more than about eleven percent of your salary, you will consider retiring earlier than planned, even if your pension provisions remain the same ..... (13%)

    If the pension provisions you will earn in future years are reduced you will consider retiring earlier than planned, even if your contribution rates remain the same ..... (19%)

    You are unlikely to consider retiring earlier than planned as a result of changes to your future pension provisions and contribution rates. .. (55%)

    Don't know (DO NOT READ OR RANDOMIZE) ..... (10%)
    Refused (DO NOT READ OR RANDOMIZE) ..... (4%)

21. Do you work at an elementary school, a secondary school, or at another organization?

    Elementary ..... (63%)
    Secondary ..... (33%)
    Other ..... (4%)
    Refused ..... (<1%)

We have come to the end of our survey. Thank you very much for your time, we appreciate your participation. (IF RESPONDENT WANTS TO LEARN MORE ABOUT THE ISSUES DISCUSSED IN THE SURVEY: Would you like me to give you some web site addresses that provide further detail on the pension plan issues discussed in this survey? (IF YES): www.otpp.com; www.otffeo.on.ca)

22. Gender (INTERVIEWER-RECORDED)

    Male ..... (26%)
    Female ..... (74%)

23. Employment type (SAMPLE)

    Full-time ..... (83%)
    Part-time ..... (7%)
    Occasional ..... (10%)

24. Employer type (SAMPLE)

English School Board	(94%)
French School Board	(5%)
Other	(1%)

25. Years of credit (SAMPLE)

0-4.9	(26%)
5-9.9	(28%)
10-14.9	(15%)
15-19.9	(14%)
20-24.9	(8%)
25 And Over	(9%)

26. Career Status Grouping (SAMPLE)

Newer members (0-4.9 years)	(26%)
Newer members (5-9.9 years)	(26%)
Mid-career members (10-14.9 years)	(12%)
Mid-career members (15-21.9 years)	(7%)
Older members (within 10 years of an unreduced pension)	(14%)
Older members (within 5 years of an unreduced pension)	(12%)
Older members (eligible for unreduced pension)	(5%)

27. Other years of credit collapse (SAMPLE)

0-6.9 years of actual credit	(36%)
7-14.9 years of actual credit	(27%)
15-21.9 years of actual credit	(7%)
Within 10 years or less of an unreduced pension	(14%)
Within 5 years of unreduced pension	(12%)
Already eligible unreduced pension	(5%)

29. Age (SAMPLE)

Under 35 Yrs	(24%)
35-44	(32%)
45-54	(31%)
55-64	(13%)
65 And Over	(<1%)

30. Urban/Rural (SAMPLE)

Urban	(86%)
Rural	(14%)

31. Administration (SAMPLE)

Administration	(6%)
Non-Administration	(94%)

Appendix B: LTIP interview schedule

LTIP interview schedule

- Some individuals contained in member records were receiving long-term income protection (LTIP) through their employer. A total of 21 individuals on LTIP completed this survey. These results have been excluded from the findings presented in other sections of this report because the mandate of the study was to understand contribution and benefit issues among active, *contributing* pension plan members.
- A total of 21 individuals on LTIP completed the survey, the results of which are presented in the following interview schedule. Due to the extremely small sample size, results should not be generalized to all individuals on LTIP.

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Interview Schedule

A. Introduction

Good morning/afternoon/evening. May I please speak with (MEMBER NAME)?

IF AVAILABLE- CONTINUE
IF NOT AVAILABLE - SCHEDULE APPOINTMENT TO CALL BACK (IF NECESSARY, READ FIRST 2 SENTENCES OF PREAMBLE BELOW AND SCHEDULE CALL-BACK)

(WHEN MEMBER IS ON LINE) Good morning/afternoon/evening. My name is ( ) and I am calling on behalf of the Ontario Teachers' Pension Plan, the Ontario Teachers' Federation and the Ontario Government, from POLLARA, a national research firm. We are conducting a survey of pension plan members, which will provide these groups with information about members' preferences. Would you mind if I asked you some questions? All of your responses will be kept completely confidential. (IF ASKED: On average, the survey takes about 10 minutes to complete.)

(IF YES) Thank you (PROCEED TO QUESTION 1)
(IF NO) When is a better time for me to call back? (SCHEDULE APPOINTMENT UP TO AND INCLUDING May 2; MONDAY-FRIDAY 5pm-9pm; SATURDAY 9am-5pm; NO SUNDAY CALLS.)

LTIP Plan
(n=21)

B. Objective 1: To determine the level of awareness and understanding among Plan members about the current level of benefits and contributions.

To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF BENEFITS)

1. Members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (100%)

2. The monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries. (IF NECESSARY: Were you aware or unaware of this?)

   Aware ..... (86%)
   Unaware ..... (10%)
   Don't know ..... (5%)

	LTIP Plan (n=21)
3. The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made. (IF NECESSARY: Were you aware or unaware of this?)	
Aware	(76%)
Unaware	(24%)

(END RANDOMIZATION OF STATEMENTS)

Now I'd like to ask you about some other pension issues.

4. Prior to my call, were you aware or unaware that the pension plan does not provide dental and other health benefit coverage to retirees?	
Aware	(71%)
Unaware	(24%)
Don't know	(5%)
5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?	
Aware	(48%)
Unaware	(38%)
Don't know	(14%)
6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible? (IF REQUIRED: Similar to an RRSP, you can deduct your total pension contributions from your net income on page 3 of your tax return.)	
Aware	(67%)
Unaware	(29%)
Don't know	(5%)
7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?	
Higher	(29%)
Lower	(5%)
About the same amount	(24%)
Don't know	(43%)

	LTIP Plan (n=21)

8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan? (READ LIST - STOP AFTER ANSWER IS GIVEN)

Less than 5%	(5%)
5% to less than 7%	(<1%)
7% to less than 9%	(14%)
9% to less than 12%	(24%)
12% to less than 15%	(<1%)
15% or more	(<1%)
Don't know (DO NOT READ)	(52%)
Refused (DO NOT READ)	(5%)

9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

Up	(43%)
Down	(10%)
Stay the same	(24%)
Don't know	(24%)

C. Objective 2: To measure plan members' preferences in terms of increased contributions vs. decreased benefits, if a future valuation shows an increased shortfall.

Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These increases are required to keep pension provisions for future service at current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

10. (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

Higher	(22%)
Lower	(11%)
Same	(56%)
Don't know	(11%)

	LTIP Plan (n=21)

11. (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

Yes	(42%)
No	(42%)
Don't know	(17%)

Although all members are guaranteed pensions, the Ontario Teachers' Pension Plan, like many other pension plans, is facing funding challenges. Decisions may need to be made about whether to further increase members' contributions beyond the increases we have just discussed. The alternative to increasing contributions is reducing the level of pension provisions that will be earned from the time the change is made until members retire.

(IF RESPONDENT ASKS: By law, such changes could not affect the pensions provided to those who have already retired. Likewise, pension provisions that have already been earned by working members could not be reduced. Such changes could only be applied into the future.)

12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't Know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(14%)
10.0%	(14%)
10.1%-11.0%	(10%)
11.1%-12.0%	(10%)
12.1%-13.0%	(10%)
13.1%-14.0%	(<1%)
14.1%-15.0%	(14%)
Greater than 15.0%	(5%)
Don't know	(14%)
Refused	(10%)
Mean (%):	11.03
Median (%):	11.50
Mode (%):	10.00

	LTIP Plan (n=21)

13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12. EXCLUDE IF Q12 = "Don't know" or "Refused") If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than (INSERT RESPONSE FROM Q12) of your salary in order to keep all pension provisions at current levels?

(IF ASKED: Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate. These changes are required to keep the pension provisions for future service at their current levels. By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

In favour	(62%)
Not in favour	(31%)
Don't know	(8%)

Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level. Please tell me whether you would be in favour or not in favour of each of the following changes. How about: (READ - RANDOMIZE ORDER OF PROVISIONS)

(IF REQUIRED, READ: Please keep in mind that by law, these changes could not affect the pensions provided to those who have already retired. Likewise, current pension provisions that have already been earned by working members could not be reduced.)

14. Increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it. (IF ASKED: Members can currently retire with unreduced monthly pension payments when their age plus years of service equals eighty-five, or when they reach the age of 65.) (IF ASKED: Discussions would take place between the OTF and the government to decide on a transition period.)

In favour	(48%)
Not in favour	(48%)
Refused	(5%)

	LTIP Plan (n=21)

15. Reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

In favour	(19%)
Not in favour	(43%)
Don't know	(33%)
Refused	(5%)

16. Making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

In favour	(62%)
Not in favour	(29%)
Don't know	(5%)
Refused	(5%)

(END OF QUESTION RANDOMIZATION)

17. We've just discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. When I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan. (RANDOMIZE ORDER OF CHANGES)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.)

Decreasing your monthly pension for future service by 10%	(14%)
Increasing the eighty-five factor to a ninety factor	(33%)
Providing flexibility for the cost-of-living adjustment	(33%)
Don't know (DO NOT READ OR RANDOMIZE)	(10%)
Refused (DO NOT READ OR RANDOMIZE)	(10%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

LTIP Plan (n=21)

18. Which potential change are you least willing to have made? (REPEAT REMAINING CHANGES AS REQUIRED)

(IF REQUIRED: By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act)

Decreasing your monthly pension for future service by 10%	(53%)
Increasing the eighty-five factor to a ninety factor	(21%)
Providing flexibility to the cost-of-living adjustment	(21%)
Don't know (DO NOT READ OR RANDOMIZE)	(5%)

(IF REQUIRED: READ FULL WORDING FROM Q14 TO Q16 AGAIN)

19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%. (INTERVIEWER PROBE IF "Don't Know": "Please provide your best estimate.") (IF RESPONDENT GIVES A RANGE: "Please provide the maximum total percentage you would be willing to contribute, rather than a range.")

Less than 10.0%	(10%)
10.0%	(5%)
10.1%-11.0%	(14%)
11.1%-12.0%	(14%)
12.1%-13.0%	(10%)
14.1%-15.0%	(10%)
Greater than 15.0%	(10%)
Don't know	(24%)
Refused	(5%)
Mean (%):	11.51
Median (%):	12.00
Mode (%):	12.00

LTIP Plan (n=21)

D. Objective 3: To identify the views of sub-groups of members who may have different perspectives based on their circumstances.

20. (ASK IF AGE + YEARS OF CREDIT = >74) Which one of the following three statements best represents your own viewpoint: (RANDOMIZE ORDER OF STATEMENTS - REPEAT AS REQUIRED)

    If pension contributions increase to more than about eleven percent of your salary, you will consider retiring earlier than planned, even if your pension provisions remain the same ..... (21%)
    If the pension provisions you will earn in future years are reduced you will consider retiring earlier than planned, even if your contribution rates remain the same ..... (7%)
    You are unlikely to consider retiring earlier than planned as a result of changes to your future pension provisions and contribution rates. .. (36%)
    Don't know (DO NOT READ OR RANDOMIZE) ..... (21%)
    Refused (DO NOT READ OR RANDOMIZE) ..... (14%)

21. Do you work at an elementary school, a secondary school, or at another organization?

    Elementary ..... (43%)
    Secondary ..... (33%)
    Other ..... (14%)
    Refused ..... (10%)

We have come to the end of our survey. Thank you very much for your time, we appreciate your participation. (IF RESPONDENT WANTS TO LEARN MORE ABOUT THE ISSUES DISCUSSED IN THE SURVEY: Would you like me to give you some web site addresses that provide further detail on the pension plan issues discussed in this survey? (IF YES): www.otpp.com; www.otffeo.on.ca)

22. Gender (INTERVIEWER-RECORDED)

    Male ..... (29%)
    Female ..... (71%)

23. Employment type (SAMPLE)

    Full-time ..... (100%)

	LTIP Plan (n=21)
24. Employer type (SAMPLE)	
English School Board	(71%)
French School Board	(24%)
Other	(5%)
25. Years of credit (SAMPLE)	
5-9.9	(10%)
10-14.9	(14%)
15-19.9	(19%)
20-24.9	(29%)
25 And Over	(29%)
26. Career Status Grouping (SAMPLE)	
Newer members (5-9.9 years)	(5%)
Mid-career members (10-14.9 years)	(5%)
Mid-career members (15-21.9 years)	(10%)
Older members (within 10 years of an unreduced pension)	(10%)
Older members (within 5 years of an unreduced pension)	(29%)
Older members (eligible for unreduced pension)	(43%)
27. Other years of credit collapse (SAMPLE)	
7-14.9 years of actual credit	(10%)
15-21.9 years of actual credit	(10%)
Within 10 years or less of an unreduced pension	(10%)
Within 5 years of unreduced pension	(29%)
Already eligible unreduced pension	(43%)
29. Age (SAMPLE)	
Under 35 Years	(5%)
35-44	(10%)
45-54	(19%)
55-64	(62%)
65 And Over	(5%)
30. Urban/Rural (SAMPLE)	
Urban	(67%)
Rural	(33%)
31. Administration (SAMPLE)	
Non-Adminsitration	(100%)

About POLLARA

- POLLARA Inc., a leading-edge Canadian public opinion and marketing research firm, helps its clients improve their performance through strategic research designed and analyzed by consultants who are experts in their fields. Drawing on the talents of employees located in six Canadian cities, POLLARA provides a full range of research services to leading global, national and local companies and to public and non-profit sector organizations. These services include quantitative and qualitative research and counsel in the areas of public affairs/public policy, employee satisfaction, customer value/satisfaction, new product development, advertising testing and tracking, branding, and consumer demand and pricing models.

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2007 Teachers Survey.pdf

The contribution and benefit preferences of active members of the Ontario Teachers' Pension Plan

Prepared for:

OTF/FEO ONTARIO TEACHERS' PENSION PLAN Ontario

by:

POLLARA

June 2007

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I. Objectives

- The goals of this survey of active, contributing members of the Ontario Teachers' Pension Plan are:
  - → To determine the level of awareness and understanding among plan members about the current level of benefits and contributions.
  - → To measure plan members' preferences in terms of increased contributions and decreased benefits, if a future valuation shows an increased shortfall.
  - → To identify the views of sub-groups of members who may have a different perspective based on their circumstances (i.e., years from retirement).
- In order to achieve these objectives, the study required a sound research methodology that would accurately measure member preferences. This methodology is detailed in the following pages.

II. Methodology

- A total of 2,820 telephone interviews were conducted with OTPP members between April 11th and May 2nd, 2007.

A. Questionnaire development

- The survey questionnaire and methodology were developed by POLLARA in conjunction with the Ontario Teachers' Pension Plan (OTPP), the Ontario Teachers' Federation (OTF), and the Ontario Government, through a series of meetings held between September 11th and December 11th, 2006.

- In addition, six focus groups, four English (Brampton & Toronto) and two French (Ottawa), were conducted in October 2006 with early, mid, and late career members to facilitate the overall design of the questionnaire. An important goal of the focus groups was to identify pension terminology and explanations that members do or do not understand to determine the appropriate level of communication for the questionnaire. A draft copy of *Let's talk about the future of your pension*, a primer created by the OTPP, OTF, and Ontario Government, was also assessed during these sessions, and member feedback was used to refine the document in a way that would make it most easily understood.

II. Methodology, continued

A. Questionnaire development, continued

- As well, using a draft questionnaire, POLLARA conducted 17 pre-test interviews with OTPP members in November, 2006. After further questionnaire refinement, a second pre-test of 46 English and French members was conducted in March, 2007. A stratified sample was used for both pre-tests, to ensure a good mix of members. The questionnaire tested well in both cases and after each pre-test modifications were made to facilitate respondent comprehension of survey topics.

B. Member communications

- *Let's talk about the future of your pension*, a primer created by the OTPP, OTF, and Ontario Government was mailed to all pension plan members the week of March 19th, 2007. The primer informed members that they may be called to participate in a survey and encouraged them to familiarize themselves with the document and to keep it available for reference in case they were contacted. The resource was also included on OTPP's website.

- In addition to the primer, in December, 2006, the Ontario Teachers' Federation released, *What About My Teachers' Pension?*, a multi-media educational resource that was sent to local presidents for distribution to schools. The resource was also included on OTF's website, and was included as a link on OTPP's website.

II. Methodology, continued

B. Member communications, continued

- Members were also informed about the survey through OTPP's 2006 Annual Report, its 2006 Report to Members, its 2007 Annual Meeting, detailed Q&As on its website, and its Pensionwise newsletter.

C. Interviewing

- Pension plan members were telephoned by POLLARA weekdays between 5 p.m. and 9 p.m. and on Saturday between 9 a.m. and 5 p.m. If the time of the initial call was deemed inconvenient or if members wanted additional time to review reference material on the survey topics, the researcher offered to schedule an appointment to call back.
- Of the 3,636 eligible members POLLARA spoke with, 78% completed the survey and 22% declined to participate. The survey response rate, calculated according to the Marketing Research and Intelligence Association (MRIA) formula, was 40%.
- All interviewers were briefed on the project's background and questionnaire. 100% of interviews were supervised, and 10% were monitored, as per MRIA guidelines.

II. Methodology, continued

D. Sampling and data weighting

- The source of the survey sample was OTPP current member records.
- Additional interviews were conducted among member sub-groups in order to accurately understand the views of these segments. Specific groups to be oversampled were selected in consultation with POLLARA, by OTPP, OTF, and the Ontario Government.
- The overall results of the survey were weighted to reflect the actual distribution of members within these sub-groups.

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II. Methodology, continued

D. Sampling and data weighting, continued

- The following table shows the distribution of interviews and the corresponding margins of error. Overall results are accurate to within ±1.8%, nineteen times out of twenty. Sub-sample results have a larger margin of error.

		Actual # of interviews	Weighted # of interviews	Margin of error (%)
Career groupings	Newer members (0 – 4.9 years credit)	481	255	±4.4
	Newer members (5 – 9.9 years credit)	398	259	±4.9
	Mid-career members (10 – 14.9 years credit)	361	120	±5.1
	Mid-career members (15 – 21.9 years credit)	353	65	±5.1
	Older members (within 10 years of an unreduced pension)	431	137	±4.7
	Older members (within 5 years of an unreduced pension)	392	117	±4..9
	Older members (eligible for unreduced pension)	404	47	±4.7
Gender	Female	2077	736	±2.1
	Male	743	264	±3.6
Employment type	Full-time	2082	829	±2.1
	Part-time	354	73	±5.1
	Occasional	384	98	±4.9
Employer type	District school board – English	2345	938	±2.0
	District school board – French	429	48	±4.6
	Other	46	14	±14.3
TOTAL		**2,820***	**1,000***	**±1.8**

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*Sub-group interviews do not add up to the total due to overlap.

III. Key findings

Key findings

In summary, the study indicates that members would be willing to contribute an average maximum of 12.3% in order to preserve their current level of benefits. This amount is 1.3 percentage points above the increase scheduled to take effect in 2009 that will bring contributions to an average of 11%. Six-in-ten members say they would be willing to contribute *more* than 11% of their before-tax income to preserve their current level of benefits, while 27% would be willing to contribute *up to* 11%. If members were contributing their maximum, the benefit change they would be most willing to support is making cost-of-living increases to future retirees' pensions flexible (supported by 51%). They would be least supportive of reducing monthly pension for future service by about 10% (supported by 32%).

A. Awareness of current level of benefits and contributions

- Overall, the majority of pension plan members have a high level of aided awareness of all pension plan provisions and issues tested in this study. Almost all are aware of the 85 factor and that their monthly pension amount is based on a formula. Another three-quarters are aware of the inflation protection provision. Of the other pension plan issues tested, the majority of members are aware of the lack of dental and health coverage, tax deductibility of contributions, and government matching of pension plan contributions.
  - → Awareness is widespread among all career groupings. Understandably, newer members are less aware of all provisions/issues than those approaching retirement.

Key findings, continued

- Almost two-fifths of members say that the $750,000 value of the average teacher's pension at retirement, in today's dollars, is about the same as they expected. Almost one-quarter say that this amount is more than they expected, and one-in-ten report that they thought the value was higher than $750,000. Three-in-ten are unsure.
  - → Almost two-fifths of members in all career groupings report that this amount is about what they expected.
- Members' awareness of the amount they currently contribute to their pension plan is not very widespread. Specifically, only one-quarter of members correctly name 9% to 11.9% as the amount of their before-tax salary they contribute to the pension plan. In addition, more than one-third of all members say they do not know how much they contribute.
  - → Interestingly, members who are already eligible for retirement are as likely as newer members to say they don't know how much they contribute to their pension plan.
- Awareness of scheduled contribution increases is widespread, with over three-quarters of members understanding that their contributions will increase over the next two years.
  - → Newer members are least likely to be aware of these increases, whereas members already eligible for unreduced pension are most likely to be aware.
- When scheduled contribution increases are outlined for members who expect an increase, almost two-thirds see the amounts as in line with their expectations, whereas, about a quarter feel they are higher than expected. Only 3% say that the increases are less than expected.

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Key findings, continued

- When prompted, half of those who had *not* expected a contribution increase recall hearing or seeing information about the change.

B. Preferences in terms of increased contributions and decreased benefits

Increased contributions

- If a future valuation shows an increased shortfall, pension plan members would be willing to contribute a maximum of 12.3% in order to maintain current pension provisions. Six-in-ten members are willing to have contributions *exceed* 11%, while 27% are willing to contribute *up to* 11%.
  - → Average maximum pension plan contributions are very consistent across career groupings, ranging from 11.9% to 12.8%.
  - → Part-time workers (13.0%) are willing to contribute the most in order to maintain their current pension provisions, whereas French school board members are willing to contribute slightly less (10.7%) than average.

Key findings, continued

- Members whose maximum contribution is 8.1% or higher were asked if they would be willing to contribute more than their maximum if a commitment was made to reduce contributions to eight percent if the pension plan shows a surplus in future. More than half do not support such a move. However, over one-third of members would increase their maximum contribution under this circumstance.
- After three potential benefit changes are reviewed with members, the average maximum contribution increases by 0.3 (to total 12.6%) and the proportion of members willing to contribute more than 11% increases by seven percentage points (to total 67%). Average maximum pension plan contributions are again very consistent across career groupings (12.1% to 13.0%).

Decreased benefits

- Respondents were asked to imagine that their contributions are at the maximum amount they would be willing to contribute in order to keep all pension provisions at current levels. They were then read a list of changes that could be made to future pension provisions in order to keep contributions from rising beyond this level.

Key findings, continued

- The most popular option is making cost-of-living adjustments flexible, which is supported by more than one-half of pension plan members.
  - → Newer members are more likely than older members to be in favour of this choice. Occasional workers and French school board members are also more likely to favour this option.
- Two-fifths of all members are in favour of increasing the 85 factor to 90.
  - → Unlike the cost-of-living option, those already eligible for an unreduced pension are more likely to be in favour of this plan than newer members.
- One-third of plan members are in favour of reducing monthly pension for future service by about 10%.
  - → Newer members are more likely to be in favour of this option than older members, as are occasional workers, and French school board members.
- When asked to identify the one potential benefit change they prefer, the most popular response (provided by more than two-fifths) is making cost-of-living adjustment flexible.
  - → This is the preferred option for five of seven career groupings and rural residents.
- The second most preferred benefit change is increasing the 85 factor to 90, chosen by almost four-in-ten members.
  - → Only members within five years of unreduced pension and those already eligible for unreduced pension name this change as their top option.

Key findings, continued

- Reducing monthly pension for future service by 10% is preferred by just over one-in-ten members, ranking this option third.
  - → Preference for this option is consistently low among all career groupings, with no more than 13% naming this change as their preferred option.
- When members are asked for their least preferred option amongst all three, increasing the 85 factor to 90 comes out on top, with two-fifths saying is it the least desirable option.
  - → This option is the least favourite choice for five of the seven career groupings.
  - → Reducing monthly pension for future service by 10% ranks as the second least preferred option overall (chosen by 37%). This is the number one least preferred option among members within five years of unreduced pension and those already eligible to retire.
  - → Less than one-fifth of members rank flexible cost-of-living adjustments as their third least preferred option. Only those already eligible for unreduced pension rank this option as their second least preferred option.

All of the findings in this summary are analyzed in greater detail within the remaining sections of this report.

IV. Level of awareness and understanding among plan members about the current level of benefits and contributions

Awareness and understanding of pension plan benefits and contributions

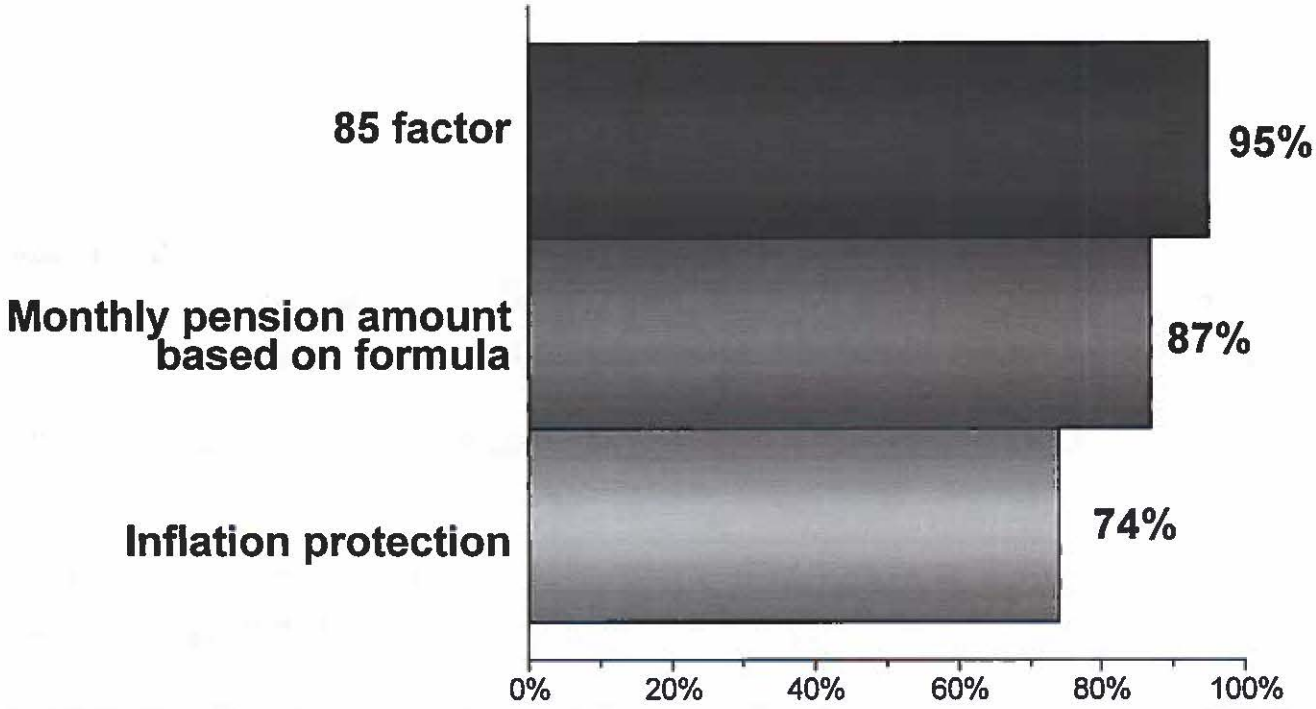
- Prior to delving into pension plan members' preferences in terms of contributions and benefits, a number of questions were asked of members at the onset of the questionnaire, the goals of which were:

  → To understand members' aided awareness of their pension provisions.

  → To ensure that survey respondents were aware of current provisions before they answered more detailed questions concerning their benefit and contribution preferences.

Majority of pension plan members aware of each current pension plan provision tested

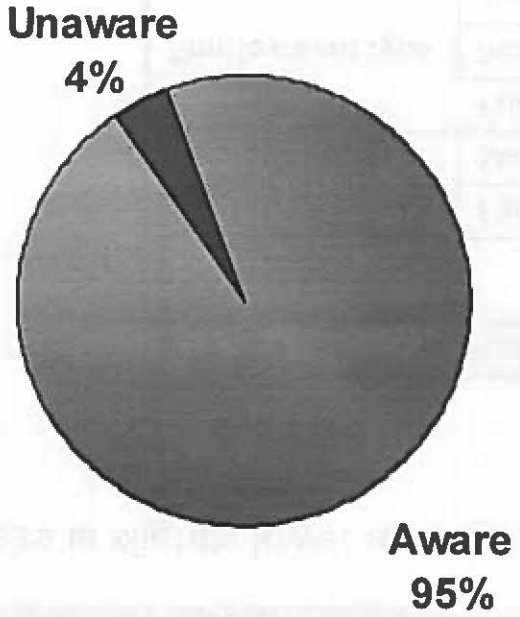
- Of the three pension plan provisions tested, members are most likely to be aware of the 85 factor, followed by the use of a formula to determine the amount of their pension, and inflation protection.



Qs 1-3. To start, I'd like to read you a list of some of the provisions of your pension plan. Please tell me whether or not you were aware of each provision prior to my call. How about: (RANDOMIZE ORDER OF PROVISIONS)

Almost all pension plan members aware of 85 factor

- Almost all pension plan members (95%) are aware that they can retire with unreduced monthly pension payments when their age plus number of teaching years equals 85, or when they reach the age of 65.
- Awareness is slightly lower among newer members (90%) and close to unanimous among older members, those within 10 years of unreduced pension eligibility, and those already eligible for unreduced pension.



Career groupings	Aware (%)
Newer members (0 – 4.9)	90%
Newer members (5 – 9.9)	95%
Mid-career members (10 – 14.9)	98%
Mid-career members (15 – 21.9)	99%
Older members (within 10 yrs unreduced pension)	98%
Older members (within 5 yrs unreduced pension)	99%
Older members (eligible for unreduced pension)	99%

Q1. Please tell me whether or not you were aware of each provision prior to my call. How about: members can retire with unreduced monthly pension payments when their age plus the length of their teaching career equals eighty-five, or when they reach the age of 65.

POLLARA

Large majorities of all member segments aware of 85 factor

- Awareness is slightly lower among occasionally employed pension plan members (85%).

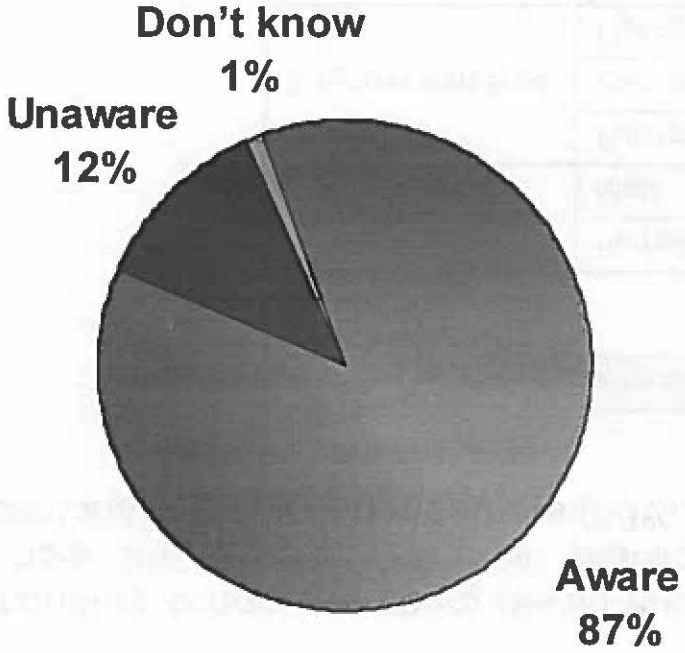
Member segment		Aware (%)
OVERALL		95%
Gender	Female	96%
	Male	95%
Employment type	Full-time	97%
	Part-time	95%
	Occasional	85%
Employer type	District school board – English	96%
	District school board – French	92%
Place of work	Elementary	95%
	Secondary	96%
Urban/Rural	Urban	95%
	Rural	97%

Less likely

POLLARA

Large majority of pension plan members aware of how their monthly pension is determined

- Almost nine-in-ten pension plan members (87%) are aware that their basic annual pension is determined through a formula.
- Awareness increases as members approach retirement, with almost three-quarters (71%) of newer members (0-4.9 years) to almost all (99%) unreduced pension eligible members being aware.



Career groupings	Aware (%)
Newer members (0 – 4.9)	71%
Newer members (5 – 9.9)	89%
Mid-career members (10 – 14.9)	93%
Mid-career members (15 – 21.9)	94%
Older members (within 10 yrs unreduced pension)	96%
Older members (within 5 yrs unreduced pension)	95%
Older members (eligible for unreduced pension)	99%

POLLARA

Q2. Please tell me whether or not you were aware of each provision prior to my call. How about: the monthly pension amount paid to a retiree is based on a formula that multiplies two percent by the years of service by the average of their best five annual salaries.

Awareness that pension amount based on formula widespread among all member segments

- Secondary school members (94%) and men (93%) are slightly more aware than average of how the amount of their pension is determined. Awareness is lowest among occasionally employed members (66%).

Member segment		Aware (%)
OVERALL		87%
Gender	Female	85%
	Male	93%
Employment type	Full-time	90%
	Part-time	84%
	Occasional	66%
Employer type	District school board – English	87%
	District school board – French	83%
Place of work	Elementary	84%
	Secondary	94%
Urban/Rural	Urban	87%
	Rural	91%

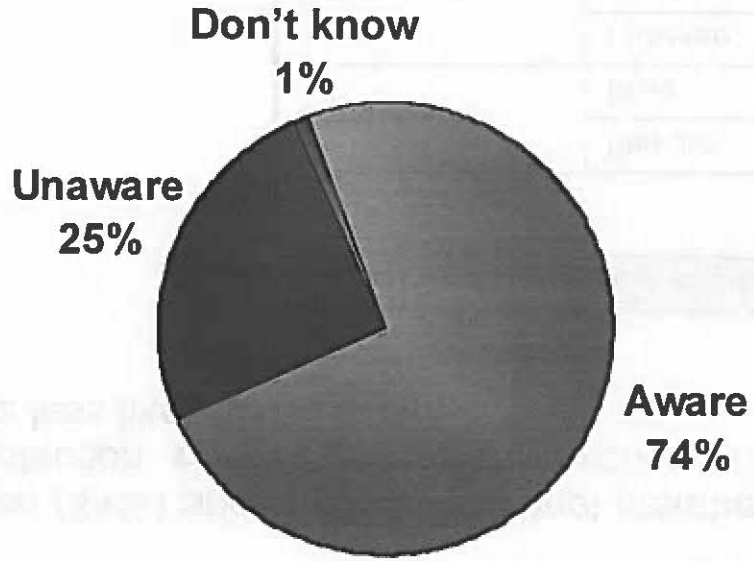
More likely

Less likely

POLLARA

Almost three-quarters of pension plan members aware that monthly payments are protected against inflation

- Almost three-quarters of pension plan members (74%) are aware that monthly pension payments are protected against inflation.
- Again, awareness is higher among members approaching retirement. Just over half (52%) of newer members (0-4.9 years of credit) are aware of inflation protection, compared to 85% of mid-career members (15-21.9 years). Unreduced pension eligible members are almost unanimously aware that a guaranteed cost-of-living adjustment is made (97%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	52%
Newer members (5 – 9.9)	68%
Mid-career members (10 – 14.9)	80%
Mid-career members (15 – 21.9)	85%
Older members (within 10yrs unreduced pension)	92%
Older members (within 5 yrs unreduced pension)	93%
Older members (eligible for unreduced pension)	97%

POLLARA

Q3. Please tell me whether or not you were aware of each provision prior to my call. How about: The monthly pension payments made to retirees are protected against inflation. In other words, a guaranteed cost-of-living adjustment is made.

Inflation protection awareness widespread among most member segments

- Men (84%) and secondary school members (81%) are more likely to be aware of inflation protection, whereas occasional workers (55%) and French school board members (61%) are less likely to be aware.

Member segment		Aware (%)
OVERALL		74%
Gender	Female	70%
	Male	84%
Employment type	Full-time	76%
	Part-time	71%
	Occasional	55%
Employer type	District school board – English	75%
	District school board – French	61%
Place of work	Elementary	70%
	Secondary	81%
Urban/Rural	Urban	73%
	Rural	78%

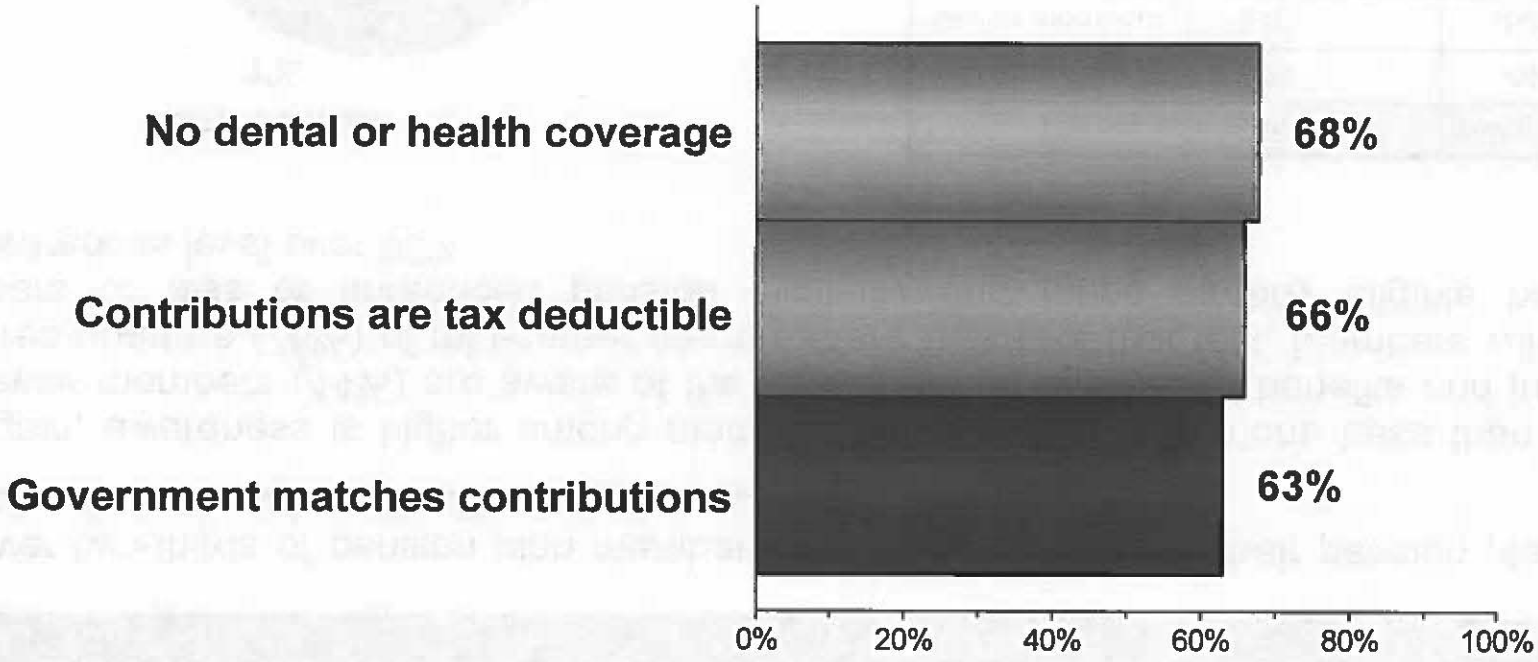
More likely

Less likely

POLLARA

Majority of pension plan members are aware of other aspects of their pension plan

- In addition to testing awareness of plan provisions, members' aided awareness of three other aspects of their plan were explored.
- More than six-in-ten members are aware of the lack of dental and health coverage in the plan, followed by the tax deductibility of their contributions, and contribution matching by the Ontario government.

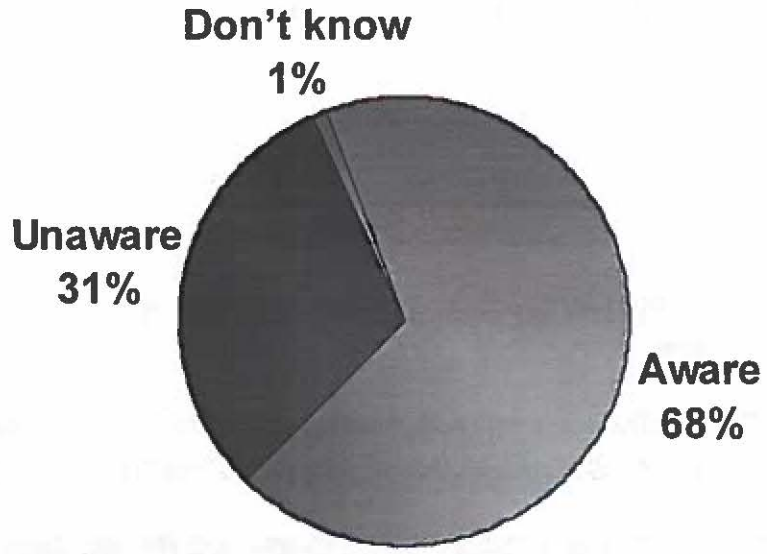


POLLARA

Qs 4-6. Now I'd like to ask you about some other pension issues. Prior to my call, were you aware or unaware…

More than two-thirds of members aware that pension plan does not provide dental and health benefit coverage

- Over two-thirds of pension plan members (68%) are aware that their pension plan does not include dental and health benefit coverage.
- Again, awareness is higher among members approaching retirement. Less than half of newer members (44%) are aware of the lack of dental and health benefits and just over three-quarters (76%) of mid-career members are aware of that fact. Members within five years or less of unreduced pension eligibility and those already eligible have an awareness level over 90%.



Career groupings	Aware (%)
Newer members (0 – 4.9)	44%
Newer members (5 – 9.9)	62%
Mid-career members (10 – 14.9)	75%
Mid-career members (15 – 21.9)	76%
Older members (within 10 yrs unreduced pension)	82%
Older members (within 5 yrs unreduced pension)	92%
Older members (eligible for unreduced pension)	98%

Q4. Prior to my call, were you aware or unaware that the pension plan <u>does not</u> provide dental and other health benefit coverage to retirees?

POLLARA

Majority of all member segments aware of lack of dental and health benefits

- Occasional workers (52%), French school board members (56%), and part-time workers (60%) are less likely to be aware that their pension plan lacks dental and health coverage.

Member segment		Aware (%)
OVERALL		68%
Gender	Female	68%
	Male	69%
Employment type	Full-time	71%
	Part-time	60%
	Occasional	52%
Employer type	District school board – English	69%
	District school board – French	56%
Place of work	Elementary	67%
	Secondary	71%
Urban/Rural	Urban	68%
	Rural	68%

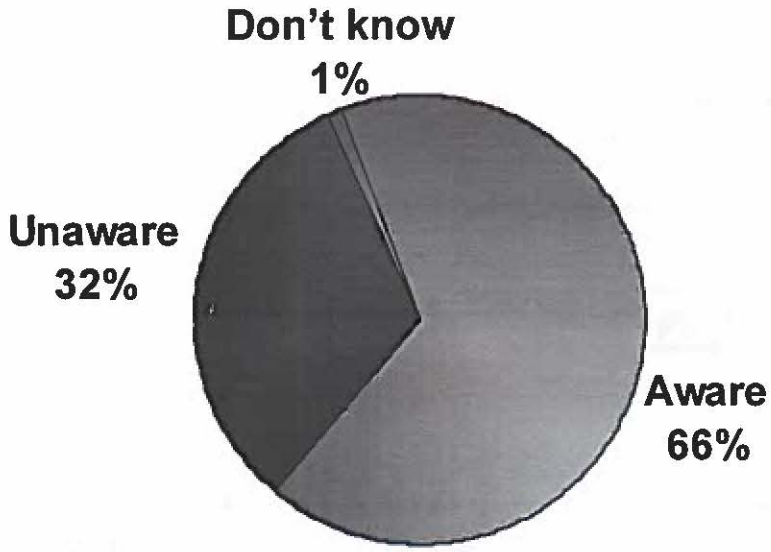
More likely

Less likely

POLLARA

Two-thirds of pension plan members aware that money contributed to pension plan is tax deductible

- Two-thirds of pension plan members (66%) are aware that their pension plan contributions are tax deductible.
- Newer members, once again, are least aware (55%), whereas members already eligible for unreduced pension score the highest (81%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	55%
Newer members (5 – 9.9)	65%
Mid-career members (10 – 14.9)	71%
Mid-career members (15 – 21.9)	76%
Older members (within 10 yrs unreduced pension)	73%
Older members (within 5 yrs unreduced pension)	71%
Older members (eligible for unreduced pension)	81%

Q6. And prior to my call, were you aware or unaware that the money you contribute to your pension plan is tax deductible?

POLLARA

Majority of all member segments aware of tax deductibility of contributions

- Awareness of tax deductibility is higher among men (73%) and secondary school workers (73%), and lower among occasional workers (56%) and French school board members (59%).

Member segment		Aware (%)
OVERALL		66%
Gender	Female	64%
	Male	73%
Employment type	Full-time	68%
	Part-time	64%
	Occasional	56%
Employer type	District school board – English	66%
	District school board – French	59%
Place of work	Elementary	63%
	Secondary	73%
Urban/Rural	Urban	66%
	Rural	66%

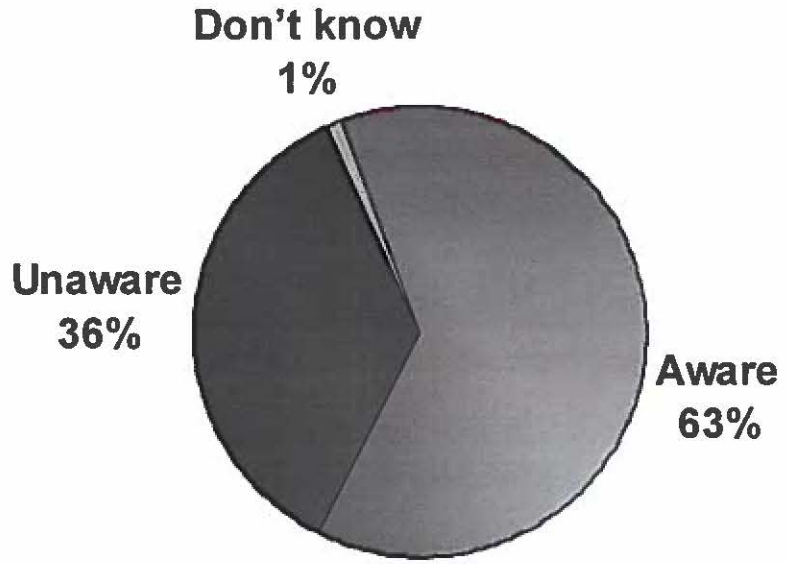
More likely

Less likely

POLLARA

Majority of pension plan members aware that the Ontario government matches members' contributions to the pension plan

- Almost two-thirds of pension plan members (63%) are aware that the Ontario government matches members' contributions to their pension plan.
- Again, awareness is lowest among newer members (45%) and highest among those who are eligible for an unreduced pension (81%).



Career groupings	Aware (%)
Newer members (0 – 4.9)	45%
Newer members (5 – 9.9)	60%
Mid-career members (10 – 14.9)	70%
Mid-career members (15 – 21.9)	78%
Older members (within 10 yrs unreduced pension)	73%
Older members (within 5 yrs unreduced pension)	78%
Older members (eligible for unreduced pension)	81%

Q5. And were you aware or unaware that the Ontario government matches members' contributions to the pension plan?

POLLARA

Majority of most member segments aware government matches contributions

- Men (77%) and secondary school members (73%) are more likely to be aware of contribution matching. French school board members (41%), occasional (44%) and part-time (53%) workers, women (58%), and elementary school members (58%) are all less likely to be aware of contribution matching.

Member segment		Aware (%)
OVERALL		63%
Gender	Female	58%
	Male	77%
Employment type	Full-time	66%
	Part-time	53%
	Occasional	44%
Employer type	District school board – English	65%
	District school board – French	41%
Place of work	Elementary	58%
	Secondary	73%
Urban/Rural	Urban	63%
	Rural	67%

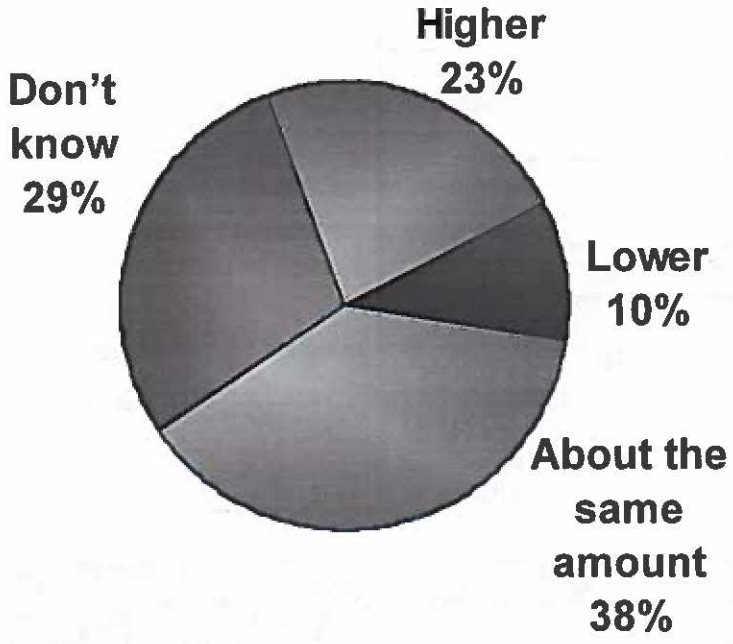
More likely

Less likely

POLLARA

More than six-in-ten members expect the value of the average teacher's pension to be $750,000 or less

- Members were told that the average teacher's pension at retirement, in today's dollars, is valued at $750,000. Almost two-fifths (38%) of pension plan members say this is about what they expected, whereas, 23% think it is higher than expected. Only one-in-ten (10%) say it is lower than expected and almost three-in-ten (29%) don't know.
- Expectations are very consistent between career groups. Between 21% and 24% of each group say the $750,000 is higher than expected, 9%-15% say lower, and 36%-42% say about the same as expected.



Career groupings	Higher (%)	Lower (%)	Same (%)	DK (%)
Newer members (0 – 4.9)	24%	9%	36%	31%
Newer members (5 – 9.9)	22%	9%	39%	29%
Mid-career members (10 – 14.9)	24%	9%	38%	30%
Mid-career members (15 – 21.9)	21%	10%	41%	28%
Older members (within 10 yrs unreduced pension)	21%	15%	37%	28%
Older members (within 5 yrs unreduced pension)	22%	8%	42%	28%
Older members (eligible for unreduced pension)	22%	9%	40%	29%

POLLARA

Q7. The value of the average teacher's pension at retirement, in today's dollars, is $750,000. Is this amount higher, lower or about the same amount that you expected?

Majority of all member segments say pension value same or higher than they expected

- Part-time (30%) and occasional (31%) workers are more likely than average to say that the $750,000 value of the average teachers' pension is higher than they expected. Men (47%) are more likely to say that $750,000 is about the same as expected.

Member segment		Higher	Lower	Same	DK
OVERALL		23%	10%	38%	29%
Gender	Female	25%	8%	35%	32%
	Male	16%	13%	47%	23%
Employment type	Full-time	21%	10%	40%	29%
	Part-time	30%	5%	30%	34%
	Occasional	31%	11%	30%	28%
Employer type	District school board – English	23%	9%	39%	29%
	District school board – French	19%	12%	35%	35%
Place of work	Elementary	25%	9%	36%	30%
	Secondary	19%	10%	41%	29%
Urban/Rural	Urban	23%	9%	38%	29%
	Rural	20%	13%	37%	30%

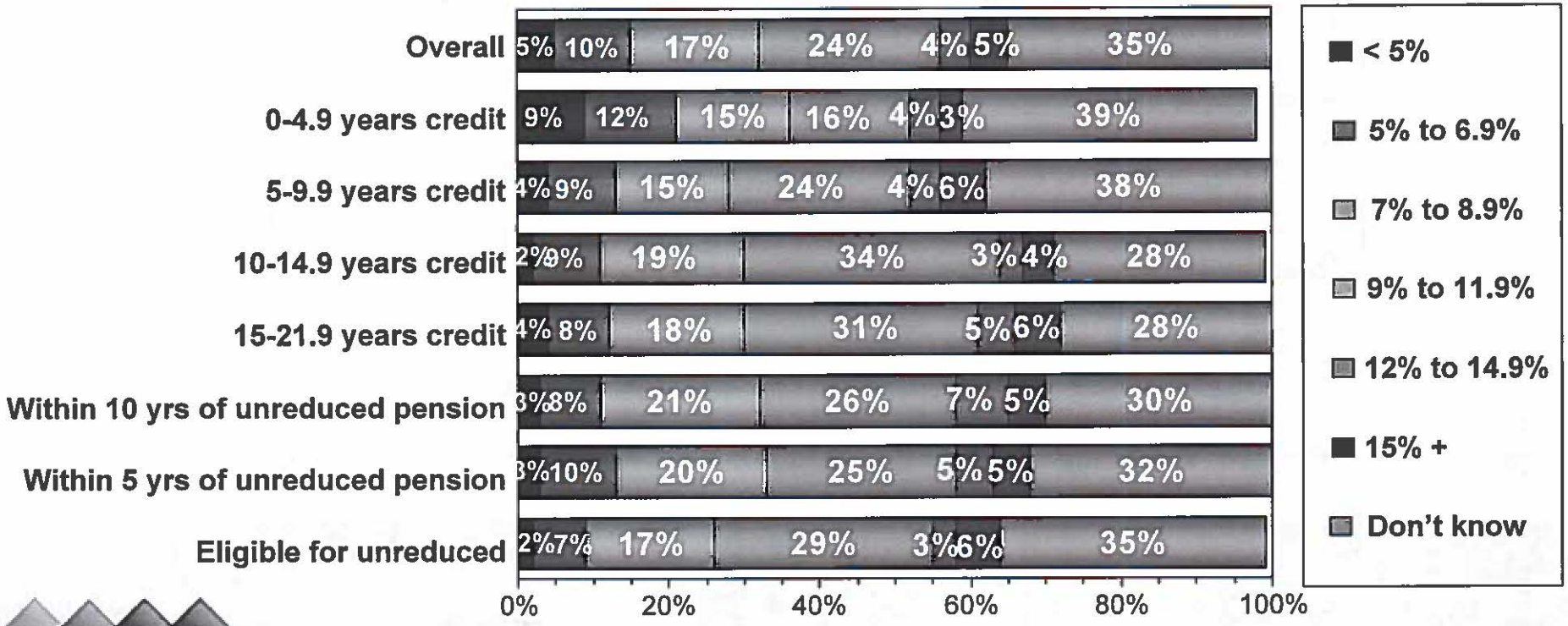
More likely

Less likely

POLLARA

Almost one-quarter of members believe they contribute 9% to less than 12% of their before-tax salary to their pension plan

- Almost one-quarter (24%) of members correctly believe that they contribute 9% to less than 12% of their before-tax salary to their pension plan. Over one-third (35%) do not know how much they are contributing.
- Interestingly, members who are already eligible for an unreduced pension (35%) are almost as likely to say they don't know how much they contribute to their pension plan as newer members (39%). However, newer members are less likely to have chosen the correct percentage range (16% vs. 29%) than their older counterparts.



Q8. To the best of your knowledge, approximately what percentage of your before-tax salary do you currently contribute to your pension plan?

Men more likely then women to know their contribution amounts

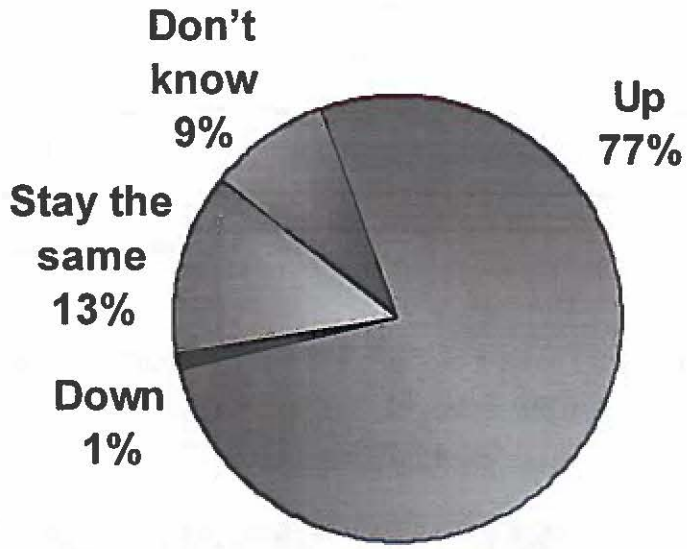
- Men (32%) are more likely than women (21%) to be aware of current contribution levels. An additional 40% of women say they do not know how much they contribute, while occasional workers (43%) are most likely to provide this response.

Member segment		<5%	5-6.9%	7-8.9%	9-11.9%	12-14.9%	15%+	DK
OVERALL		5%	10%	17%	24%	4%	5%	35%
Gender	Female	5%	9%	15%	21%	4%	5%	40%
	Male	5%	11%	23%	32%	5%	3%	21%
Employment type	Full-time	4%	9%	18%	25%	5%	5%	33%
	Part-time	4%	10%	17%	23%	3%	4%	39%
	Occasional	12%	12%	15%	14%	3%	1%	43%
Employer type	District school board – English	5%	10%	17%	25%	4%	5%	35%
	District school board – French	5%	13%	19%	19%	6%	4%	32%
Place of work	Elementary	5%	10%	16%	20%	4%	5%	39%
	Secondary	4%	9%	20%	32%	5%	4%	26%

More likely Less likely

More than three-quarters of members understand that pension plan contributions are scheduled to increase over the next two years

- Three-quarters (77%) of pension plan members understand that contributions are scheduled to increase over the next two years. Only 1% believe that contributions are scheduled to decrease, and another 13% believe they will stay the same. One-in-ten (9%) do not know.
- Newer members (69%) are least likely to know that contributions are scheduled to increase. Members already eligible for unreduced pension are most likely to know that contributions are increasing (85%).



Career groupings	Up (%)	Down (%)	Same (%)
Newer members (0 – 4.9)	69%	1%	16%
Newer members (5 – 9.9)	77%	2%	13%
Mid-career members (10 – 14.9)	80%	1%	13%
Mid-career members (15 – 21.9)	82%	<1%	11%
Older members (within 10 yrs unreduced pension)	81%	<1%	10%
Older members (within 5 yrs unreduced pension)	77%	2%	14%
Older members (eligible for unreduced pension)	85%	1%	9%

Q9. To the best of your knowledge, is the amount you currently contribute to your pension plan scheduled to go up, down, or stay the same in the next two years?

POLLARA

Majority of every member segment believes contributions scheduled to increase

- Occasional and part-time workers are less likely than average to believe that contributions are scheduled to increase (59% and 72%) over the next two years and occasional workers are also more likely to say they don't know (21%).

Member segment		Up (%)	Down (%)	Same (%)	DK (%)
OVERALL		77%	1%	13%	9%
Gender	Female	76%	1%	13%	9%
	Male	78%	1%	13%	8%
Employment type	Full-time	79%	1%	12%	7%
	Part-time	72%	1%	14%	13%
	Occasional	59%	1%	19%	21%
Employer type	District school board – English	77%	1%	13%	9%
	District school board – French	74%	2%	21%	4%
Place of work	Elementary	76%	1%	13%	10%
	Secondary	78%	1%	14%	7%
Urban/Rural	Urban	76%	1%	13%	10%
	Rural	79%	2%	13%	6%

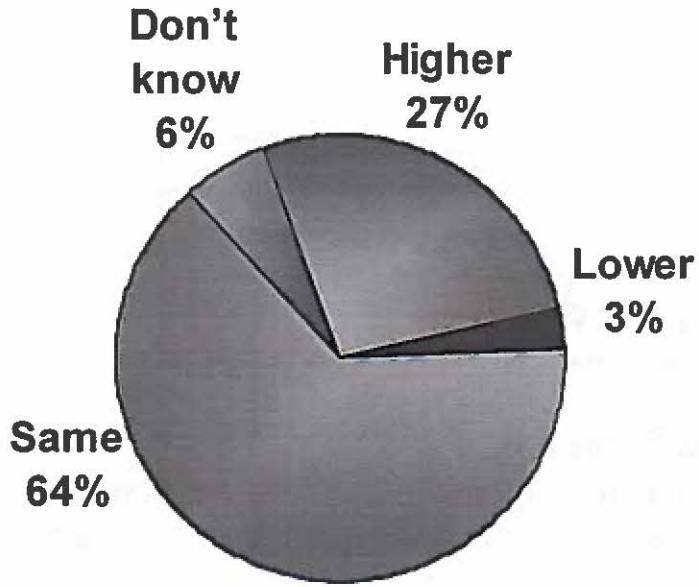
More likely

Less likely

POLLARA

Scheduled contribution increases are in line with expectations of the majority of members who are expecting an increase

- Among the 77% of members who expect an increase, almost two-thirds (64%) say the amount of future increases is what they expected. A further 27% feel that the future increases are higher than expected and only 3% expected smaller increases in the next two years.
- In most cases about two-thirds of members in each career grouping feel that the future increases are as they expected.



Career groupings	Higher (%)	Lower (%)	Same (%)	DK (%)
Newer members (0 – 4.9)	26%	3%	64%	8%
Newer members (5 – 9.9)	29%	4%	59%	8%
Mid-career members (10 – 14.9)	29%	1%	66%	4%
Mid-career members (15 – 21.9)	24%	3%	70%	4%
Older members (within 10 yrs unreduced pension)	23%	4%	67%	5%
Older members (within 5 yrs unreduced pension)	27%	3%	62%	7%
Older members (eligible for unreduced pension)	26%	3%	67%	4%

Q10. Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate… (IF EXPECTING INCREASE) Are these increases higher, lower, or about the same amount that you had expected?

POLLARA

Majority of all member segments say amount of scheduled increases is same as expected

- Rural residents (70%) are most likely to report that the proposed increases are as expected.

Member segment		Higher (%)	Lower (%)	Same (%)
OVERALL		27%	3%	64%
Gender	Female	27%	3%	63%
	Male	27%	4%	66%
Employment type	Full-time	27%	3%	63%
	Part-time	22%	5%	66%
	Occasional	23%	2%	66%
Employer type	District school board – English	27%	3%	64%
	District school board – French	24%	6%	63%
Place of work	Elementary	26%	3%	63%
	Secondary	27%	3%	66%
Urban/Rural	Urban	28%	3%	63%
	Rural	20%	3%	70%

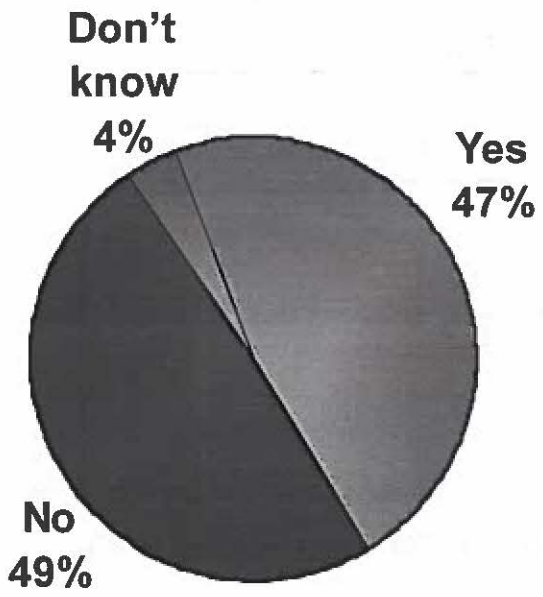
More likely

Less likely

POLLARA

Of those who do not expect contributions to increase, almost half recall seeing or hearing about increases when prompted

- Among the 23% of members who believe that contributions are going down (1%), staying the same (13%), or who are unsure (9%), almost one-half (47%) remember hearing or seeing about contribution increases, when prompted.
- Less than two-in-five newer members (38%) recall seeing or hearing such information, whereas, two-thirds (67%) of those approaching unreduced pension eligibility or those already eligible (67%) recall hearing or seeing about contribution increases.



Career groupings	Yes (%)
Newer members (0 – 4.9)	38%
Newer members (5 – 9.9)	38%
Mid-career members (10 – 14.9)	53%
Mid-career members (15 – 21.9)	57%
Older members (within 10 yrs unreduced pension)	58%
Older members (within 5 yrs unreduced pension)	67%
Older members (eligible for unreduced pension)	67%

Q11. Currently, members contribute an average of ten percent of their before-tax salary to the pension plan. This will rise to an average of ten point three percent in 2008. There is a further scheduled increase in 2009 that will bring members' contributions to about eleven percent. A financial review next year may change this rate… (IF EXPECTING DECREASE/STAY THE SAME/DON'T KNOW/REFUSED) Do you recall seeing or hearing anything about these increases?

POLLARA

French school board members and men are more likely to recall seeing or hearing about increases

- Of those who do not expect contributions to increase, French school board members (58%), men (52%), and rural members (52%) are all more likely to recall hearing or seeing information about contribution increases, when prompted. Occasional workers (35%) are less likely.

Member segment		'Yes' (%)
OVERALL		47%
Gender	Female	45%
	Male	52%
Employment type	Full-time	50%
	Part-time	44%
	Occasional	35%
Employer type	District school board – English	47%
	District school board – French	58%
Place of work	Elementary	45%
	Secondary	51%
Urban/Rural	Urban	46%
	Rural	52%

More likely

Less likely

POLLARA

V. Pension plan members' preferences in terms of increased contributions and decreased benefits, if a future valuation shows an increased shortfall

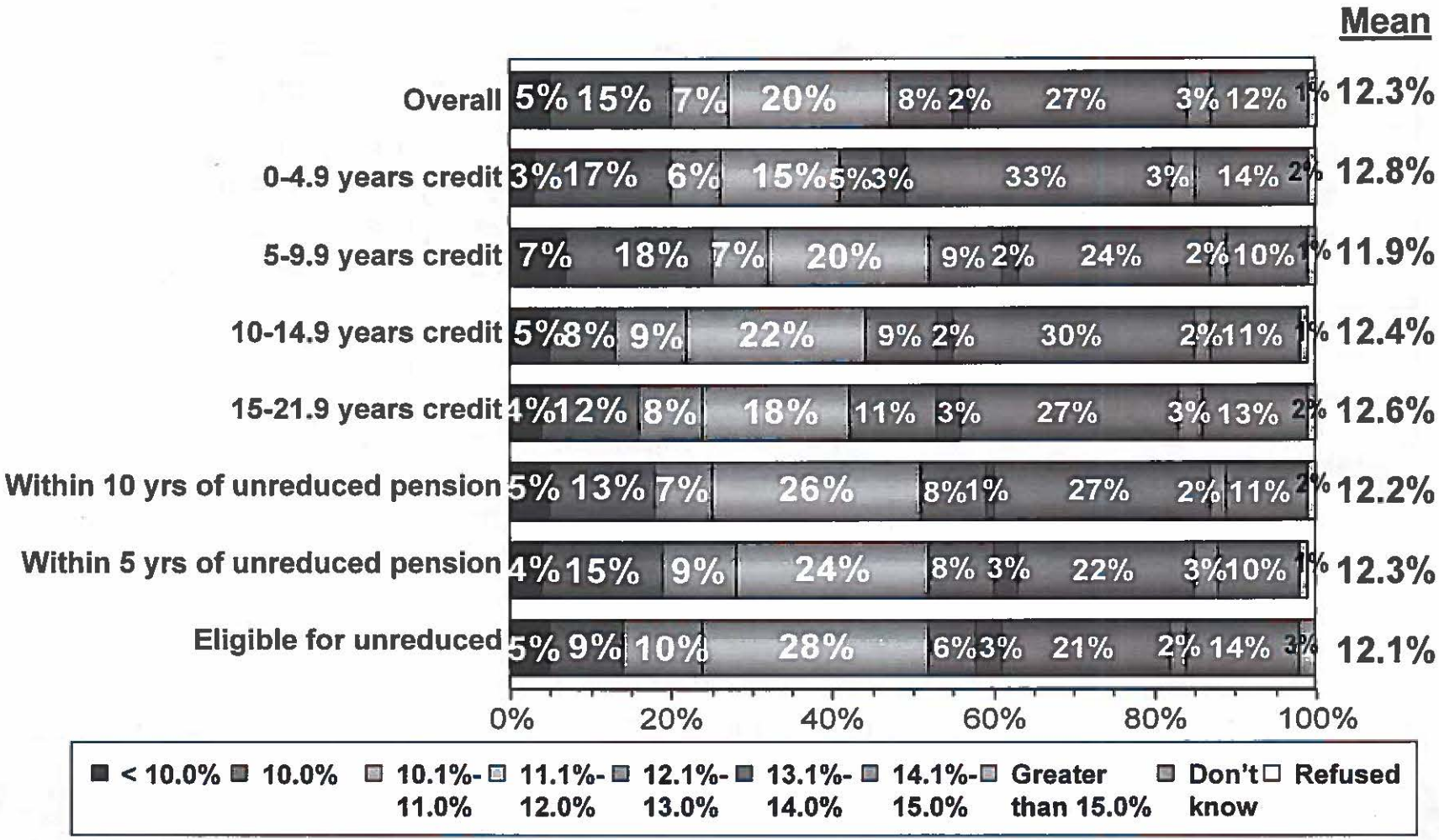
Members willing to contribute average maximum of 12.3% to maintain current pension provisions

- Prior to reviewing potential benefit changes, members were asked to identify the maximum contribution they would be willing to make in order to maintain current pension provisions.
  - → Members are willing to contribute an average (mean) maximum of 12.3% in order to maintain current pension provisions. Six-in-ten (60%) members are willing to have contributions exceed 11%, while more than one-quarter (27%) are willing to contribute up to 11%. The median for this result is 12%.
  - → Interestingly, maximum contribution rates are similar across career groupings (mean of 11.9%-12.8%), as detailed on the next page.
  - → Members were asked the same question after reviewing potential benefit changes and their mean response was 0.3 points higher (12.6%). This result is discussed in greater detail on page 58.

Contribution	Members (%)
Less than 10.0%	5%
10.0%	15%
10.1%-11.0%	7%
11.1%-12.0%	20%
12.1%-13.0%	8%
13.1%-14.0%	2%
14.1%-15.0%	27%
Greater than 15.0%	3%
Don't know	12%

POLLARA

Average maximum contribution, in order to maintain current pension provisions, is remarkably similar across career groupings



Q12. First, thinking into the future, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

Maximum contributions fairly consistent among all member segments

- Part-time workers (13%) have a slightly higher average maximum contribution rate, whereas French school board members are willing to contribute slightly less than average (10.7%).

Member segment		Mean
OVERALL		12.3%
Gender	Female	12.4%
	Male	12.2%
Employment type	Full-time	12.3%
	Part-time	13.0%
	Occasional	12.6%
Employer type	District school board – English	12.4%
	District school board – French	10.7%
Place of work	Elementary	12.4%
	Secondary	12.2%
Urban/Rural	Urban	12.3%
	Rural	12.6%

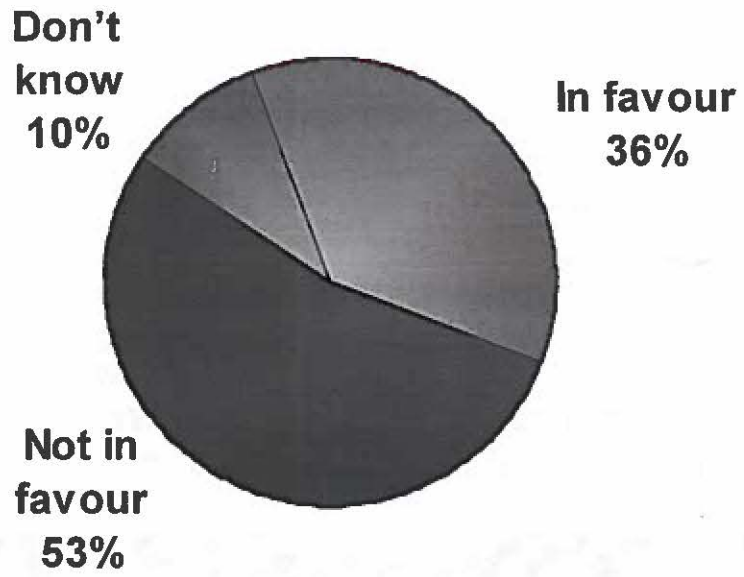
More likely

Less likely

POLLARA

More than one-third would increase their maximum contribution if reduced to 8% with future surplus; 53% opposed

- Members whose maximum contribution was 8.1% or higher (79% of members) were asked if they would be willing to contribute more if a commitment was made to reduce contributions to eight percent if the pension plan shows a surplus in future. Over one-third of members (36%) would increase their maximum contribution under this circumstance, including 45% of those already eligible for unreduced pension. More than half (53%) do not support such a move.
- There is a greater willingness to exceed one's maximum contribution among those approaching retirement.



Career groupings	In favour (%)	Not In favour (%)
Newer members (0 – 4.9)	32%	53%
Newer members (5 – 9.9)	38%	54%
Mid-career members (10 – 14.9)	36%	56%
Mid-career members (15 – 21.9)	36%	51%
Older members (within 10 yrs unreduced pension)	38%	55%
Older members (within 5 yrs unreduced pension)	39%	52%
Older members (eligible for unreduced pension)	45%	46%

Q13. (ASK ONLY TO THOSE WHO RESPONDED 8.1% OR MORE TO Q12.) If a commitment was made to reduce members' contributions to eight percent if the pension plan shows a surplus in the future, would you be in favour or not in favour of increasing pension plan contributions to more than [RESPONSE FROM Q12] of your salary in order to keep all pension provisions at current levels?

POLLARA

Support and opposition to increasing maximum contribution for future reduction is fairly consistent across member segments

- Rural members (30%) are slightly less likely to be in favour of increasing their maximum contribution with a reduction to eight percent in the event of a surplus.

Member segment		In favour (%)	Not in favour (%)
OVERALL		36%	53%
Gender	Female	36%	53%
	Male	37%	55%
Employment type	Full-time	36%	52%
	Part-time	32%	57%
	Occasional	38%	57%
Employer type	District school board – English	36%	53%
	District school board – French	39%	50%
Place of work	Elementary	37%	53%
	Secondary	34%	54%
Urban/Rural	Urban	37%	53%
	Rural	30%	55%

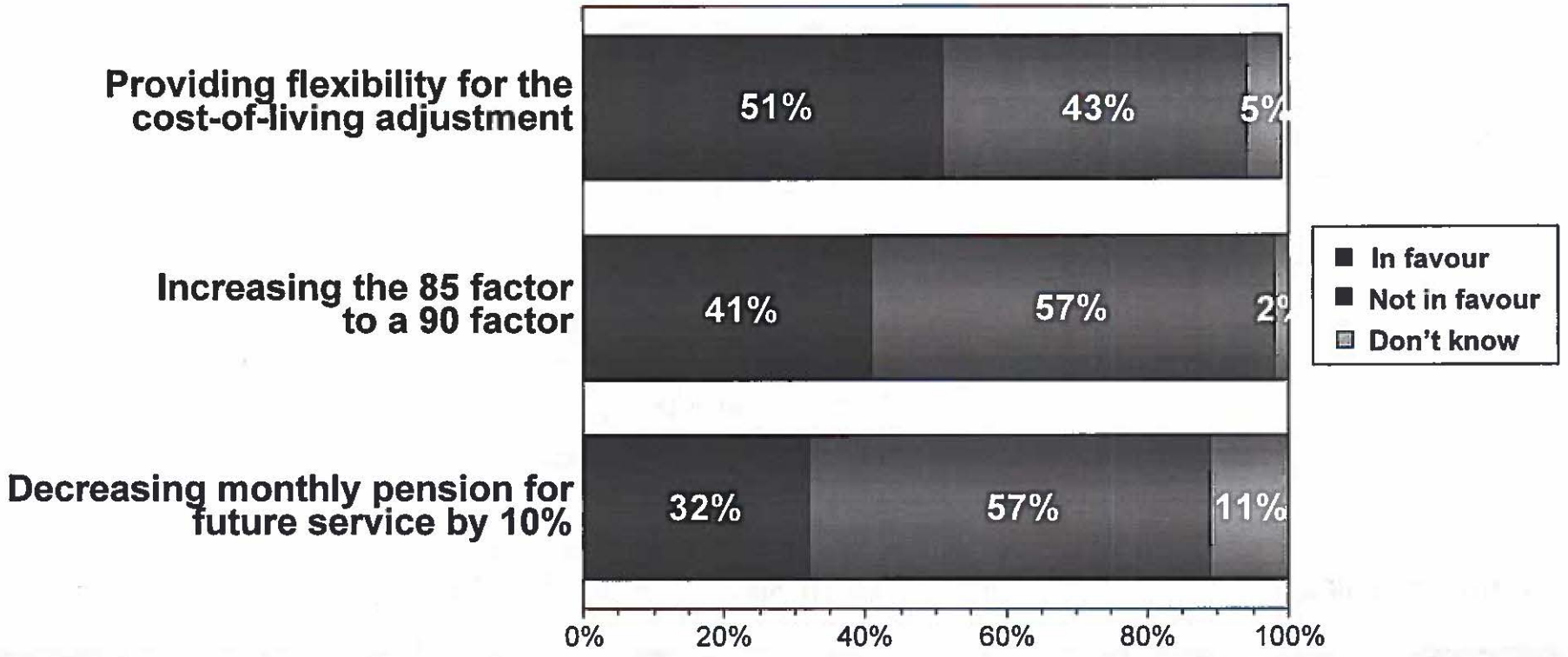
More likely

Less likely

POLLARA

Support for benefit changes to keep contributions from rising beyond maximum ranges from 32% to 51%

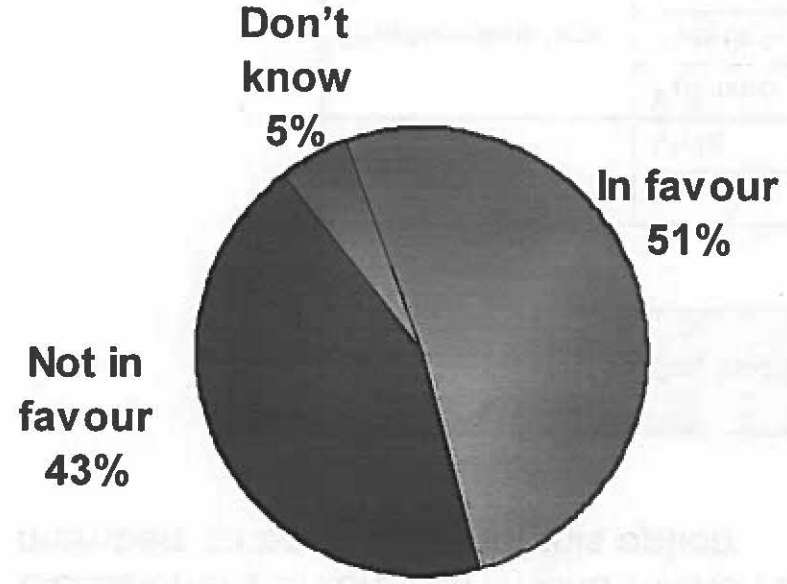
- If members were contributing their maximum, support for potential benefit changes would range from 32% (for reducing pensions by 10%) to 51% (for making the cost-of-living adjustment flexible).



Qs 14-16.Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about… (RANDOMIZE ORDER)

One-half of pension plan members would be in favour of making cost-of-living increases to future retirees' pension flexible

- One-half (51%) of pension plan members are in favour of making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible.
- This option is the favourite among newer members, with 59% being in favour. Support decreases as members approach retirement.



Career groupings	In favour (%)	Not in favour (%)
Newer members (0 – 4.9)	59%	33%
Newer members (5 – 9.9)	59%	37%
Mid-career members (10 – 14.9)	51%	45%
Mid-career members (15 – 21.9)	45%	49%
Older members (within 10 yrs unreduced pension)	43%	53%
Older members (within 5 yrs unreduced pension)	38%	57%
Older members (eligible for unreduced pension)	37%	61%

Q16. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about making cost-of-living increases to future retirees' pension flexible when the pension plan is under-funded, with the understanding that the full cost-of-living adjustment would be restored when possible?

POLLARA

Support for flexible cost-of-living adjustment fairly consistent among member segments

- Occasional workers (66%) and French board members (56%) are more likely than other members to be in favour of this option.

Member segment		In favour (%)	Not in favour (%)
OVERALL		51%	43%
Gender	Female	51%	43%
	Male	51%	45%
Employment type	Full-time	50%	46%
	Part-time	52%	40%
	Occasional	66%	27%
Employer type	District school board – English	51%	44%
	District school board – French	56%	29%
Place of work	Elementary	53%	42%
	Secondary	48%	47%
Urban/Rural	Urban	51%	43%
	Rural	53%	43%

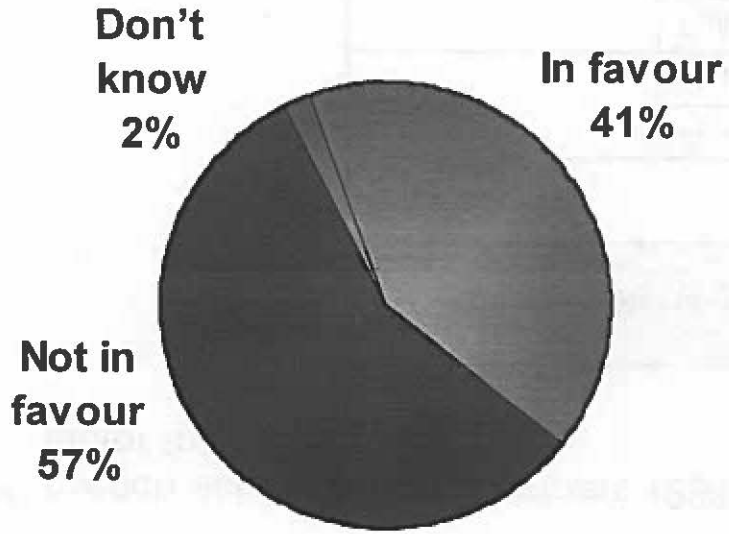
More likely

Less likely

POLLARA

Two-fifths of members support increasing 85 factor to 90 to keep contributions from rising beyond their maximum; more than half disagree

- Over two-fifths (41%) of pension plan members are in favour of increasing the 85 factor to 90, meaning that in the future members would work an extra two and a half years to quality for unreduced pension in order to retire before age 65.
- Members who are already eligible for unreduced pension are significantly more likely to be in favour of switching to a 90 factor (74%). Newer members are second most likely to be in favour (44%), followed by older members within 5 years of unreduced pension (42%). No more than 38% of members are in favour of switching to a 90 factor among the other groupings.



Career groupings	In favour (%)	Not In favour (%)
Newer members (0 – 4.9)	44%	52%
Newer members (5 – 9.9)	38%	59%
Mid-career members (10 – 14.9)	36%	64%
Mid-career members (15 – 21.9)	34%	63%
Older members (within 10 yrs unreduced pension)	36%	62%
Older members (within 5 yrs unreduced pension)	42%	56%
Older members (eligible for unreduced pension)	74%	22%

Q14. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about increasing the eighty-five factor to ninety, meaning that in the future members would work an extra two and a half years to qualify for an unreduced monthly pension in order to retire before age 65? If this situation were to arise, there would be some type of grand fathering. If you have already reached your eighty-five factor, you would not lose it.

POLLARA

More than half of every member segment not in favour of changing 85 factor to 90

- French school board members (29%) are least likely to be in favour of increasing the 85 factor to 90.

Member segment		In favour (%)	Not in favour (%)
OVERALL		41%	57%
Gender	Female	41%	56%
	Male	41%	58%
Employment type	Full-time	40%	57%
	Part-time	43%	55%
	Occasional	44%	51%
Employer type	District school board – English	41%	56%
	District school board – French	29%	70%
Place of work	Elementary	42%	55%
	Secondary	38%	60%
Urban/Rural	Urban	41%	57%
	Rural	43%	54%

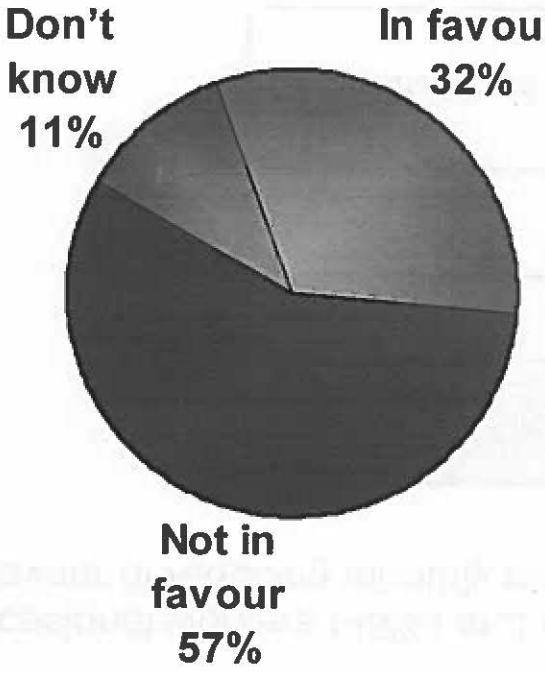
More likely

Less likely

POLLARA

Almost one-third of pension plan members are in favour of reducing monthly pension for future service by about 10%; more than half disagree

- Almost one-third (32%) of pension plan members are in favour of reducing monthly pension for future service by about 10%.
- Newer members (41% and 34%) are more supportive than other career groupings of reducing monthly pension for future service by about 10%.



Career groupings	In favour (%)	Not in favour (%)
Newer members (0 – 4.9)	41%	47%
Newer members (5 – 9.9)	34%	54%
Mid-career members (10 – 14.9)	29%	60%
Mid-career members (15 – 21.9)	24%	62%
Older members (within 10 yrs unreduced pension)	26%	65%
Older members (within 5 yrs unreduced pension)	27%	64%
Older members (eligible for unreduced pension)	24%	63%

Q15. Please imagine that your contributions are at the maximum amount you would be willing to contribute in order to keep all pension provisions at current levels. I'd like to read you a list of changes that could be made to future pension provisions in order to keep contributions from rising above this level. Please tell me whether you would be in favour or not it favour of each of the following changes. How about reducing your monthly pension for future service by about ten percent? By future service, I mean any benefits you would earn from a specified date in the future until the date you retire. Any benefits you earned in the past are guaranteed under Ontario's Pension Benefits Act.

POLLARA

Reduction to monthly pension by about 10% opposed by more than half of most member segments

- Occasional workers (45%) and French school board members (45%) are more likely to be in favour of reducing monthly pension for future service by 10%.

Member segment		In favour (%)	Not in favour (%)
OVERALL		32%	57%
Gender	Female	32%	57%
	Male	34%	57%
Employment type	Full-time	31%	59%
	Part-time	33%	53%
	Occasional	45%	44%
Employer type	District school board – English	32%	57%
	District school board – French	45%	41%
Place of work	Elementary	34%	55%
	Secondary	28%	61%
Urban/Rural	Urban	32%	58%
	Rural	35%	52%

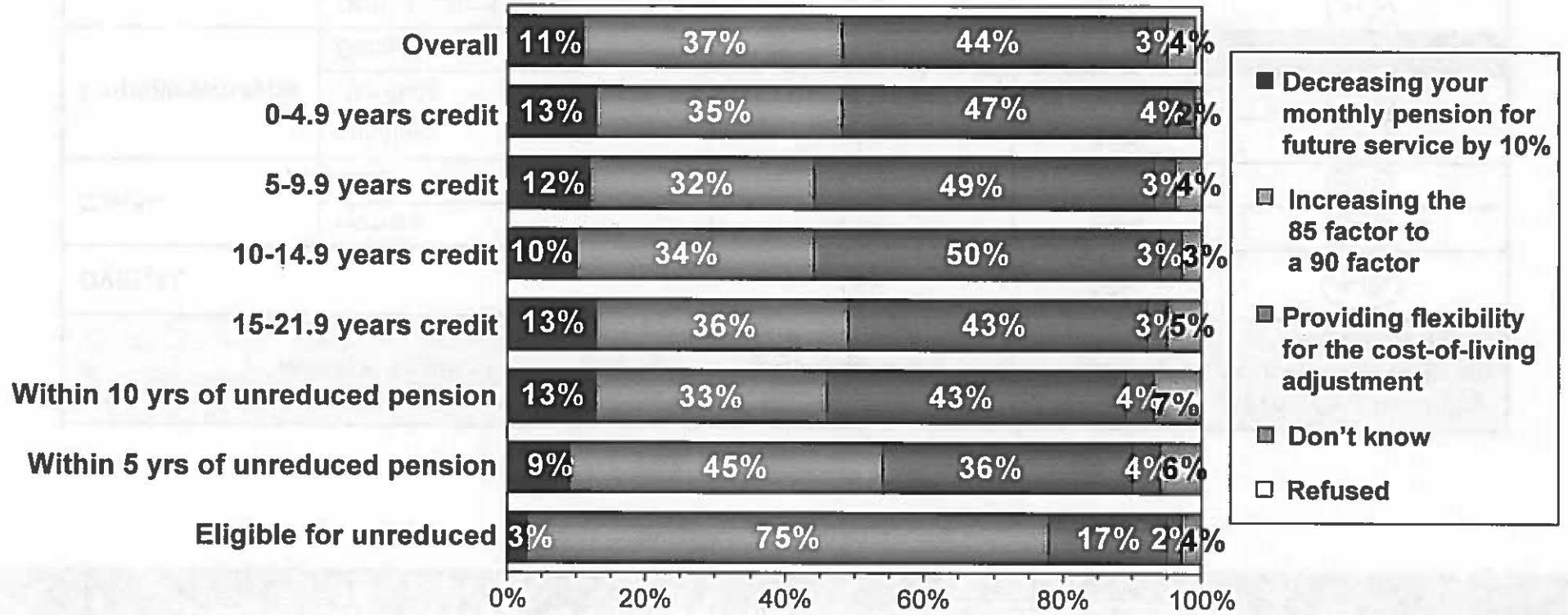
More likely

Less likely

POLLARA

Providing flexibility for the cost-of-living adjustment is the preferred potential change to members' pension plan

- When asked which of the three potential plan changes they preferred, 44% of pension plan members opt for the flexible cost-of-living adjustment.
- This change is the top choice for five of the seven career groupings. Only members within five years of unreduced pension and those already eligible for unreduced pension prefer increasing the 85 factor to 90.



Q17. We've discussed three changes that could be made to pension provisions in the future, depending on the future financial situation of the pension plan. I'd like to read you descriptions of all three of these potential changes. when' I'm done, please tell me which one of these changes you would be most willing to have made to your pension plan.

Plurality of all member segments name flexible cost-of-living adjustment as preferred change

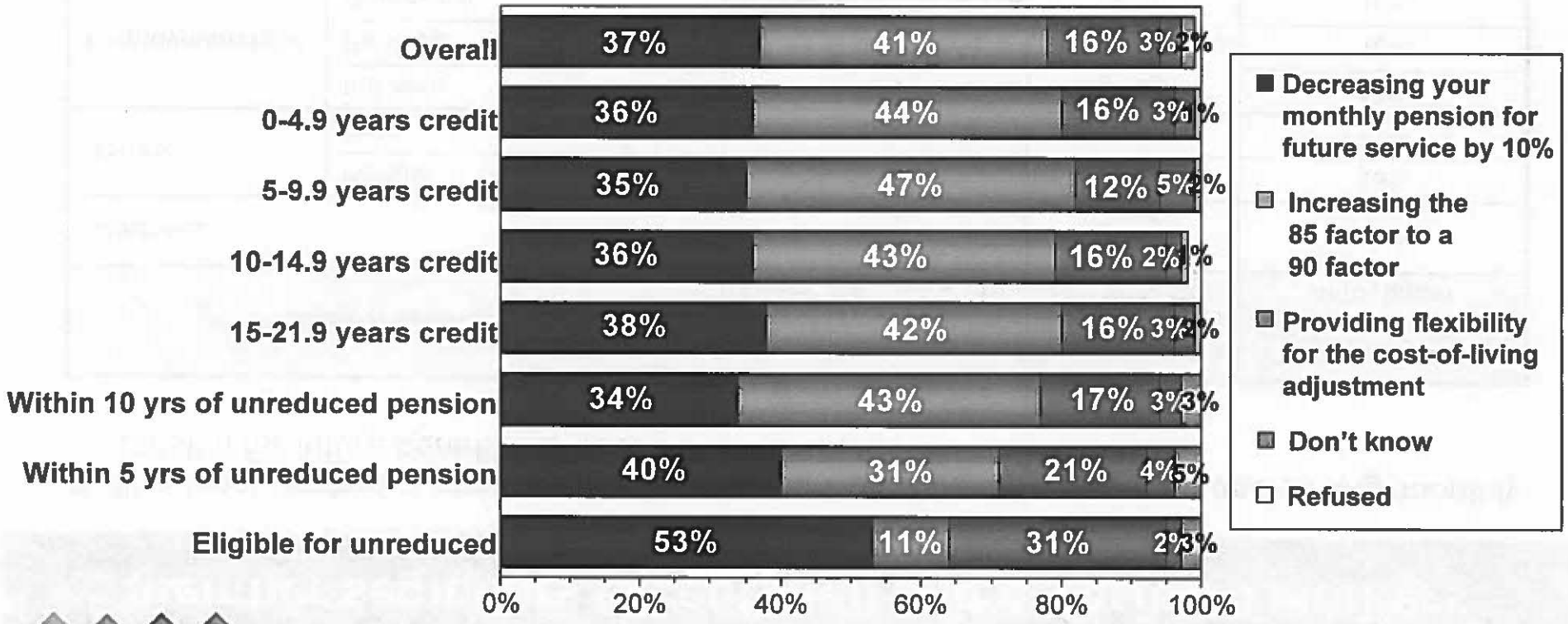
Member segment		Decreasing your monthly pension for future service by 10%	Increasing the 85 factor to a 90 factor	Providing flexibility for the cost-of-living adjustment
OVERALL		11%	37%	44%
Gender	Female	11%	36%	45%
	Male	11%	38%	43%
Employment type	Full-time	11%	37%	44%
	Part-time	12%	38%	42%
	Occasional	13%	31%	52%
Employer type	District school board – English	11%	37%	44%
	District school board – French	25%	20%	46%
Place of work	Elementary	12%	36%	45%
	Secondary	10%	38%	44%
Urban/Rural	Urban	12%	37%	43%
	Rural	8%	35%	50%

More likely Less likely

POLLARA

Increasing 85 factor to 90 is the least preferred potential change to the pension plan

- When asked which of the three potential plan changes they are least willing to have made, a plurality (41%) name increasing the 85 factor to a 90 factor.
- This option is the least favourite choice for five of the seven career groupings. Again, only members within five years of unreduced pension and those already eligible for unreduced pension have different least favourite options.



Q18. Which potential change are you least willing to have made?

Increasing 85 factor to 90 is the least preferred change for all member segments except men and occasional workers

- The least preferred change among men and occasional workers is decreasing monthly pension for future benefits by 10%.

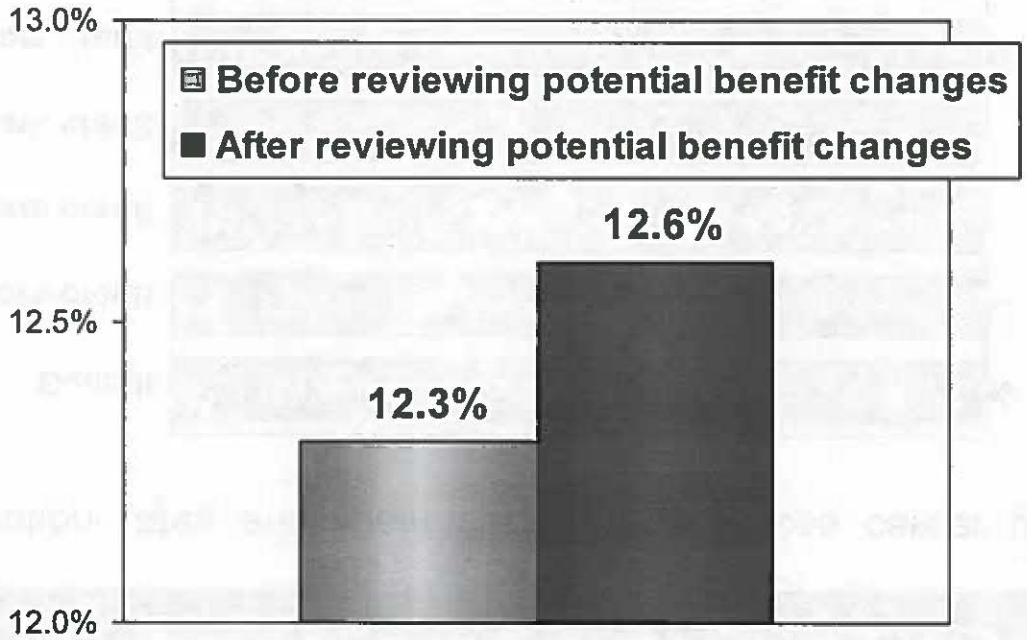
Member segment		Decreasing your monthly pension for future service by 10%	Increasing the 85 factor to a 90 factor	Providing flexibility for the cost-of-living adjustment
OVERALL		37%	(41%)	16%
Gender	Female	36%	(42%)	16%
	Male	40%	38%	17%
Employment type	Full-time	36%	(41%)	17%
	Part-time	38%	(42%)	15%
	Occasional	(42%)	40%	15%
Employer type	District school board – English	38%	(40%)	16%
	District school board – French	23%	(58%)	15%
Place of work	Elementary	38%	(42%)	15%
	Secondary	35%	(39%)	19%
Urban/Rural	Urban	37%	(41%)	17%
	Rural	38%	(42%)	13%

More likely **Less likely**

POLLARA

After reviewing potential benefit changes, members increase their maximum contribution from 12.3% to 12.6%

- After reviewing potential changes to their pension provisions, members were asked to identify the maximum contribution they would be willing to make in order to maintain their current provisions.
- Members' maximum contribution increased to an average maximum of 12.6% (up 0.3 points). A quarter (25%, down 2 percentage points) of members became willing to contribute up to 11%. More than two-thirds (67%, up 7 points) of members became willing to have contributions exceed 11%.

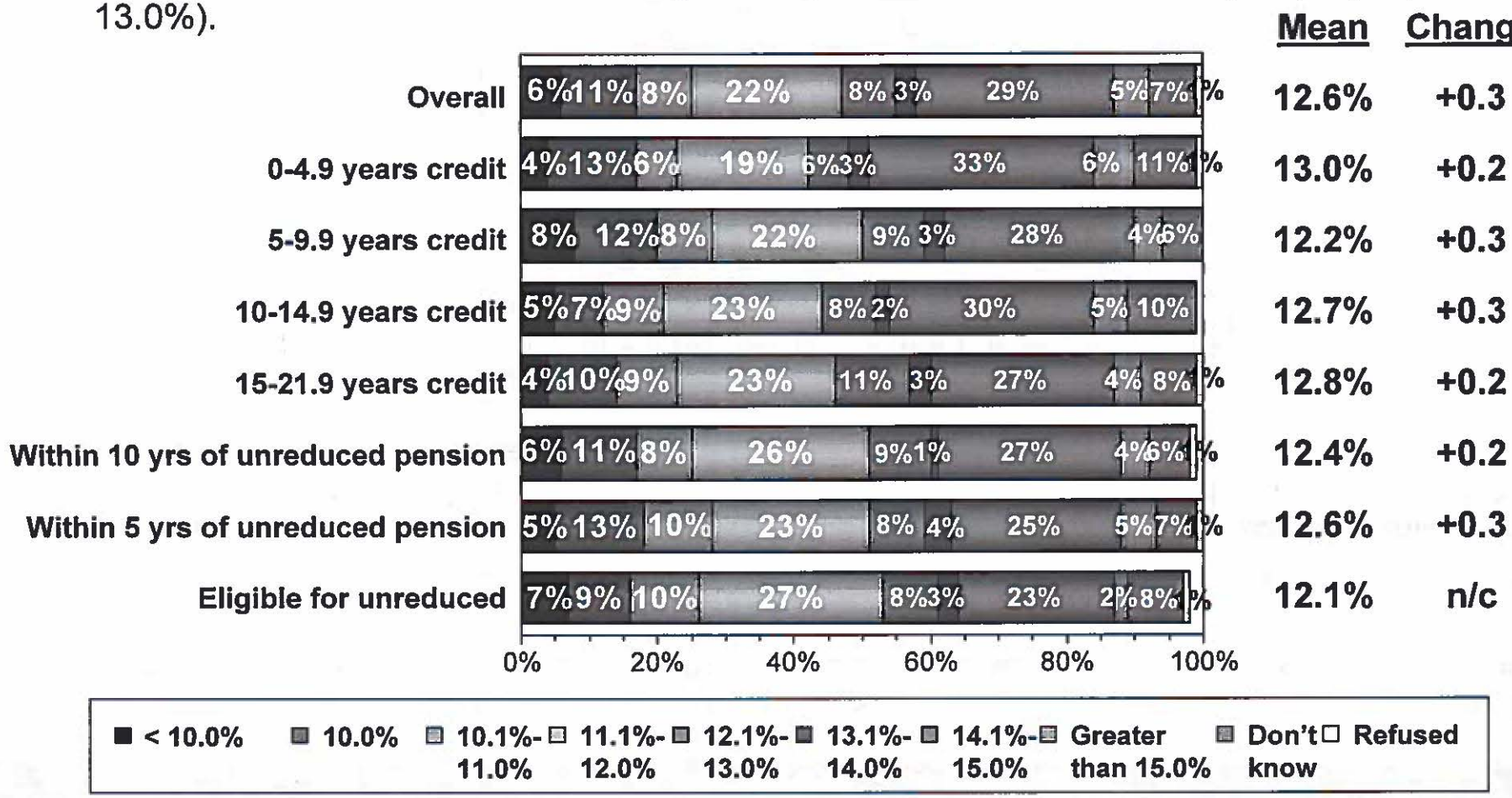


Q19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

POLLARA

Maximum pension contributions fairly consistent among different career groupings

- Maximum contribution rates are again very similar across career groupings (12.1%-13.0%).



Q19. Now that you are more familiar with the types of changes that could be made to the pension plan, what is the maximum total percentage of your before tax salary that you would be willing to contribute in order to keep pension provisions at current levels? Please keep in mind you are currently contributing 10%.

POLLARA

Maximum contributions fairly consistent among different member segments

- Part-time workers (13%) once again are willing to contribute slightly more, whereas French school board members are willing to contribute the least (10.7%).

Member segment		Mean	Change
OVERALL		12.6%	+0.3
Gender	Female	12.6%	+0.2
	Male	12.3%	+0.1
Employment type	Full-time	12.5%	+0.2
	Part-time	13.0%	n/c
	Occasional	12.7%	+0.1
Employer type	District school board – English	12.6%	+0.2
	District school board – French	10.7%	n/c
Place of work	Elementary	12.6%	+0.2
	Secondary	12.4%	+0.2
Urban/Rural	Urban	12.5%	+0.2
	Rural	12.8%	+0.2

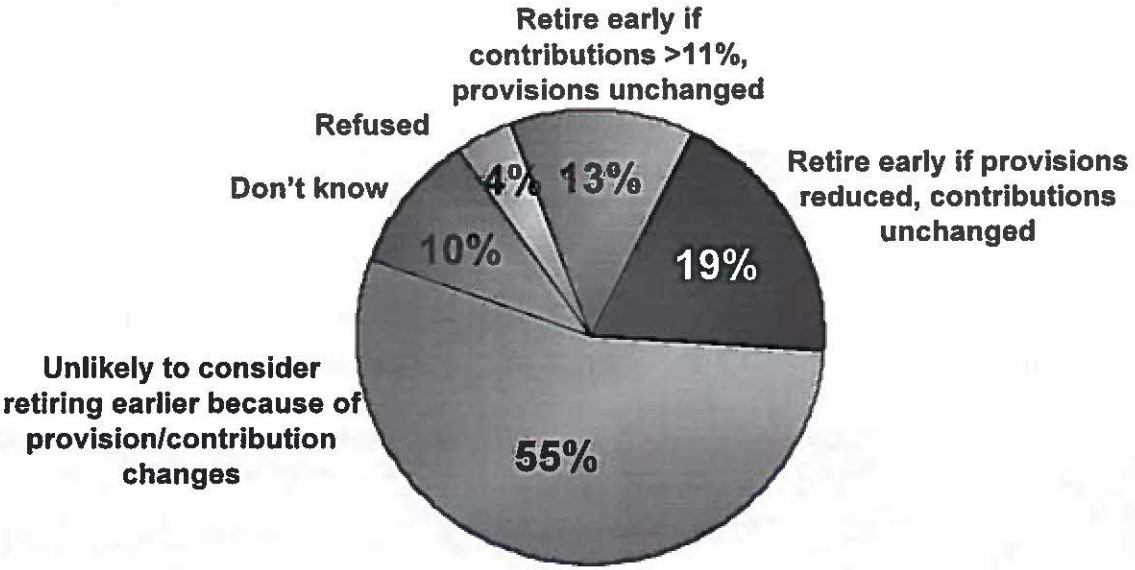
More likely

Less likely

POLLARA

Early retirement slightly more likely if provisions reduced rather than contributions increased; more than half say intentions unchanged

- More than half (55%) of members approaching retirement (age plus years of credit ≥ 74) say they are unlikely to consider retiring earlier than planned as a result of changes to their future pension provisions and contribution rates.
- A further 19% would consider retiring earlier than planned if the pension provisions they will earn in future years are reduced, even if their contributions rates remain the same. If contributions increase to more than about 11% of their salary, 13% would consider retiring earlier than planned, even if their provisions are unchanged.
- Overall results are mirrored by members within five years of unreduced pension and those who are already eligible. Men (17%) are slightly more likely than women (10%) to retire if contributions increase to more than 11%.



Q20. (ASK IF AGE + YEARS OF CREDIT ≥ 74) Which ONE of the following three statements best represents you own viewpoint: (RANDOMIZE ORDER OF STATEMENTS)

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Provis, Ian (TBS); Keates, James (TBS); Saboor, Ibrahim (TBS); Georgegiana Tanudjaja (Georgegiana.Tanudjaja@auditor.on.ca); marcia.desouza@auditor.on.ca; Audelyn.Budihardjo@auditor.on.ca; Bill Pelow <Bill.Pelow@auditor.on.ca> (Bill.Pelow@auditor.on.ca); Chen, Doris (MECP); lucy.durocher@ca.pwc.com; michael.hawtin@ca.pwc.com
Cc:	"lucy.durocher@pwc.com"; "Alexander Truong"; Lau, Lucia (MECP); Taylor, Heather (MECP); Whitestone, Jim (MECP)
Subject:	Audit planning and cap and trade
Start:	January 16, 2017 10:00:00 AM
End:	January 16, 2017 11:30:00 AM
Location:	Office of the Auditor General of Ontario, 15th Floor, 20 Dundas Street West

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Toll Free 1-866-633-1033
Local Number 416-212-8013
Conference ID 3855914

Briefing on Draft Report.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; kdanyluk@deloitte.ca [kdanyluk@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Briefing on Draft Report
Date: Thursday, September 22, 2016 11:39:02

Matt/Kerry,

We have been asked to invite you to attend a short briefing of senior officials on the results in your draft report this afternoon (around 5:30 pm). As we are hoping to receive the draft report by 4 pm, hopefully that timing would work for you. The location of the meeting would be in the Whitney Block (close to the legislature, just north of our offices).

Please confirm your availability to provide an overview of your results this afternoon.

Thanks.

Nadine

Call.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Call
Date: Wednesday, September 28, 2016 09:31:01

Hi Nadine,

I can't make the 1:30 invitation you sent. I am travelling this afternoon and will be tackling airport security around then!

I can do a call later in the day, say between 5:30 and 7pm.
Or I can do a call earlier this morning before 12pm.

Tomorrow I am at a conference, but I could step out in the morning for a call.

Let me know what works best for you.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Cap and Trade.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]
Subject: Cap and Trade
Date: Friday, September 30, 2016 09:22:09

Hello

We are in the process of preparing our budget and would like to know when your next billing on the above will arrive. So far you have billed us for $9129.27. I would really appreciate if you could provide me with the breakdown on how much you are planning to work on the above project for this fiscal which is ending on March 2017 and the next fiscal which starts from April 1, 2017 till your contract ends which would be in September 2017.

Your assistance would be greatly appreciate.

Thanks

Shyrose Virani

Cap and trade related question.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Provis, Ian (TBS) [Ian.Provis@ontario.ca]
Subject: Cap and trade related question
Date: Thursday, November 17, 2016 12:12:32

Hi Nadine and Ian

Do you know if there are other examples in the Province's public accounts where "quotas" are sold to other entities pursuant to regulations. An example would be fishing quotas (designed to limit the amount of fishing by certain participants), but I suspect this is not something Ontario is into - but are there other schemes with similar quotas. As I was updating the memo to articulate "what" the EAs are the similarities between them and other quotas made me think it was worth asking if there are any precedents, because this could be critical in forming/supporting a view over revenue recognition if there were.

Thanks,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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bi-weekly calls with David and Michael - PwC.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Provis, Ian (TBS) [Ian.Provis@ontario.ca]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]
Subject: bi-weekly calls with David and Michael - PwC
Date: Tuesday, November 08, 2016 10:47:10

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bi-weekly calls with David and Michael - PwC.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: bi-weekly calls with David and Michael - PwC
Date: Friday, October 14, 2016 09:58:30

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bi-weekly calls.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Scheifley, Rob (TBS) [Rob.Scheifley@ontario.ca]
CC: 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'david.c.greenall@pwc.com' [david.c.greenall@pwc.com]
Subject: bi-weekly calls
Date: Tuesday, September 27, 2016 15:22:13

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bi-weekly calls.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Scheifley, Rob (TBS) [Rob.Scheifley@ontario.ca]
CC: 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'david.c.greenall@pwc.com' [david.c.greenall@pwc.com]
Subject: bi-weekly calls
Date: Tuesday, September 20, 2016 09:13:30

---

bi-weekly calls.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Scheifley, Rob (TBS) [Rob.Scheifley@ontario.ca]
CC: 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'david.c.greenall@pwc.com' [david.c.greenall@pwc.com]
Subject: bi-weekly calls
Date: Tuesday, September 20, 2016 09:13:54

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bi-weekly calls.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Scheifley, Rob (TBS) [Rob.Scheifley@ontario.ca]
Subject: bi-weekly calls
Date: Wednesday, September 14, 2016 12:24:32

Ceiling Analysis.rtf

From: Petsche, Nadine (TBS) []
To: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]; Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]
CC: Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]
Subject: Ceiling Analysis
Date: Friday, June 30, 2017 15:13:48
Attachment 1: image001.jpg

Shayan/Christina,

Please advise when we might expect to receive the updated ceiling test documents? Now that the pension adjustments have been processed, it would be great to finalize the docs.

Thanks and have a wonderful Canada Day Weekend!

Nadine

image001.pdf

Canada
Happy
Canada Day

Contact info .rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
CC: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Contact info
Date: Sunday, September 18, 2016 17:59:14

Hi Matt.

In sending you this note, I am providing you with contact info for Lucy Durocher, the lead contact from PwC who is the lead on an engagement to review the Province's pension accounting as related to OTPP, specifically as related to the reported pension asset balance on the Province's books.

Lucy understands that she is able to connect with you and that you are able to share information regarding the pension matter under assessment. Likewise, please feel free to connect with Lucy on this file.

Nadine

Deck outline.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Deck outline
Date: Thursday, October 27, 2016 17:09:04
Attachment 1: Deck outline (JK) - OTPP Pension Asset Oct 27np.docx

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Hi Lucy.

Jim has drafted an outline for a preliminary briefing deck, based on the previous version of the position paper. Attached are my suggested edits which I have not yet shared with him.

I was thinking that it might be worthwhile to also get your comments so that he could revise the content more efficiently (once transferred to a pp format, track changes will be more challenging).

Hoping that you have some time to reflect and provide feedback on the outline.

Would like to provide him feedback by tomorrow, if possible.

Thanks in advance.

Nadine

Deck outline (JK) - OTPP Pension Asset Oct 27np.pdf

Accounting by the Province of Ontario for the Ontario Teachers' Pension Plan

Preamble

Analysis is specific to OTPP

Constating documents are different than for other pension plans in Ontario and in other provinces

Issue being considered

The Province followed the same accounting for OTPP for the prior 14 years during which the pension accounting standard (Section PS 3250) was the same

In relation to the 2015-16 public accounts for the Province of Ontario, the OAG disagreed with the Province's accounting for OTPP and OPSEUPP

The OAG disagrees that the surplus in OTPP is a reportable~~n~~ asset to the Province on the basis that:

- ~~as~~ there is no~~t~~ a legally enforceable right to the assets
- ~~and~~ no agreement is in place at March 31, 2016 with the Ontario Teachers' Federation (OTF) to reduce future contributions

Reporting in the 2015-16 Public Accounts

The Province disagrees with the AG's interpretation of PSAB standards.

The Province intended to benefit from the reported pension assets through reduced contributions and has performed the requested pension asset ceiling test to confirm that the Province's estimated asset value is not impaired.

For purposes of the 2015/16 Public Accounts, the Province regulated the accounting treatment for pension assets for the jointly sponsored pension plans (OTPP and OPSEUPP) to reflect the Auditor General's interpretation of PSAB. The regulation was necessary to achieve the AG's accounting treatment and to allow management to sign off on the Statement of Responsibility (since Management does not agree with the AG's interpretation of PSAB as related to the jointly sponsored pension plans).

~~Regulated accounting for the 2015-16 public accounts does not reflect the Province's view of pension accounting under PSAS~~

Overview of OTPP

A jointly sponsored pension plan as defined in the Pension Benefits Act

The sponsors are the Province of Ontario and the OTF

The sponsors are jointly responsible for decision making, share in making contributions, and collectively address any plan surplus/deficit (at least every 3 years)

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The plan administrator is an independent board of directors and follows the direction of the co-sponsors (not able to make any decisions w.r.t. contribution rates, uses of surpluses, etc.)

(INSERT SLIDE EXPLAINING PSAB STANDARDS AND COMPUTATION OF NET PENSION ASSET?)

PSAB options for recognition of pension asset were benefits to be realized through surplus withdrawal/contribution reductions…

Prior accounting for OTPP by the Province

Since 2001-2002, the Province has recorded its portion (50%) of the pension asset of OTPP in accordance with Section PS 3250

With regards to expected future benefit of the surplus, the Province would not expect to withdraw any surplus, but through reduced future contributions

-→ review history of use of surpluses for OTPP

~~Section PS 3250 is a primary source of GAAP which specifically addresses recognition and measurement of pension plans in government financial statements; compliance with PSAS requires following Section PS 3250 where applicable~~

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Section PS 3250 was issued in 2001; there have not been consequential changes to the standard since its introduction

Question 1 – Recognition of a pension asset

First we address why the surplus of OTPP is an asset to the Province

Applicability of Section PS 3250 to OTPP

What is a JDBP?

~~Section PS 3250 specifically addresses the accounting for pension plans in government financial statements~~ Primary source of gaap

Shared control

~~Section PS 3250 defines different types of pension plans; OTPP qualifies as a joint defined benefit plan (JDBP) as the sponsors share control over the plan (share in decisions relating to administration, levels of benefits and contributions)~~

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Definition of JDBP

XX

Concept of shared control and asset recognition

Section PS 3250 requires the government to account for its portion (as there is shared control) of a JDBP following the accounting requirements for a defined benefit plan within PS 3250; no distinction is made as to whether the plan is in a surplus or deficit position

"Shared control" is not addressed in the definition of an asset in the conceptual framework of PSAS; the definition requires "control" over an economic resource

~~Section PS 3250 was not revised when the existing conceptual framework was developed~~

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The concept of shared control is included in other standards in PSAS for example relating to government partnerships (Section PS 3060) which existed prior to PS 3250

Conclusion on recognition

Section PS 3250 on its own is sufficient to assess ~~addresses~~ the accounting for OTPP by the Province

OTPP is appropriately classified as a JDBP under Section PS 3250

Section PS 3250 requires recognition by the Province of 50% of the plan assets of OTPP

Unilateral c~~C~~ontrol is not necessary for asset recognition (e.g. government partnerships), shared control is appropriate for a JDBP

Uncertainty relating to OTPP's pension surplus relates to measurement, not uncertainty regarding expected future benefits for the Province

Question 2 – Measurement of a pension asset

Second we address how to measure the pension asset of OTPP in the Province's financial statements

Yes- slide above would explain measurement

Reference to valuations of pension asset ceiling having been done and results (different assumptions w.r.t. 50% benefits from contribution reductions vs. benefits, etc)

Guidance in Section PS 3250 on measurement

Only the portion of the pension surplus for which expected future benefits are to be realized by the government is to be recognized as an asset

A valuation allowance is to be recorded for any excess of adjusted benefit assets over the expected future benefit (referred to as the asset ceiling test)

A government may benefit from the pension surplus by either withdrawing the surplus from the plan or by taking a contribution holiday

Guidance on measurement as applicable to OTPP

The Province expects future benefits from OTPP's plan surplus to be realized through reduced future contributions, not withdrawals

Expectations of benefitting from the surplus are based on:

1. The Teachers' Pension Act requires equal contributions from the Province and from plan members of OTPP;
2. The history of surplus utilization for OTPP demonstrates sharing of the financial benefit between sponsors;
3. No sponsor of OTPP can unilaterally utilize the plan's surplus; and
4. If the sponsors of OTPP cannot agree on how to utilize the pension surplus, the matter can be submitted to arbitration.

The Province considers that the uncertainties around how and when to utilize the surplus do not result in an inability or lack of entitlement to utilize the surplus

Calculating the limit on the carrying amount of an accrued benefit asset (asset ceiling test)

Section PS 3250 indicates the expected future benefit to be recorded by the government is the sum of:

a. The present value of its expected future accrual for service for the current number of active employees less the present value of minimum contributions the government is required to make regardless of any surplus; plus
b. The amount of the plan surplus that can be withdrawn in accordance with the existing plan and any laws and regulations.

The next slides will consider this calculation relative to the Province's 50% share of OTPP

Through withdrawal of the surplus (Part b of the asset ceiling test)

Section PS 3250 requires that the expected future benefit include amounts to which a government has a legally enforceable right of withdrawal; the concept of legal enforceability is included in PS 3250 but relative only to the withdrawal of a surplus

Commented [np1]: This wording is not right. Need to position properly.

In accordance with the Funding Management Policy for OTPP, the parties must negotiate ~~a side agreement must be reached by the sponsors~~ in order for a withdrawal of the surplus to happen.

Commented [np2]: Insert reference to FSCO?

As the Province does not have a signed~~de~~ agreement with OTF regarding the withdrawal of the surplus, there is no legally enforceable right of withdrawal, and there is no expected future benefit for the

Province ~~under part b~~with reference to a withdrawal of surplus; however, as stated above, the Province expects to benefit through future contribution reductions, not surplus withdrawals.

Through reducing future contributions (Part a of the asset ceiling test)

The present value of its expected future accrual for service is typically calculated based on the Province's share (50% for OTPP) of the current service cost reported in the most recent actuarial valuation taken into perpetuity

There is no guidance in PSAS on determining the present value of minimum contributions the government is required to make; professional judgement is required. The Province engaged consultants to calculate this value for OTPP considering different assumptions on future minimum contributions.

Commented [np3]: Need to insert reference to the 3 year mandated negotiation timeline and/or when plan is in funding surplus position.

For purposes of OTPP in the 2015-16 public accounts, 11 years was used by the Province reflecting management's best estimate of the number of future years for which current minimum contributions are to be made until the Income Tax Act limits are reached

Based on the Province's best estimate calculation of the expected future benefit, no valuation allowance was ~~recorded~~ deemed necessary in relation to the pension asset of OTPP at March 31, 2016

Other guidance in PSAS on measurement

Section PS 2130 provides guidance on dealing with measurement uncertainty

Measurement uncertainty in pension plan accounting exists for example in the estimation of the valuation allowance and in the determination of the discount rate (which is often management's best estimate of the rate of return on plan assets)

Historical rates of return on plan assets have supported the past discount rates used by the Province in relation to OTPP

Comparability of Ontario's accounting for JDBPs to other Provinces

Provinces such as British Columbia and New Brunswick do not report assets for their provincial joint sponsored pension plans or alternatively provide a valuation allowance to reduce the pension asset balance to nil

The difference in accounting versus the Province of Ontario (for OTPP) results from these other provinces not having any right to the pension surpluses unlike in Ontario

Conclusion on measurement

The Province's position is that the attributes of the JDBP arrangements for OTPP entitle the Province to access its portion of the plan surplus through the right to negotiate its use of the Province's benefit through future reduced contributions

Significant professional judgement and estimation is involved in determining the valuation allowance under Section PS 3250; the Province has applied reasonable estimates

Based on the result of modelling performed in relation to the asset ceiling test, the Province concluded that no valuation allowance was ~~concluded to be appropriate by the Province~~necessary to the pension asset that would have otherwise be reported on the Province's books as at March 31, 2016.

Deloitte.rtf

From: Virani, Shyrose (TBS) []
To: Askcontractorscreening (TBS) [Askcontractorscreening@ontario.ca]
Subject: Deloitte
Date: Wednesday, October 19, 2016 11:29:39

Hi

Can you please let me know if the following staff from Deloitte has clearance:

1. Trevor Gary
2. Matt Colley
3. Clair Grindley
4. Max Bazile
5. Kerry Danyluk
6. Ray Martin

Determining shared control (002).docx.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Determining shared control (002).docx
Date: Friday, October 07, 2016 20:14:47
Attachment 1: Determining shared control (002).docx

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Determining shared control (002).pdf

Determining Shared Control for Government Partnerships

Background:

Paragraph PS 3060.06 defines a government partnership as follows:

> A government partnership is not a government organization but is a contractual arrangement between the government and a party or parties outside of the government reporting entity that has all of the following characteristics:
>
> a) the partners co-operate toward achieving significant clearly defined common goals;
> b) the partners make a financial investment in the government partnership;
> c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and
> d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.
>
> The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control.

Determining whether the definition of a government partnership is met for a certain situation can be difficult. Much of this difficulty arises when trying to determine whether the criteria in subparagraph PS 3060.06(c) is met. Section PS 3060 does not provide a significant amount of guidance on how to determine shared control. However paragraphs .13 and .20 state the following [emphasis added]:

> .13 **The contractual arrangement establishes shared control** over the government partnership. Such a requirement **ensures that no single partner is in a position to control the activities of the government partnership unilaterally**. The arrangement **identifies those decisions in areas essential to the goals** of the government partnership **that require the consent of all the partners** and **those decisions which may require the consent of a specified majority of partners**.
>
> ...
>
> .20 Shared control of a government partnership means that the partners make **decisions related to the financial and operating activities** of the government partnership **on an ongoing basis based on the terms of the contractual arrangement**; **none of the partners is in a position to exercise unilateral control over the government partnership**. When there is shared control, partners have an **active ongoing interest or relationship** in the arrangement other than as passive investors or as parties to a purchase / sale transaction. Shared control would exist, for example, when a joint board is established to oversee the provision of police or fire protection services for a number of local governments.

Question 1: For the criteria on shared control in subparagraph PS 3060.06(c) to be met, what are the essential decisions that would be required to be made by unanimous consent of the board members?

Paragraph PS 3060.13 states that the contractual arrangement establishes shared control over the government partnership…The arrangement identifies **those decisions in areas essential to the goals of the government partnership that require the consent of all the partners** and those decisions which may require the consent of a specified majority of partners.

Additionally, paragraph PS 3060.20 states shared control of a government partnership means that the partners **make decisions related to the financial and operating activities of the government partnership** on an ongoing basis based on the terms of the contractual arrangement…

Based on what is in paragraphs PS 3060.13 and .20, it is clear that the decisions which require the consent of all the partners are those that are essential to the goals of the government partnership, which would include decisions related to the financial and operating activities of the government partnership. Section PS 3060 does not provide specific guidance on how to determine what these essential decisions would be. As a result, a municipality, for example, that is trying to determine whether it has shared control of an entity, would apply one of the following views:

View A – Determination of what the essential decisions of the entity are would be considered in the context of the indictors of control in Section PS 1300, Government Reporting Entity.

Since there is no specific guidance in Section PS 3060 that assists in determining what these essential decisions would be, it would be appropriate for a municipality to consider the indicators of control in paragraphs PS 1300.18-.19 in determining what the essential decisions of the entity are in the above situation.

View B – Determination of what the essential decisions of the entity are would be considered by also looking to guidance outside of the PSA Handbook.

The indicators of control in paragraphs PS 1300.18-.19 are a good starting point for determining the essential decisions of the entity. However, these paragraphs do not specifically consider which decisions most affect the "activities and goals" of the partnership. These "activities and goals" may be considered equivalent to the "relevant activities" of an entity as described in IFRS 10, *Consolidated Financial Statements.* Therefore, it may be helpful to look outside the PSA Handbook and to the guidance in IFRS when determining the essential decision of the entity.~~Since there is no specific guidance in the PSA Handbook on determining what the essential decisions would be that would result in shared control, a municipality could decide to look outside of the PSA Handbook and could look to IFRS for guidance.~~ IFRS 10, Consolidated Financial Statements, and IFRS 11, Joint Arrangements, provide guidance on what is considered in determining control and joint control[1]. Under this view, in determining the essential decisions of the entity the guidance in IFRS 10 on relevant activities and substantive vs. protective rights would also be applied.

View C – Determination of what the essential decisions of the entity are would be made by using professional judgment.

[1] The determination of control in IPSAS 35, *Consolidated Financial Statements,* is based on the same principles as IFRS 10.

Since there is no specific guidance in the PSA Handbook on determining what the essential decisions of the entity are that would result in shared control and because a government would not be required to look outside of the PSA Handbook for guidance in making this determination, each government would use its own professional judgment and consider the facts and circumstances of the situation to determine whether the decisions that require unanimous consent are essential decisions of the entity and confer on the government shared control.

Let's examine this issue and each of the views by looking at the scenario in Appendix A.

Question 2: If it is determined there is not shared control in the scenario in Appendix A, the entity would not be a government partnership. Since the entity is not controlled by a single government, it would not be any type of government organization. The entity is also not a government itself nor is it a government component since it is a separate legal entity. As a result, the entity that was created by and is owned by a group of governments would not be with the scope of the PSA Handbook. Does this highlight an issue with the scope of the PSA Handbook?

Appendix A:

Scenario:

A contractual arrangement was entered into by 10 municipalities. In accordance with the terms of the contractual arrangement, a separate entity has been incorporated.

The contractual arrangement was entered into and the entity was formed in order to provide specific municipal services to the residents of the 10 municipalities and to share the costs and revenues associated with providing those services (paragraph PS 3060.06(a) is met).

Each municipality made an initial financial investment in the entity and took back a 10% interest in the incorporated entity. This initial financial investment was used to construct the infrastructure required to provide the services to the 10 municipalities (paragraph PS 3060.06(b) is met).

The entity's annual operations are funded by users fees charged to each participating municipality based on the usage of the services provided by the entity.

The entity is run by a board of 10 directors. Each of the 10 municipalities appoints one director who serves for a three year term. Each director has one vote. The board operates in accordance with the terms of the contractual arrangement and holds meetings on a regular basis. The following decisions must be made my unanimous consent:

- Approval of any significant financial investment required by the municipalities;
- Approval of any borrowing arrangements the entity wants to enter into;
- Approval of any additional municipality that wants to participate in the contractual arrangement in the future;
- Approval of a change to the contractual arrangement; and
- Approval to terminate the contractual arrangement.

All other decisions are required to be made by majority vote of the board members.

The 10 municipalities share on an equitable basis the significant risks and benefits associated with the operations of the entity (paragraph PS 3060.06(d) is met).

Based on the above information ~~above~~ it is clear that the criteria in sub paragraphs PS 3060.06 (a, b, and d) of the definition of a government partnership have been met. Please consider your response to the following views in terms of whether or not the criteria in subparagraph (c) on shared control has been met.

View A – Determination of what the essential decisions of the entity are would be considered in the context of the indictors of control in Section PS 1300, Government Reporting Entity

Since there is no specific guidance in Section PS 3060 that assists in determining what these essential decisions would be, it would be appropriate for a municipality to consider the indicators of control in paragraphs PS 1300.18-.19 in determining what the essential decisions of the entity are in the above situation.

Indicators of control
.18 There are certain indicators that provide more persuasive evidence of control:

a) government has the power to unilaterally appoint or remove a majority of the members of the governing body of the organization;	N/A
b) government has ongoing access to the assets of the organization, has the ability to direct the ongoing use of those assets, or has ongoing responsibility for losses;	This indicator may be considered to be met in the context of shared control since approval of any significant financial investment by the municipalities requires unanimous consent; and the municipalities share on an equitable basis the significant risks and benefits associated with the operations of the entity.
c) government holds the majority of the voting shares or a "golden share" that confers the power to govern the financial and operating policies of the organization; and	N/A
d) government has the unilateral power to dissolve the organization and thereby access its assets and become responsible for its obligations.	This indicator would be met in the context of shared control since the contractual agreement between the municipalities that governs the entity can only be terminated by unanimous consent.
.19 Other indicators that may provide evidence of control exist when the government has the power to:	
a) provide significant input into the appointment of members of the governing body of the organization by appointing a majority of those members from a list of nominees provided by others or being otherwise involved in the appointment or removal of a significant number of members;	N/A
b) appoint or remove the CEO or other key personnel;	This indicator would not be met in the context of shared control since this is not a decision that would require unanimous consent, but instead would be made by majority vote.
c) establish or amend the mission or mandate of the organization;	This indicator would be met in the context of shared control since the mission and mandate of the entity would be laid out in the contractual arrangement and any changes to the contractual arrangement must be made by unanimous consent.
d) approve the business plans or budgets for the organization and require amendments, either on a net or line-by-line basis;	This indicator would not be met in the context of shared control since decisions about the entity's business plan or annual budget are~~would~~ not required to be made by unanimous consent, but instead would be made by majority vote.
e) establish borrowing or investment limits or restrict the organization's investments	This indicator for shared control would be met in the context of the borrowing criteria -since approval of any borrowing arrangements the

	entity wants to enter into must be made by unanimous consent. However, this indicator would not be met for shared control in terms of the investments since ~~-~~any decisions regarding what the entity can invest any excess cash do not require unanimous consent, but instead ~~in~~ would be made by majority vote.
f) restrict the revenue-generating capacity of the organization, notably the sources of revenue; and	This indicator would not be met in the context of shared control since a change in the user fees charged by the entity~~,~~ (which is its primary source of revenue~~,~~) is not a decision that ~~would~~ requires unanimous consent, but instead would be made by majority vote.
g) establish or amend the policies that the organization uses to manage, such as those relating to accounting, personnel, compensation, collective bargaining or deployment of resources.	This indicator would not be met in the context of shared control since this is not a decision that ~~would~~ requires unanimous consent, but instead would be made by majority vote.

In considering the indicators outlined in paragraphs PS 1300.18-.19 above in relation to this scenario each municipality may determine that it has shared control in this situation. This is because, the guidance in paragraph PS 1300.18 are considered to be more persuasive indicators of control and the indicator in .18(b) may be considered to be met and the criteria in .18(d) is met, while the remaining criteria in .18(a) and (c) are not considered applicable in this situation. This is further supported by the fact that the criteria in paragraph PS 1300.19(c) and (e) also appear to be met. Therefore, it could be argued that each municipality has shared control of the entity in this situation since the decisions which require unanimous~~the~~ consent of all the partners (i.e. approval of any significant financial investment required by the municipalities, approval of any borrowing arrangements the entity wants to enter into, approval of any additional municipality joining the contractual arrangement in the future, approval of any changes to the contractual arrangement and termination of the contractual arrangement) are those~~e~~ decisions that are "essential" to the goals of the entity.

View B – Determination of what the essential decisions of the entity are would be considered by also looking to guidance outside of the PSA Handbook

The indicators of control in paragraphs PS 1300.18-.19 are a good starting point for determining the essential decisions of the entity. However, these paragraphs do not specifically consider which decisions most affect the "activities and goals" of the partnership. These "activities and goals" may be considered equivalent to the "relevant activities" of an entity as described in IFRS 10, *Consolidated Financial Statements*. Therefore, it may be helpful to look outside the PSA Handbook and to the guidance in IFRS 10 when determining the essential decision of the entity. ~~If we look at the guidance in~~ Under IFRS 10~~, *Consolidated Financial Statements,* regarding~~ when assessing~~determining~~ control[2], the~~is~~ standard requires a determination of the entity's relevant activities and how decisions about those

[2] Note determining joint control under IFRS 11 is based on the same control principles contained in IFRS 10. Additionally, the determination~~ing~~ of control in IPSAS 35, *Consolidated Financial Statements,* is also based on the same principles as IFRS 10.

relevant activities are made. Paragraphs IFRS 10.B11-12 provide the following examples of relevant activities:

> B11 For many investees, a range of operating and financing activities significantly affect their returns. Examples of activities that, depending on the circumstances, can be relevant activities include, but are not limited to:
>
> a) selling and purchasing of goods or services;
> b) managing financial assets during their life (including upon default);
> c) selecting, acquiring or disposing of assets;
> d) researching and developing new products or processes; and
> e) determining a funding structure or obtaining funding.
>
> B12 Examples of decisions about relevant activities include but are not limited to:
>
> a) establishing operating and capital decisions of the investee, including budgets; and
> b) appointing and remunerating an investee's key management personnel or service providers and terminating their services or employment.

In the scenario being considered, relevant activities would be the municipal services provided by the entity. Decisions about those relevant activities would be those that determine the level and types of services provided, the user fees charged for the services, and decisions made to approve the entity's operating and capital budgets. According to the scenario facts all of these types of decisions are made by majority vote of the participating municipalities, they are not decisions that are required to be made by unanimous consent.

Under IFRS 10, when an investor is assessing whether it has control over an investee, it only considers substantive rights that it holds. It does not consider "protective rights". Protective rights relate to fundamental changes to the activities of an investee or apply in exceptional circumstances, and do not give a party power over an entity to which the rights relate. IFRS 10 also provides guidance on identifying protective rights and paragraph B28 provides the following examples:

> B28 Examples of protective rights include but are not limited to:
>
> a) a lender's right to restrict a borrower from undertaking activities that could significantly change the credit risk of the borrower to the detriment of the lender.
> b) the right of a party holding a non-controlling interest in an investee to approve capital expenditure greater than that required in the ordinary course of business, or to approve the issue of equity or debt instruments.
> c) the right of a lender to seize the assets of a borrower if the borrower fails to meet specified loan repayment conditions.

For a right to be substantive, the holder must have the practical ability to exercise that right (IFRS 10.B22). Determining whether rights are substantive requires judgement and paragraph B23 provides a list of factors to consider in making this determination (refer to full text of paragraph B23 included in Appendix B).

Based on the guidance in IFRS 10, when a municipality is determining whether it has shared control of the entity in this situation, it would consider those substantive rights that it has related to the entity's relevant activities and it would not consider protective rights in making this determination. The rights related to approvals of any significant financial investment required by the municipalities, approval of borrowing arrangements the entity wants to enter into, approval of an additional municipality joining the contractual arrangement in the future and termination of the contractual arrangement would likely be considered protective rights in that they relate to fundamental changes to the business and not to directing the primary activities.

Therefore, based on the above analysis the municipalities in this scenario would not have shared control over the entity since the decisions that require unanimous consent are not substantive decisions about the entity's relevant activities.

View C – Determination of what the essential decisions of the entity are would be made by using professional judgment

Under this view each municipality would use its own professional judgment and consider the facts and circumstances of the situation to determine whether the decisions that require unanimous consent are in fact essential decisions of the entity and therefore provide the municipality with shared control. Under this view it is possible for there to be diversity in practice as each of the municipalities involved could differ in what they believe the essential decisions of the entity are and as a result some municipalities could determine they have shared control while others may determine they do not have shared control.

Are there any other views?

Appendix B:

Excerpts from Section *PS 3060, Government Partnerships*

.06 The following definitions have been adopted for the purposes of this Section:
A government partnership is not a government organization but is a contractual arrangement between the government and a party or parties outside of the government reporting entity that has all of the following characteristics:

e) the partners co-operate toward achieving significant clearly defined common goals;
f) the partners make a financial investment in the government partnership;
g) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and
h) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.

The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]

...

ELEMENTS THAT DEFINE A GOVERNMENT PARTNERSHIP

Contractual arrangement

.11 A distinctive characteristic common to all government partnerships is that two or more partners are bound by a contractual arrangement which establishes that the partners have shared control over the government partnership. This characteristic of shared control distinguishes a government's interest in a government partnership from investments in other activities in which the government may exercise control (see GOVERNMENT REPORTING ENTITY, Section PS 1300, BASIC PRINCIPLES OF CONSOLIDATION, Section PS 2500, ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510, and PORTFOLIO INVESTMENTS, Section PS 3041).

.12 Activities conducted with no formal contractual arrangement, but which meet the definition of a government partnership set out in paragraph PS 3060.06, are in substance government partnerships for the purposes of this Section.

.13 The contractual arrangement establishes shared control over the government partnership. Such a requirement ensures that no single partner is in a position to control the activities of the government partnership unilaterally. The arrangement identifies those decisions in areas essential to the goals of the government partnership that require the consent of all the partners and those decisions which may require the consent of a specified majority of partners.

.14 The contractual arrangement may be evidenced in a number of ways, for example, by a contract between the partners or minutes of discussions between the partners. In some cases, the arrangement is incorporated in the enabling legislation, articles or other by-laws of the government partnership. Whatever its form, the contractual arrangement is usually in writing and deals with such matters as:

(a) the activity, duration and reporting obligations of the government partnership;
(b) the appointment of the board of directors or equivalent governing body of the government partnership and the voting rights of the partners;
(c) the financial investments by the partners; and
(d) the sharing by the partners of the output, revenues, expenses or surpluses or deficits of the government partnership.

.15 In some cases, the contractual arrangement may designate a partner, or an outside party or parties, as the manager or operator of the government partnership. The manager does not control the government partnership, nor does the manager exercise shared control with the partners solely by virtue of his or her management role. Rather, the manager acts within the financial and operating policies that the partners have prescribed.

.16 A government may incorporate regulations in any contractual arrangement it enters into (e.g., level of service, level of maintenance of an asset that may be returned to it at the end of a set term). Governments regulate a variety of activities with which they have no ongoing operational involvement. As such, regulations in and of themselves do not constitute shared control.

Significant clearly defined common goals

.17 Common goals are those that all partners share. For example, a number of communities may join together to build and operate a landfill site or a recreational facility. The significant common goals of the communities involve service provision and sharing the costs and revenues associated with the operations of the facility, and so, the arrangement would qualify as a government partnership.

.18 On the other hand, a community may hire an individual or organization to operate a recreational facility for a fee. The significant goals of the government are to provide a service and cost savings, while the significant goal of the management organization is to earn revenues from the contract to manage the facility. While the significant goals of each party are mutually beneficial, they are not common to both parties to the contract, and so, the arrangement does not qualify as a government partnership.

Financial investment

.19 A financial investment may be in the form of assets and/or assuming responsibility for ongoing operating costs. The investment of financial assets and tangible capital assets in the government partnership would be accounted for in accordance with paragraphs PS 3060.41-.54. The value assigned to the responsibility for ongoing operating costs would be that determined in the contractual arrangement for the government partnership.

Shared control

.20 Shared control of a government partnership means that the partners make decisions related to the financial and operating activities of the government partnership on an ongoing basis based on the terms of the contractual arrangement; none of the partners is in a position to exercise

unilateral control over the government partnership. When there is shared control, partners have an active ongoing interest or relationship in the arrangement other than as passive investors or as parties to a purchase / sale transaction. Shared control would exist, for example, when a joint board is established to oversee the provision of police or fire protection services for a number of local governments.

Shared risks and benefits

.21 In a government partnership, each partner is exposed to a share of the combined risks and shares in the benefits related to the common goals of the government partnership. In a government partnership, there must be an equitable sharing among the partners of the significant risks and benefits. For example, the government partners may operate a landfill site to provide a service to their constituents on a shared cost basis. The partners would generally share the operating and environmental risks, as well as the revenues associated with operating the landfill site.

.22 Risks and benefits would not be considered to be equitably shared in an arrangement where the government retains the full risk of owning an asset while allowing another party to receive the benefit of earning revenue from user fees derived from that asset. Risks and benefits would not be equitably shared when, for example, a government owned a highway that it allowed a private sector organization to operate and earn revenues from, based on the agreement and any necessary legislation.

FORMS AND STRUCTURES OF GOVERNMENT PARTNERSHIPS

...

Organizations under shared control

.27 An organization under shared control is a type of government partnership which involves the establishment of a separate organization (e.g., a corporation) in which each partner has an interest. The organization operates similarly to other organizations, except that a contractual arrangement between the partners establishes shared control over the economic activities of the organization.

.28 In an organization under shared control, each partner usually contributes cash or other resources to the government partnership. The organization owns the assets of the government partnership and incurs liabilities and expenses. It may enter into contracts in its own name and raise financing for the purposes of the activities of the government partnership. For example, several local governments may operate a transit organization to provide transit services to their constituents.

Excerpts from IFRS 10*, Consolidated Financial Statements*

Relevant activities and direction of relevant activities

B11 For many investees, a range of operating and financing activities significantly affect their returns. Examples of activities that, depending on the circumstances, can be relevant activities include, but are not limited to:

f) selling and purchasing of goods or services;
g) managing financial assets during their life (including upon default);
h) selecting, acquiring or disposing of assets;

i) researching and developing new products or processes; and
j) determining a funding structure or obtaining funding.

B12 Examples of decisions about relevant activities include but are not limited to:
c) establishing operating and capital decisions of the investee, including budgets; and
d) appointing and remunerating an investee's key management personnel or service providers and terminating their services or employment.

B13 In some situations, activities both before and after a particular set of circumstances arises or event occurs may be relevant activities. When two or more investors have the current ability to direct relevant activities and those activities occur at different times, the investors shall determine which investor is able to direct the activities that most significantly affect those returns consistently with the treatment of concurrent decision-making rights (see paragraph 13). The investors shall reconsider this assessment over time if relevant facts or circumstances change.
…

Rights that give an investor power over an investee
…
Substantive rights
B22 An investor, in assessing whether it has power, considers only substantive rights relating to an investee (held by the investor and others). For a right to be substantive, the holder must have the practical ability to exercise that right.

B23 Determining whether rights are substantive requires judgement, taking into account all facts and circumstances. Factors to consider in making that determination include but are not limited to:
a) Whether there are any barriers (economic or otherwise) that prevent the holder (or holders) from exercising the rights. Examples of such barriers include but are not limited to:
    i. financial penalties and incentives that would prevent (or deter) the holder from exercising its rights.
    ii. an exercise or conversion price that creates a financial barrier that would prevent (or deter) the holder from exercising its rights.
    iii. terms and conditions that make it unlikely that the rights would be exercised, for example, conditions that narrowly limit the timing of their exercise.
    iv. the absence of an explicit, reasonable mechanism in the founding documents of an investee or in applicable laws or regulations that would allow the holder to exercise its rights.
    v. the inability of the holder of the rights to obtain the information necessary to exercise its rights.
    vi. operational barriers or incentives that would prevent (or deter) the holder from exercising its rights (eg the absence of other managers willing or able to provide specialised services or provide the services and take on other interests held by the incumbent manager).
    vii. legal or regulatory requirements that prevent the holder from exercising its rights (eg where a foreign investor is prohibited from exercising its rights).
b) When the exercise of rights requires the agreement of more than one party, or when the rights are held by more than one party, whether a mechanism is in place that provides those parties with the practical ability to exercise their rights collectively if they choose to do so. The lack of such a mechanism is an indicator that the rights may not be substantive. The more parties

that are required to agree to exercise the rights, the less likely it is that those rights are substantive. However, a board of directors whose members are independent of the decision maker may serve as a mechanism for numerous investors to act collectively in exercising their rights. Therefore, removal rights exercisable by an independent board of directors are more likely to be substantive than if the same rights were exercisable individually by a large number of investors.

c) Whether the party or parties that hold the rights would benefit from the exercise of those rights. For example, the holder of potential voting rights in an investee (see paragraphs B47–B50) shall consider the exercise or conversion price of the instrument. The terms and conditions of potential voting rights are more likely to be substantive when the instrument is in the money or the investor would benefit for other reasons (eg by realising synergies between the investor and the investee) from the exercise or conversion of the instrument.

B24 To be substantive, rights also need to be exercisable when decisions about the direction of the relevant activities need to be made. Usually, to be substantive, the rights need to be currently exercisable. However, sometimes rights can be substantive, even though the rights are not currently exercisable.

…

B25 Substantive rights exercisable by other parties can prevent an investor from controlling the investee to which those rights relate. Such substantive rights do not require the holders to have the ability to initiate decisions. As long as the rights are not merely protective (see paragraphs B26–B28), substantive rights held by other parties may prevent the investor from controlling the investee even if the rights give the holders only the current ability to approve or block decisions that relate to the relevant activities.

Protective rights

B26 In evaluating whether rights give an investor power over an investee, the investor shall assess whether its rights, and rights held by others, are protective rights. Protective rights relate to fundamental changes to the activities of an investee or apply in exceptional circumstances. However, not all rights that apply in exceptional circumstances or are contingent on events are protective (see paragraphs B13 and B53).

B27 Because protective rights are designed to protect the interests of their holder without giving that party power over the investee to which those rights relate, an investor that holds only protective rights cannot have power or prevent another party from having power over an investee (see paragraph 14).

B28 Examples of protective rights include but are not limited to:

d) a lender's right to restrict a borrower from undertaking activities that could significantly change the credit risk of the borrower to the detriment of the lender.
e) the right of a party holding a non-controlling interest in an investee to approve capital expenditure greater than that required in the ordinary course of business, or to approve the issue of equity or debt instruments.
f) the right of a lender to seize the assets of a borrower if the borrower fails to meet specified loan repayment conditions.

Draft Memo For Your Review - Assessment of HOOPP Letter (dated April 28th).rtf

From: Sun, Alicia (TBS) []
To: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]; Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]
CC: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]
Subject: Draft Memo For Your Review - Assessment of HOOPP Letter (dated April 28th)
Date: Wednesday, June 07, 2017 15:08:42
Attachment 1: HOOPP Letter (Apr 28) Assessment_For EY review.docx
Attachment 2: image003.jpg

Hi Christina/Shayan,

As you may recall that HOOPP provided a letter (dated April 28th) to the Province indicating a change in indexation change for expected terminated members. Please see Appendix 1 for the original HOOPP letter.

We did an analysis based on your initial feedback and some consultation with our Pension Policy group. Please see attached a draft memo for your review.

Please provide comments.

We can have a brief discussion on this topic tomorrow if you wish.

Thanks,

Alicia

Alicia Sun, MBA, CPA, CGA

Manager, Broader Public Sector Reporting

Office of the Provincial Controller Division |Treasury Board Secretariat

7 Queen's Park Crescent, Frost South, 2nd Floor

Toronto, ON, M7A 1Z5

Email: Alicia.sun@ontario.ca

Tele: (416) 325-8155

HOOPP Letter (Apr 28) Assessment_For EY review.pdf

Issue

HOOPP made a change in an actuarial assumption by reflecting an allowance for future inflation protection for terminated members who choose to take a lump-sum payout. How would this change impact the Province's 2016-17 Public Accounts and future years?

Background

In December each year, the Province sends a request letter to the HOOPP board requesting the actuarial valuations of the HOOPP obligation for the Province's budget and Public Accounts reporting purposes. The response from HOOPP for the purposes of the fiscal 2016-17 interim forecast and Public Accounts was received on January 26th, 2017.

For update purposes, since the original plan estimates in the January letter are based on information as at December 31st, for purposes of the Public Accounts, the Province also requests HOOPP to communicate any events between December 31st and March 31st of the following year which would affect the valuation results of the January response letter in a material way. HOOPP responded to this request on April 28th, 2017 (see Appendix 1) indicating that subsequent to the actuarial valuation provided to the Province on January 26th, 2017, they made an assumption change which increased the year end plan obligation. The assumption change was to include 100% future inflation protection for post-2005 service for anticipated terminated members who choose to take a lump-sum payout which is referred to as a commuted value.

HOOPP indicated that the assumption change was made as a result of discussions with the provincial regulator, Financial Services Commission of Ontario (FSCO). The impact of this change was an increase to HOOPP's obligation of $1 billion which was reported and disclosed in HOOPP's annual report for the year ending December 31st, 2016.

Analysis

In determining the estimated pension assets/liabilities, and pension expense related to HOOPP, management's best estimates are made for the following factors:

- Rate of return/Discount rate,
- Salary growth rate, and
- Inflation indexation.

Currently, the Province uses the same assumptions that HOOPP is using for its valuation with the exception of the above key assumptions (see Appendix 2 for the differences in assumptions used by the Province and HOOPP).

With regards to inflation indexation, while the Province has used 75% inflation indexation assumption for all future years, HOOPP only includes board approved ad hoc inflation protection in the obligation for their valuation purposes. A history of CPI indexation of the plan is summarized in Appendix 3.

Upon receipt of the HOOPP letter dated April 28th, 2017, the Province requested HOOPP to provide an estimate of the impact to the plan obligation used in the Province's December 31, 2016 valuation. HOOPP estimated that the impact would be approximately a $350 million increase to the obligation for Public Accounts purposes. This translates into a $166 million impact to the Province's HOOPP obligation (85% of 56% of $350 million) for the hospitals' portion. The increase of $166 million represents a 0.6% increase to the obligation currently used in the Province's 2016-17 valuation of HOOPP ($26,449 million).

The change is due to a change in actuarial assumption, therefore in accordance with PS 3250 which states:

.060 The periodic actuarial valuation of a government's obligation for retirement benefits will usually determine that adjustments are required due to experience different from that assumed or to changes in actuarial assumptions. Adjustments are needed when the actual experience of the benefit plan is different than that expected. Adjustments due to changes in actuarial assumptions are needed when a government believes revised assumptions are necessary to reflect a relatively permanent change in expected experience or to reflect new information. Adjustments are inevitable because the actuarial valuation requires ongoing forecasts of uncertain future events.

.061 Actuarial gains and losses would be amortized over a reasonable future period because of their tentative nature and because further adjustments will likely be required in the future. A reasonable future period is the expected average remaining service life of the related employee group. Amortization may commence in the period following the determination of the adjustment. Actuarial gains and losses would be determined on a market value basis or a basis adjusted to market value, consistent with paragraph PS 3250.035.

For the 2016-17 Public Accounts, the Province would recognize an increase to HOOPP obligation for benefits, and an actuarial loss which offsets the increase to the obligation (See Appendix 4) as a result of the change in actuarial assumption. The actuarial loss will be amortized over the expected average remaining service life (EARSL) of the plan starting in the following year, 2017-18. There would be no fiscal impact to the Province in the year of change, which is 2016-17.

The expected impact to future years is estimated to be approximately an annual increase of $22 million to the HOOPP expense starting in 2017-18 ($166 million, being amortized over 13 years, plus approximately $9 million for additional interest expense due to the increase in obligation). The total expense for HOOPP is forecasted at $554 million for 2017-18 ($452 million in pension expense, and $102 million valuation allowance to write-off the net pension assets). The HOOPP is forecasted to be in an asset position starting from 2017-18 and is projected to remain in an asset position even with the increase of $166 million in obligation. Therefore, any increase in pension expense starting from 2017-18 will be offset by a lower valuation allowance and consequently, the fiscal impact due to this indexation assumption change will be nil in future years.

Subsequent Event Analysis

According to PS 2400 subsequent events:

.01 This Section establishes standards on how to account for and disclose events occurring between the financial statement date and the date of their completion. Financial statements are prepared to reflect a government's financial position at a particular date and changes in financial position for a period ended on that date. However, events occurring after the financial statement date may indicate a need to adjust items or to make specific disclosures in those statements. Therefore, in preparing financial statements, the implications and financial effects of subsequent events would be considered.

.02 The period during which subsequent events are considered will depend on the government's managerial structure and procedures followed in completing the financial statements. The appropriate cut-off point for subsequent events is a matter of judgment taking into account the particular circumstances and reporting requirements.

.03 In general, there are two types of subsequent events:

(a) those which provide further evidence of conditions which existed at the financial statement date, and

(b) those which are indicative of conditions which arose subsequent to the financial statement date.

Since the Province received the letter on April 28, 2017, this is considered a subsequent event for the 2016-17 Public Accounts. In addition, it provides further evidence of conditions which existed at the financial statement date. According to PSAS, the financial statements should be adjusted for conditions that existed at the date of the financial statements:

.08 Subsequent events may provide additional information relating to items included in the financial statements and may reveal conditions existing at the financial statement date that affect the estimates involved in the preparation of financial

statements. All such information that becomes available prior to completion of the financial statements would be used in evaluating the estimates made and the financial statements would be adjusted where necessary. For example, the restructuring of the terms of the loans receivable in a significant government lending program, subsequent to the date of the financial statements, may be indicative of the underlying financial situation of the program and its debtors at the date of the financial statements. If the provision for those loans were inadequate, adjustment of the financial statements would be required.

.09 *Financial statements should be adjusted when events occurring between the date of the financial statements and the date of their completion provide sufficient, additional evidence relating to conditions that existed at the date of the financial statements.* [MARCH 1997]

Based on the HOOPP's estimate of the impact to the Province's 2016 interim valuation, the adjustment would be an increase to the Province's HOOPP obligation of $166 million and an offsetting actuarial loss. The net liability position for HOOPP as reported on the financial statements will remain unchanged. However, the increase in pension obligation and decrease in actuarial gain will be disclosed in the details of the pension liability in Note 6 (Appendix 4). There will be no impact to the 2016-17 statement of operations.

Recommendation

HOOPP made a change effective December 31st, 2016 to its actuarial assumptions reflecting an allowance for future inflation protection for terminated members who choose to take a lump-sum payout. The change was communicated to the Province on April 28th, 2017 (subsequent to year end but before the financial statement completion date).

Based on the above analysis and opinions obtained from external consultants and IPPD, receipt of the letter from HOOPP is a subsequent event which provides further evidence of conditions which existed at the financial statement date (i.e. March 31, 2017). The Public Accounts of the Province for the year ended March 31st, 2017 should therefore be adjusted accordingly.

The change in actuarial assumption does not impact the financial statements. The net pension liability position reported on the statement of financial positon remain unchanged because the increase to the obligation for benefits is offset by the corresponding increase to the actuarial loss, in which both components comprise the net pension liability at the year-end. The increase to the actuarial loss will be amortized into pension expense starting from 2017-18; therefore, there is no impact to the 2016-17 statement of operations. Due to the valuation allowance for HOOPP, there will also be no impact to the total expense for the future years.

However, the change will impact the pension disclosure included in Note 6 to the Public Accounts. Note 6 will be adjusted to reflect the change in actuarial assumption.

No additional disclosure is recommended for the change in assumption to HOOPP's valuation and the impact of the Province's valuation for future years for materiality reasons.

Prepared by: Patricia Ma

Reviewed by: Alicia Sun/Nadine Petsche

Date: June 7th, 2017

Appendix 1: HOOPP Letter

HOOPP
Healthcare of Ontario
Pension Plan

T 416-369-9212 1 York Street, Suite 1900 hoopp.com
F 416-369-0225 Toronto, Ontario M5J 0B6

April 28, 2017

Cindy Veinot
Assistant Deputy Minister & Provincial Controller
Office of the Provincial Controller Division
Ministry of Finance
2nd Floor, Frost Building South
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

DELIVERED VIA E-MAIL

AND

Alex Killoch, Director
BPS Pension Branch, Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Ms. Veinot and Mr. Killoch:

Subject: INFORMATION REQUIREMENT FROM HOOPP

In the letter sent to HOOPP by Leah Myers on December 15, 2016 requesting actuarial and financial information as at December 31, 2016 for preparation of the Province's 2017 Budget and 2016-17 financial statements, it was also requested that by April 28, 2017, HOOPP communicate whether to the best of our knowledge, there were any events between December 31, 2016 and March 31, 2017, which would affect the valuation results in a material way.

Subsequent to providing you with our response letter of January 26, 2017, HOOPP entered into discussions with the provincial regulator (Financial Services Commission of Ontario) which led to HOOPP making an assumption change within its year-end 2016 financial results. Specifically, the assumption change reflects an allowance to include future inflation protection for post-2005 service for members who are assumed will terminate from HOOPP and choose a lump sum (commuted value) option. The impact of this change using HOOPP's going concern actuarial basis as of December 31, 2016 was an increase to the liabilities of $1 billion. Further disclosure of this can be found in HOOPP's annual report, which is posted on HOOPP's website.

One further note relates to your request that HOOPP present two different sets of year-end financial results. One is based on HOOPP's contractual indexing provision (i.e., with no future inflation protection for post-2005 service). A second set of results is prepared assuming future inflation protection at 75% of CPI is provided for post-2005 service.

The liability impact of this assumption change would have a similar impact to the results we provided based on the contractual indexing provision (item #1 from our January 26 letter).

Although it's not clear to us why the second set of results is needed at all by the Province, nor exactly how these two different sets of results would be used in the Province's annual reporting, given the additional inclusion of future inflation protection for post-2005 service, the impact to this set of results would be much smaller.

Please do not hesitate to contact me if you have any questions or require any further information about this.

Sincerely,

HEALTHCARE OF ONTARIO PENSION PLAN

Greg Tebbutt
Senior Director, ALM

Cc: Leah Myers, Assistant Deputy Minister of Finance (via email)
Robert Pomykacz, Manager, Public Sector Pension Policy (via email)
David Miller, HOOPP General Counsel & SVP, Governance

Appendix 2: Key Assumptions Used in the Province's and HOOPP's Valuation

Assumption	Province's 2016-17 Valuation	HOOPP 2016 Valuation
Rate of Return/Discount Rate	5.75%	5.45%
Salary growth rate	4.00%	3.50%
Inflation indexation	75% of CPI on post-2005 contributory service	100% of CPI on commuted values for all service

Appendix 3

The history of CPI indexation of the plan is summarized in the following table:

Year of Change	Years of Service Credited	% Indexation
N/A	inception- 2005	75% of the prior year's increase in CPI (guaranteed)
2006	2006-2013	75% of the prior year's increase in CPI (ad hoc)
2014	2014-2016	100% of the prior year's increase in CPI (ad hoc)
2015	2002-2013	Catch up from 75% to 100% of prior year's increase in CPI for retired and deferred members (ad hoc)

Appendix 4

The below is an extract of Note 6 of 2015-16 Public Accounts for illustrative purposes. For 2016-17, the Obligations for benefits will increase by $166 million and the Unamortized actuarial gains will decrease by $166 million resulting in nil impact to the total pensions liability of the Province for the change in assumption for HOOPP.

6. Pensions and Other Employee Future Benefits

Pensions and Other Employee Future Benefits Liability (Asset)

As at March 31 ($ Millions)	2016 Pensions	2016 Other Employee Future Benefits	2016 Total	2015 Total
Obligation for benefits	$117,542	$10,999	**$128,541**	$124,726
Less: plan fund assets	(141,749)	(562)	**(142,311)**	(129,880)
Unamortized actuarial gains	12,649	305	**12,954**	6,084
Adjustments[1]	2,246	9	**2,255**	2,221
Accrued liability (asset)	(9,312)	10,751	**1,439**	3,151
Valuation Allowance[2]	10,668	–	**10,668**	–
Total	**$1,356**	**$10,751**	**$12,107**	$3,151

[1] Adjustments for pensions consist of:
i) differences for amounts reported by the pension plans at December 31, instead of the Province's year-end of March 31;
ii) unamortized difference between employer and employee contributions for jointly sponsored pension plans; and
iii) amounts payable by the Province that are reflected as contributions in the pension plan assets.

[2] Valuation allowances are related to the pension assets for the Ontario Teachers' Pension Plan and for the OPSEU Pension Plan (Note 18).

Appendix 5: Other Considerations

Consultations

OPCD consulted with external consultants on the issue. Their opinion was that the Province is not required to revise their assumptions due to a change in the HOOPP's assumptions but may choose to do so noting that the requirements under a funding valuation and accounting valuation according to PSAS can be different and as such, an adjustment may not be necessary for the Province's financial reporting purposes.

OPCD also consulted with IPPD at MOF who noted the pattern for HOOPP to provide ad hoc inflation indexation at 100% of CPI increase (for all active members). According to PSAS:

> *In other retirement plans, regular benefit increases for inflation protection may be provided even when such protection is not promised in a contractual agreement or in legislation. For those plans, careful analysis and professional judgement are needed to determine the substance of a government's obligation. If a regular pattern of benefit increases can be established over a reasonable period, it may be appropriate to incorporate the cost of such inflation protection in the cost of retirement benefits earned to the financial statement date and reported as an accrued benefit obligation. (PS 3250.032)*

Therefore, the Province may consider an assumption change to provide for inflation protection at 100% of CPI increase (for all active members) for future valuations if the pattern of providing ad hoc inflation protection of 100% of CPI increase persists.

image003.pdf

TBS

Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; Keates, James (TBS) [James.Keates@ontario.ca]
Subject: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx
Date: Thursday, October 27, 2016 08:53:22

From: lucy.durocher@ca.pwc.com
Sent: October 27, 2016 8:47 AM
To: Petsche, Nadine (TBS)
Cc: Keates, James (TBS); Virani, Shyrose (TBS)
Subject: Re: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx

Hi Nadine,

I could do a call at the following times:

Today - between 2:30 and 4pm
Friday - any time in the afternoon up to 5pm.
Monday morning - before 11am.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Keates, James (TBS)" <James.Keates@ontario.ca>, "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
Date: 10/26/2016 05:40 PM
Subject: Re: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx

---

Thanks Lucy.
Please let us know your availability for a call later this week/early next week. N
From: lucy.durocher@ca.pwc.com

Sent: Wednesday, October 26, 2016 4:45 PM
To: Petsche, Nadine (TBS)
Cc: Keates, James (TBS)
Subject: Re: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx

Hi Nadine,

I have some suggested edits made to the attached and have also added responses into the comments where I thought my input was appropriate to explain the edits or explain no edits in some cases.

I also want to take a "clean" read of this later to make sure it flows.

In respect to the footnote 3 in 3060, it might be better to have a quick call to discuss how best to approach this.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 10/25/2016 04:32 PM
Subject: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx

Lucy,
As discussed, attached is the updated version of the paper reflecting additional edits from staff (track changes). Some additional work being done on interjurisdictional analysis that will follow.
Please let us know if you would like to discuss, and feel free to get in touch with Jim directly.
N[attachment "Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx" deleted by Lucy Durocher/CA/ABAS/PwC]

This e-mail is intended only for the person to whom it is addressed (the "addressee") and may contain confidential and/or privileged material. Any review, retransmission, dissemination or other use that a person other than the addressee makes of this communication is prohibited and any reliance or

decisions made based on it, are the responsibility of such person. We accept no responsibility for any loss or damages suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

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Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx.pdf

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); lucy.durocher@ca.pwc.com; Keates, James (TBS)
Cc:	"lucy.durocher@pwc.com"
Subject:	Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx
Start:	October 31, 2016 9:30:00 AM
End:	October 31, 2016 10:00:00 AM
Location:	teleconference 416-212-8014 passcode 1474532# (APFR Boardroom)

From: lucy.durocher@ca.pwc.com
Sent: October 27, 2016 8:47 AM
To: Petsche, Nadine (TBS)
Cc: Keates, James (TBS); Virani, Shyrose (TBS)
Subject: Re: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2_cvnp v2.docx

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http://www.pwc.com/ca

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To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
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Lucy Durocher
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PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Draft Position Paper.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Draft Position Paper
Date: Friday, October 21, 2016 16:16:11

Thanks for the update Lucy. I'm sure that Cindy won't mind receiving it tomorrow morning. I'll look forward to reviewing the draft.

Take care,

Nadine

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: October 21, 2016 4:15 PM
To: Petsche, Nadine (TBS)
Subject: RE: Draft input to position paper (background)

Hi Nadine,

The paper is coming together, but it is taking a bit longer then I expected. I'd like to work on it a bit more this evening, so "end of day" today seems a bit ambitious. Would you rather than I send you what I have at end of day (5pm) for you to circulate for initial comments from Cindy or send it later, say tomorrow morning.

Let me know.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

Draft SOW for your review.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Draft SOW for your review
Date: Friday, September 16, 2016 12:38:02
Attachment 1: PWC SOW Pensions Accounting Opinion 20160915.docx

---

Lucy,

Further to your discussion with Nadine Petsche, Director of Accounting Policy and Financial Reporting, please find attached a copy of the draft SOW for the work related to pensions accounting.

Please provide your suggested edits directly to me. Please call if you have any questions or would like to discuss.

Thanks.

Shyrose Virani

416 325 1448

PWC SOW Pensions Accounting Opinion 20160915.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective [insert date].

PricewaterhouseCoopers LLP (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of June 16, 2014 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$xx0,000.00, excluding HST.

4. *Project Start Date:* September 15, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide an accounting opinion regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pensions on the consolidated financial statements of the Province under Public Sector Accounting Standards.

   Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting opinion, including discussions with the Office of the Auditor General.

   Vendor agrees that the accounting opinion or a summary of it may be disclosed by Ontario to the public, including publication of the opinion in documentation that may be accessible to or intended for the public.

   [insert other services/deliverables required, and any terms and conditions in respect of the accounting opinion.]

7. *Ownership and Licences* - **Attachment E** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be [insert name], who is the [insert title].

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. [*Charges On Per Diem Rate Basis*– The Vendor and the Client agree that Work performed under this Statement of Work will be charged on a Per Diem Rate basis.] [TBD]

13. *Billing and Payment Process* – The Vendor shall invoice the Client in accordance with the requirements of the Master Agreement. Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	**Individual's Role and Experience Level**	**Service Category**	**Per Diem Rate** [TBD]
[insert name]	General Consultant, Level 2	Service Category 2	$
[insert name]	General Consultant, Level 2	Service Category 2	$
[insert name]	General Consultant, Level 2	Service Category 2	$

[Note to Draft: Confirm role and experience level and service category.]

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client:	Treasury Board Secretariat, Office of the Provincial Controller Division
Branch:	Accounting Policy and Financial Reporting
Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Clients designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all Confidential information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

18. *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**[insert address]**
Vendor Representative:	**[insert name and title]**
Telephone number:	**[insert telephone number]**
E-mail:	**[insert email address]**
Backup Vendor Representative:	**[insert name]**
Telephone number:	**[insert telephone number]**
E-mail:	**[insert email address]**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: _____

Name: _____

Title: _____

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor.

Draft amendment letter.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
CC: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
Subject: Draft amendment letter
Date: Tuesday, September 13, 2016 15:32:47
Attachment 1: Document69.docx

Matt,

As discussed, please find attached the draft letter for edit. Please call if you have any questions.

Nadine

Document69.pdf

September 13, 2016

Martin Raymond
1190 Avenue des Canadiens-de-Montréal,
Montréal, Quebec
Canada
H3B 0M7

Attention: Mr. Martin Raymond

To Whom It May Concern:

RE: Proposed change to Statement of Work No. MOF-OPCD-17 dated July 21, 2016, ("the Statement of Work") made between Her Majesty the Queen in right of Ontario as represented by the President of Treasury Board and Deloitte LLP.

As you know, an accounting opinion on the complex pension-related accounting matter was not anticipated by the parties. As a result, additional support will be required from Deloitte LLP in addition to the original work reflected in the SOW.

We understand that a separate engagement letter will apply to this engagement. The purpose of this letter is to document our agreement to increase the Ceiling Price under the Statement of Work by $XX,000.00 for the additional work required to undertake and deliver the work required for an accounting opinion.

This letter is sent to you in duplicate. Please indicate your receipt of this letter and your agreement to the change in Ceiling Price by signing where indicated on both copies, and returning the duplicate copy within five days of receipt of this letter.

This letter, when signed by both parties, will constitute a Change Order to the Statement of Work. The parties confirm that, except for the change referred to above, including a separate engagement letter for the envisioned accounting treatment, the Statement of Work will remain unchanged and unmodified.

Thank you for your continued cooperation and support.

Sincerely,

Nadine Petsche
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller Division

The undersigned hereby acknowledges receipt of this letter and agrees to the above on behalf of Deloitte LLP as of the date indicated above.

Deloitte LLP

Date:

Per: _____
Name:
Title:
Deloitte

I have authority to bind Deloitte LLP

CAUTION - THIS FILE RELATES TO A MATTER IN WHICH CINDY VEINOT MAY HAVE A CONFLICT OF INTEREST IN THE PERIOD BEFORE SHE BECAME A PUBLIC SERVANT.

THIS FILE MUST NOT BE SHOWN TO OR DISCUSSED WITH CINDY VEINOT

Draft input to position paper (background).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Keates, James (TBS) [James.Keates@ontario.ca]
Subject: Draft input to position paper (background)
Date: Thursday, October 20, 2016 16:55:59
Attachment 1: Outline of position paper to JK PF tab2 v5.docx

---

Hi Lucy.

Sharing the draft 'background' section for the position paper for your review and consideration. If you have any ideas on how to integrate this with your section, we would welcome your thoughts.

Thanks.

Nadine

Outline of position paper to JK PF tab2 v5.pdf

Preamble

This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP.

As described in PSAS, a pension asset arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. Contributions reflect the funding objectives of the plan. The benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (or plan surplus for accounting purposes) in OTPP and OPSEUPP are an asset to the province and it is suitable to reflect them in the financial results.

The OAG disagrees with this position. The OAG 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 Ontario Teachers' Federation (OTF) with respect to how the surplus would be utilized such that it would provide a benefit to the Province, a pension asset in the Public Accounts is not appropriate.

Ontario had followed the same pension accounting treatment for all of the past 14 years. This had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals. There has been no change to the relevant PSAS (i.e. RETIREMENT BENEFIT, Section PS 3250) over the past 14 years.

A regulation was made to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The Province filed a time-limited regulation, which legislates the accounting for pension assets of its two jointly-sponsored

pension plans for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The impact of the change resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to write off the pension assets. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

What is being asked of the Expert Advisory Panel

The Expert Advisory Panel is being asked to review and deliver advice and recommendations to the government as to the application of PSAS to Ontario's pension assets. The future accounting by the Government of its pension assets will be guided by the report of the Expert Advisory Panel.

The Expert Advisory Panel 's advice and recommendations to the government will address:

- The requirement regarding control (or shared control) with respect to recognizing a pension asset for a defined benefit plan, as it relates to the pension plans reported by the Province of Ontario, including OTPP, OPSEUPP, HOOPP, and CAAT.
- Appropriate valuation techniques to measure a pension asset that take into consideration future decision making authority by plan sponsors.
- Recommendations to the Employee Future Benefits Task Force of the Public Sector Accounting Board (PSAB) regarding issues that should be considered in their review of the retirement and post-employment benefits standards.

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1.

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
1. It provides defined benefits.
2. The defined benefits are contributory benefits.

The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the Ontario Teachers' Federation represented by its Executive (the ”OTF") (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended;
e) A Funding Management Policy, attached as Appendix A to the Partners Agreement (FMP);
f) The Ontario Teachers' Pension Plan; and
g) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

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

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3. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
4. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).

> *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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5] The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (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, 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 inception of the plan in 1917). [7] 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. [8] 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 a JSPP, 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.

Additional exerts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix E.

Accounting for OTPP by the Province

[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).
[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/101791209401-l5e47lc2b-23f1-44e6-b5cld22e3e50dbc3lHow+ Contribution+Rates*HaverEvolved.pdf As noted above, for the period from January l, 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%/11.20lo versus l0.4yo/l2Vo, respectively). It js 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.
[8] See, for example, Section 3.09 and 3.11 of the FMP.

Since fiscal year 2001-2002, the Province has recorded a pension asset for OTPP on the Statement of Financial Position. A pension asset has arisen because the government's share (50%) of the total contributions to OTPP plus the actual investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense. The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

The different objectives of funding and accounting for a pension plan are addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.*

Paragraph PS 3250.051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: "Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…"

OTPP's most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website. The OTPP's public financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015.

The pension plan surplus for OTPP for Public Account purposes differs from the surplus reported on OTPP's standalone financial statements. OTPP's financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook, which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the funding surplus or deficit. Different assumptions are used in the respective

calculations. For example the discount rate used by OTPP in their financial statements is different than the rate used by the Province of Ontario. OTPP uses a discount rate based on the market rate of bonds issued by the Province of Ontario in accordance with IFRS (IAS 19). The Province of Ontario calculates pension obligations for OTPP based on the assumed rate of return on plan assets in accordance with Section PS 3250. A review was performed of the discount rates used by other Provincial pension plans. It was determined that OTPP is an exception in using a discount rate based on the cost of borrowing. Refer to Appendix G for a comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. Unqualified audit reports have been received for each of the years from the OAG on the Public Accounts.

RETIREMENT BENEFIT, Section PS 3250 of the PSA Handbook addresses the accounting of obligations for employee retirement benefits in government financial statements. The Province has followed this standard over the prior 14 years. Over this period of time, there have been no consequential changes to Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years.

The prior pension accounting for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals during this period of time.

Over the prior 14 years, the Province has classified OTPP as a joint defined benefit plan as per Section PS 3250 (this classification will be discussed more in this document). Over this period of time, the pension expense and pension liability (asset) for OTPP reported by the Province is reflected in Appendix F.

History regarding the PSA standards

As mentioned, the financial statements for the Province have been prepared over the prior 14 years in accordance with the PSA Handbook.

Standards in the PSA Handbook relevant to the accounting for pension assets (including the dates the standards were introduced into the Handbook) are as follows:

- FINANCIAL STATEMENT CONCEPT, Section PS 1000 (a foundational section issued in January 2003)
- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015; this new standard provides additional guidance on the various components of the asset definition, it does not change the existing definition)
- RETIREMENT BENEFIT, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, Section PS 3250 which was based on Accounting Statement No. 5)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 which is effective in for periods beginning on or after April 1, 2017. As indicated

above, Section PS 3210 provides additional guidance on the various components of the existing asset definition; it does not change the definition.

GOVERNMENT PARTNERSHIPS, Section PS 3060 addresses the accounting of a contractual arrangement between the government and party or parties where there is shared control. This paper will consider the relation between government partnerships and joint defined benefit plans and the corresponding accounting.

FINANCIAL STATEMENT CONCEPTS, Section PS 1000 includes general concepts and principles reflected throughout the PSA Handbook. For example, the definitions of different types of elements (including an asset) are included in Section PS 1000. General recognition and measurement criteria are also included in Section PS 1000.

The focus of the following analysis is on the accounting requirements in RETIREMENT BENEFIT, Section PS 3250 as this standard specifically addresses the accounting for pension assets. Users of the PSA Handbook when determining the accounting for pension assets would apply the specific guidance in Section PS 3250 and refer to standards such as FINANCIAL STATEMENT CONCEPT, Section PS 1000 and GOVERNMENT PARTNERSHIPS, Section PS 3060 (with respect to shared control) to better understand the concepts and principles included in Section PS 3250.

Accounting Analysis

Question 1 – Recognition of a pension asset

The analysis below addresses whether the pension surplus in OTPP represents an asset to the Province of Ontario for purposes of preparation of the Public Accounts.

Standards in the PSA Handbook

As mentioned standards in the PSA Handbook relevant to the accounting for pension assets are:

- FINANCIAL STATEMENT CONCEPTS, Section PS 1000 (this section comprises part of the Conceptual Framework in the PSA Handbook)
- GOVERNMENT PARTNERSHIPS, Section PS 3060
- ASSETS, Section 3210 (this new standard provides additional guidance on the various components of the asset definition such as economic resources, future economic benefits and control)
- RETIREMENT BENEFIT, Section PS 3250

Included in appendix A is the definition of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and newly issued guidance on the definition included in ASSETS, Section 3210. While Section PS 3210 is only effective for periods beginning on or after April 1, 2017, this guidance will be considered as it is meant to clarify the existing asset definition.

RETIREMENT BENEFIT, Section PS 3250 – Purpose and Scope

A government applying the PSA Handbook will first refer to RETIREMENT BENEFITS, Section PS 3250 in reporting their sponsored pension plans. The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250, paragraph .003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

RETIREMENT BENEFIT, Section PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*

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

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

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

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

A joint defined benefit plan (JDBP) is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. The OTPP is a contractual arrangement between the Province and OTF in which:

(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees (addressed in paragraph 8 of the Partners' Agreement for example);

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example).

Concept of Shared Control

Included in the definition of a JDBP is the concept of shared control. Points (c) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of shared control is also included in the PSA Handbook in GOVERNMENT PARTNERSHIPS, Section PS 3060.

The similarity between the definitions of a JDBP and a government partnership are demonstrated in Appendix B to this paper. As indicated previously, RETIREMENT BENEFITS, Sections PS 3250 and GOVERNMENT PARTNERSHIPS, Section PS 3060 are standards in the PSA Handbook that were introduced into the PSA Handbook in 2001 and 1999 respectively and have not changed consequentially since.

The concept of shared control is not however addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Guidance on control is included in these sections but not shared control.

Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. On the introduction into the PSA Handbook of Section PS 1000, the concept of shared control was not removed from Sections PS 3060 and PS 3250. PSAB did not consider Sections PS 3250 (and Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

For your information, included in Appendix C is the legal opinion prepared by lawyers, Koskie Minsky, comparing access to the pension surplus of OTPP relative to pension plans in British Columbia. The Province of British Columbia does not include a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

Similarly, the accounting for pension plans by the Province of New Brunswick is different than the Province of Ontario's accounting for OTPP. In New Brunswick, the Board of Trustees for each pension plan (of which 50% of the members are appointed by the Province) is responsible for the plan assets. The Province has no access to the assets, cannot control their use, and is not responsible for any losses. As a result the Province of New Brunswick does not include a pension asset in their financial statements.

RETIREMENT BENEFIT, Section PS 3250 – Accounting for a JDBP

As OTPP meets the definition of a JDBP, the Province should account for the plan in accordance with the requirements in paragraphs .079 to .082 of RETIREMENT BENEFITS, Section PS 3250 which are as follows:

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

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

.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]

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

The OTPP has the characteristics outlined in paragraph .079 and .080 of RETIREMENT BENEFITS, Section PS 3250 including:

- the Government shares the risks and rewards with the other sponsors of the plan (i.e. the OTF);
- there is a formal agreement where the sponsors share control;
- the sponsors appoint a governing board of directors with equal representation; and
- funding contributions are shared mutually between the Government and the plan members.

The classification of OTPP as a JDBP has been consistent since 2001 and has been accepted by the OAG.

We would note that paragraph .081 of RETIREMENT BENEFITS, Section PS 3250 clearly states that a government should account for its portion of the plan in accordance with the standards for defined benefit plans. As a result, the Province of Ontario accounts for its proportionate share of OTPP (50% of the plan). Similar to GOVERNMENT PARTNERSHIPS, Section PS 3060, the requirement to account for its portion of the plan under Section PS 3250 is equally applicable if the pension plan is in a surplus or deficit position.

The concepts of recognizing your portion of an asset or liability as previously discussed is consistent with GOVERNMENT PARTNERSHIPS, Section PS 3060.

RETIREMENT BENEFITS, Section PS 3250, paragraph .081 directs the JDBP to account for its pension assets and liabilities consistent with the accounting under a defined benefit plan. Therefore, other requirements in Section PS 3250 are to be followed for OTPP including the following:

Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)

.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]

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

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

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

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

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

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

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

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

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

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

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

While many of the above paragraphs relate to measurement rather than recognition of an asset (and will be discussed in the following section of this paper), paragraph 3250.050 indicates "An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit…" In the glossary to Section PS 3250, expected future benefit is defined "… as a calculated amount representing the benefit a government expects to realize from a plan surplus." Paragraph .052 states "A government may benefit from an accrued benefit asset either by withdrawing surplus assets or

by taking a contribution holiday or receiving a refund of contributions." PS 3250.059 as provided above indicates "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

Paragraph .052 is more general regarding the ways a government can benefit from a surplus (either through a withdrawal of the surplus or a reduction in future contributions) while paragraph .059 addresses specifically "a" key factor, the ability to withdraw the surplus. Paragraph .059 is not indicating the only way a government can benefit from a surplus in a pension plan is through the ability to withdrawal the surplus.

In paragraph PS 1000.36, the first characteristic of an asset is "they embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows." The ability to benefit from the surplus through a reduction in future cash flows is consistent with the general definition of an asset.

The government's position has been that access to the expected benefit of the surplus is through reduced future contributions and not through withdrawals of the surplus. The following analysis considers the Government's ability to benefit from the surplus in OTPP through either a withdrawal of the surplus or through a reduction in future contributions.

Through withdrawal of the surplus

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, paragraph 3250.059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

The TPA for OTPP does not provide for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution, the Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

The OAG's position is that the government should not recognize a pension asset based on its ability to benefit from the surplus in OTPP through withdrawal of the surplus as the government does not have a legally enforceable right to the surplus.

Through reducing future contributions

As mentioned previously, PS 3250.059 indicates "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal." PS 3250.59 is clear that expected future benefit can only be asserted where the government has a current legally enforceable right to withdraw assets from the Plan. PS 3250.59 introduces the concept of a legally enforceable right, however it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions. Had PSAB intended legal enforceability to be the test, they would have included that notion throughout the guidance, instead of only raising it in the context of a withdrawal of surplus.

The concept of "legally enforceable" is not widely used throughout the PSA Handbook – the term is used once in two other standards Section PS 3450, FINANCIAL INSTRUMENTS (with respect to the right to offset) and PS 3260, LIABILITY FOR CONTAMINATED SITES (with respect to environmental standards to be complied with). The concept of legally enforceable is not included in the definition of an asset in

Section PS 1000 and in the guidance of an asset in Section PS 3210. Concepts in the PSA Handbook are generally principle based rather than rules based

As mentioned previous, paragraph .052 states “A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. Paragraph .052 notes that an accrued benefit asset may be impaired if a government "is not entitled to benefit fully" for example there may be uncertainties relating to a government's legal rights to use a plan's surplus. As such, the Province's present legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability. Specifically, the amount of Pension Asset that gets recorded needs to be subject to considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a Pension Asset.

Similar to the discussion regarding the withdrawal of the surplus, use of the surplus through reducing future contributions must be examined considering the constating documents of OTPP. A review of the constating documents indicate:

1. Paragraph 10(1)3 of the TPA 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 TPA 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). 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.

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 (refer to Appendix G for a history of surplus utilization for OTPP). 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 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).

While not having a legally enforceable right to reduce its future minimum contributions Section PS 3250 requires that management take into consideration "uncertainties as to a government's legal right to use a plan's accounting surplus" (3250.52). The standard does not require that there be no uncertainty in order to recognize an asset. This interpretation would not be consistent with the balance of the framework developed to account for defined benefit pension plans. As previously mentioned, the definition of an asset in Section PS 1000.35 includes the phrase ".. future economic benefits are expected to be obtained."

Pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to

the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". Expected does not equate to certainty.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (3250.42) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (3250.41). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. 3250.57 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province of Ontario has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on Plan Assets, which is one of the acceptable references suggested on PS 3250.44.

The OAG and the Government differ regarding whether it needs to be "expected" that the Government will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in paragraph .059. The Government considers that it needs to be expected that future economic benefits are to be obtained as reflected in the definition of an asset in Section PS 1000 and as reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to use a plan surplus.

CONTINGENT ASSETS, Section PS 3320, paragraph .07 indicates "The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset. For example, even though there may be measurement uncertainty related to income tax receivable, there is nothing uncertain about the fact that this asset exists. Any uncertainty is related solely to the amount thereof." Based on past history of surplus utilization for OTPP and based on the constating documents, expected future benefits for the Government are present. The uncertainty as with many types of assets relates to measurement uncertainty which will discussed further below.

Conclusion re: recognition [To be completed]

Section PS 3250 applies

OTPP meets the definition of a JDBP

OTPP's pension surplus meets the definition of an asset as it is expected that the Province will benefit from the surplus through reduced future contributions based on the constating documents and past history of surplus utilization - it is the form that the benefit will take which is uncertain not the benefit - uncertainty relates to measurement uncertainty not existence uncertainty

The Province has shared control over the surplus of OTPP (50%)- The Province is to recognize its portion of the pension asset of OTPP as reflected in PS 3250 and PS 3060

Question 2 – Measurement of a pension asset

Several of the paragraphs PS 3250.050 to .059 in RETIREMENT BENEFITS, Section PS 3250 address measurement of a pension asset.

Paragraph PS 3250.050 indicates "An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit..."

Paragraph .056 provides guidance on calculating the expected future benefit indicating "*A* government determines its expected future benefit as the sum of: a) the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus; and b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations.

Paragraph PS 3250.055 indicates "The objective of the standard in paragraph PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Note that PS 3250.052 requires one to consider "uncertainties as to a government's legal right to use a plan's accounting surplus."

After determining whether the Province has a pension asset, the next decision is whether the pension asset meets the recognition criteria in the PSA Handbook.

Other guidance in the PSA Handbook on recognition and measurement

Recognition and measurement is also addressed in the guidance in Section PS 1000 along with the recognition criteria for an asset or liability.

The recognition criteria in paragraph PS 1000.55 indicate"... the item has an appropriate basis of measurement, and a reasonable estimate can be made of the amount involved .."

Furthermore MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe

would be a useful addition to the current year financial statements. PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.*
>
> *.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.*

For an asset to be recognized it must be measurable.

PS 3250.53 to .58 lay out a mathematical calculation that determines the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in PS3250.055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where realization includes a reduction in future contributions. A valuation allowance is recorded against the Pension Asset to limit the asset value, if necessary, based on this analysis.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. This calculation is further described in PS 3250.56(a), which sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per PS 3250.81 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the Pension Asset value to be recorded in the accounts. For example, if the Pension Asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the Pension Asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for judgment in the above calculation is in the determination of future minimum contributions required to be made by the government regardless of any surplus. There is no further guidance in S 3250 as to how this calculation should be performed and what restrictions or parameters should be factored into this calculation.

Determining the number of years of contributions to include should involve consideration of legal uncertainty as set out in PS 3250.52. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the following (due to the magnitude of the OTPP asset, most of these considerations focus on that plan):

- The contractual agreements between the Sponsors that provide for the sharing of risks and benefits.
- There is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'.
- The specific framework within the Funding Management Plan for OTPP that contemplates specific funding zones and when contribution reductions will be discussed by the sponsors.
- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.98 for the 2015 change, and $1.68 for the 2014 change).
- Other regulatory requirements, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan.

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (PS 2130.03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of

action. As noted in PS 2130.13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

Actuarial reports were completed to assess the requirement for a valuation allowance. The results of those reports are summarized here:

Plan	**Asset recorded by Province (in billions)**	**Asset ceiling computed (in billions) and assumption re: years of contributions**	**Number of years contributions could be made without resulting in a valuation allowance**
OTPP	$ 10.1	$29.3 (based on 11 years of contributions noted in the funding report as the period additional contributions are required)	33

The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (3250.56(a)). There is no guidance on the meaning of minimum contributions for purposes of this calculation in PS 3250. For purposes of the OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

An important consideration in performing these asset ceiling calculations is how long contributions will be required to be made. Under the Partners' Agreement, the parties are mandated to negotiate benefits and contributions every three years as a minimum and if agreement is not reached, it is reasonable to expect that a change in contributions might occur rather than the 'status quo' being retained. In addition to the above calculations, we have considered the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that no valuation allowance is required.

We would be happy to share this analysis with you, in addition to the actuarial reports we have already provided.

We acknowledge that the estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is permissible under PSAB and consistent with rates followed by other senior Canadian governments. Historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets on the Province's books.

For information purposes, refer to Appendix D for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.

Conclusion re: measurement [To be completed]

OTPP pension assets should continue to be recorded on the books of the Province

We recognize that the estimation and judgement used in the assessment of whether a valuation allowance is required is significant

Reasonable estimates of when the surplus will result in contribution reductions were used

Discount rate is in accordance with PSAS

Based on the results of those models to date, no valuation allowance appears to be required

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Appendix A – Guidance in the PSA Handbook - FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210

Guidance in FINANCIAL STATEMENT CONCEPTS, Section PS 1000

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

.36 Assets have three essential characteristics:

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

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

(c) the transaction or event giving rise to the public sector entity's control has already occurred. [Former paragraph PS 1000.36 retained in Archived Pronouncements.]

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

(a) no future economic benefit;

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

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

(paragraph PS 1000.38 deleted) [Former paragraph PS 1000.38 retained in Archived Pronouncements.]

.39 **Financial assets** are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations.

.40 A financial asset is any asset that is:

(a) cash;

(b) a realizable asset that is convertible to cash;

(c) a contractual right to receive cash or another financial asset from another party;

(d) a contractual right to exchange financial instruments with another party under conditions that are potentially favourable to the government;

(e) an equity instrument of another entity;

(f) an investment in a government business enterprise or government business partnership;

(g) a financial claim on an outside organization or individual; or

(h) an inventory or item for sale that meets the criteria in FINANCIAL STATEMENT PRESENTATION, paragraph PS 1201.055. [Former paragraph PS 1000.40 retained in Archived Pronouncements.]

.41 Non-financial assets include tangible capital assets, and other assets such as prepaid expenses and

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inventories of supplies.

.42 **Non-financial assets** are acquired, constructed or developed assets that do not normally provide resources to discharge existing liabilities, but instead:

(a) are normally employed to deliver government services;

(b) may be consumed in the normal course of operations; and

(c) are not for sale in the normal course of operations.

RECOGNITION

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

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

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

.55 The recognition criteria are as follows:

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

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

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

.57 Purchased natural resources and Crown lands are recognized in government financial statements. However, when natural resources and Crown lands have been inherited by the government in right of the Crown and have not been purchased, they are not given accounting recognition as assets in

government financial statements. These items are not recognized as assets because the costs, benefits and economic value of such items cannot be reasonably and verifiably quantified using existing methods. Similarly, art and historic treasures are also not recognized as assets.

.58 In the absence of appropriate public sector recognition and measurement criteria for intangibles, all intangibles, including those that have been purchased, developed, constructed or inherited in right of the Crown, are not recognized as assets in government financial statements. The intangible often called "human capital" that embodies the talent or intellectual capital of government employees is not recognized as an asset under existing accounting principles.

.59 Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting. The accrual basis of accounting recognizes the effect of transactions and events in the period in which the transactions and events occur, regardless of whether there has been a receipt or payment of cash or its equivalent. Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied. Accrual accounting recognizes an asset until the future economic benefit underlying the asset is partly or wholly used or lost.

MEASUREMENT

.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

.61 Present value is the discounted amount of future cash flows expected to be received from an asset or required to settle a liability. Present value is not a basis of measurement, but a valuation technique that may be used within historical cost-based or current-value models. This technique is used in the government reporting model, for example, to estimate the cost of retirement benefits, when determining the estimated total expenditure for closure and post-closure care of a solid waste landfill site, and when determining the "grant portion" of concessionary loans and portfolio investments.

.62 Government financial statements are prepared on the basis that recognized economic resources used up are measured in financial terms with no adjustments made for the effect of a change in the general purchasing power of the currency during the period. Although a government's performance in the management of its service potential 2 is generally a focus more appropriate to the nature and objectives of government, it cannot entirely be measured in financial terms.

2. Service potential embodies both the quality of service provided and the efficiency with which it is provided.

.63 Financial statements are prepared on the assumption that the government is a going concern, meaning it will continue in operation, and will be able to realize assets and discharge liabilities and meet its statutory obligations in the normal course of operations for the foreseeable future.

Guidance in ASSETS, Section PS 3210

Economic resources

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

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

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

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

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

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

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

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

.09 Economic resources can be:

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

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

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

Future economic benefits

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

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

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

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public sector resources generate cash inflows because they have user fees associated with them.

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

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

Control

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

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

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

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

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

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

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

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

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

.22 Control of an economic resource and of access to the future economic benefits are essential characteristics of an asset, whereas possession or ownership is not. For example, a public sector entity may control the economic resource and access to the future economic benefits through a capital lease arrangement yet not own the economic resource.

.23 A public sector entity's ability to regulate an economic resource does not, in and of itself, constitute control of an asset. A public sector entity may establish the regulatory environment in an

industry or sector within which organizations operate and impose conditions or sanctions on their operations. For example, a pollution control authority may have the ability to close down the operations of entities that are not complying with environmental regulations. However, this power does not constitute control because the pollution control authority's interest extends only to the regulatory use of the economic resources and does not include the ability to control access to the future economic benefits.

.24 A public sector entity may act as trustee when it administers trusts on behalf of the beneficiaries specified in the agreement or statute. As trustee, the public sector entity merely administers the assets, following the terms and conditions set out in the agreement. It does not control the asset because it does not have access to the future economic benefits. Those benefits flow to the beneficiaries.

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Appendix B - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the	Consistent in concept with the definition of a GP focusing on investments in the partnership and the

		non-government sponsor;	definition of a JDBP focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix C – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan (''PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[9] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect to ongoing PSPP surpluses

[9] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the same way as the other BC Plans.

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The Partners have the authority (s.14(2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use

ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

We trust that these comments have been of assistance to you. Should you have any questions in regard to them, please do not hesitate to contact the undersigned.

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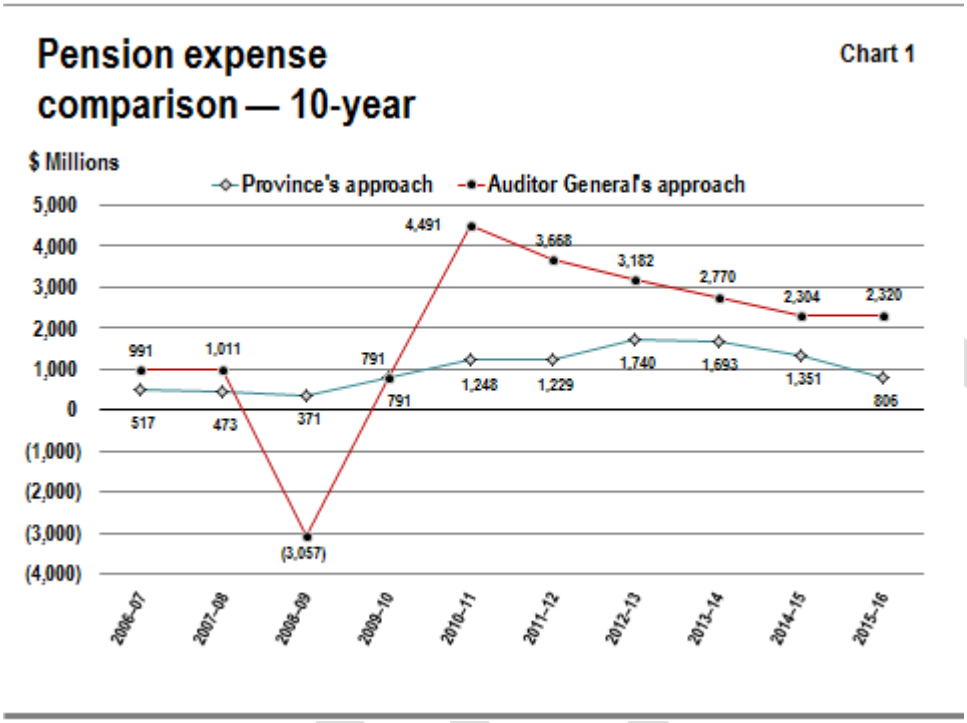
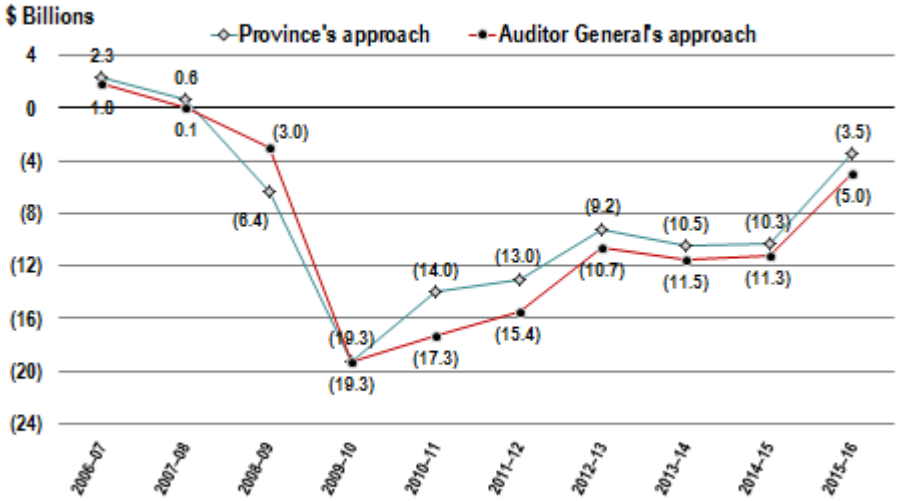
Appendix D - Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.



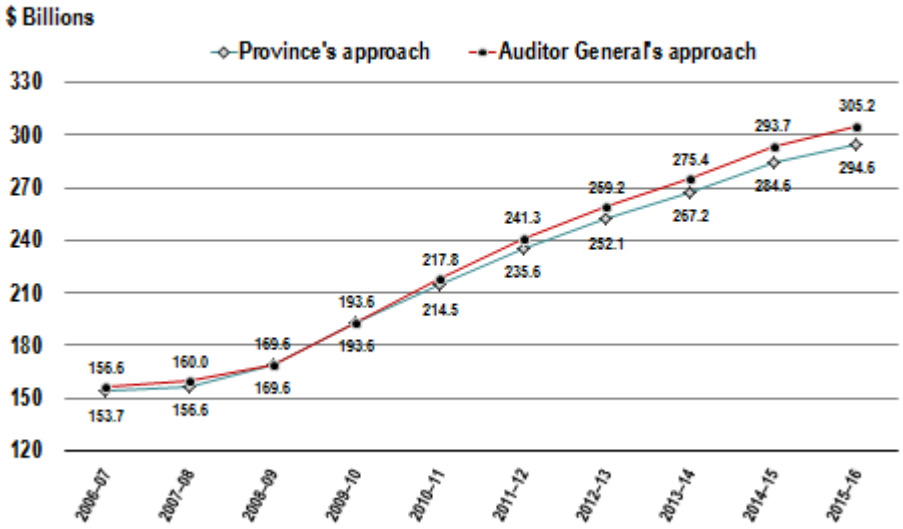
Surplus/(deficit) comparison — 10-year

Chart 2



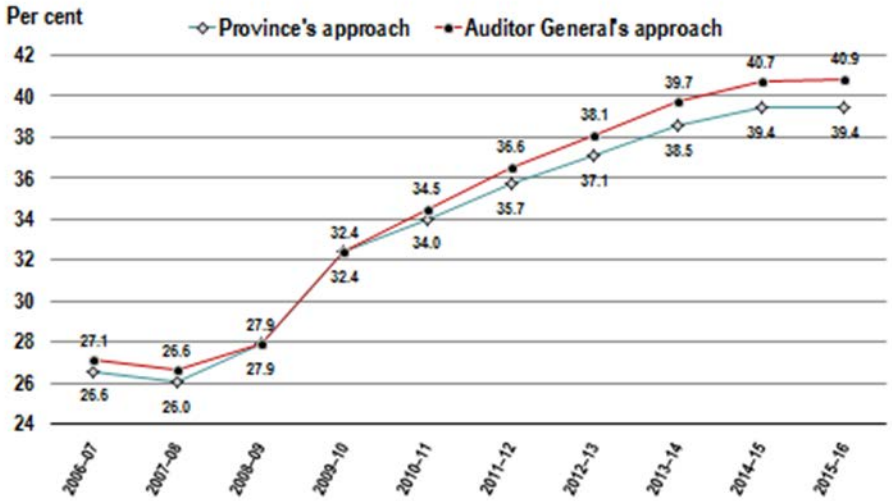
Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year

Chart 4



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Appendix E – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. By contrast, section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the Sponsors to the OTPP have the authority to utilize ongoing surpluses. The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every

three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

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

Funding Management Policy (FMP)

The FMP is an appendix to the Partners' Agreement that speaks to how the Plan should be funded and

how surpluses should be utilized by both parties. The protocol for the use of a surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP.
The FMP sets out a complex series of considerations surrounding funding management and the use of any excess of assets over liabilities. The FMP sets out a number of "funding zones", depending on the level of funding in the Plan. The following three are most relevant to addressing surpluses:
i) Restoration zone (Article 3 of the FMP) allows for a surplus to be utilized to "restore" foregone indexation and then to either increase benefits to the "run-rate benefit" level (i.e., the long-term target level) or to lower contributions (or a combination of these two options) (Section 3.06(e)).
ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).
iii) Permanent improvement zone is where the Plan is essentially fully funded and has the funding security desired to support permanent changes. Article V (Permanent Improvements) of the FMP provides for permanent actions that can be taken when Plan assets exceed current liabilities by more than 10% of current liabilities. In this regard Section 5.05 provides for actions that can be taken in respect of the amount that assets exceed current liabilities. Such actions can include changes to current benefits, current contributions, or both.

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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Appendix F – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	**2000-01**	**2001-02**	**2002-03**	**2003-04**	**2004-05**	**2005-06**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	**2006-07**	**2007-08**	**2008-09**	**2009-10**	**2010-11**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix G - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	5.95%	LT return on plan assets
Alberta				
Teachers' Post-1992 Pension Plan	7.00%	LT return on plan assets	7.25%	LT return on plan assets
Universities Academic Pension Plan	6.10%	LT return on plan assets	6.25%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)				
Local Authorities Pension Plan	5.80%	LT return on plan assets	5.80%	LT return on plan assets
Public Service Pension Plan	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Management Employees Pension Plan	6.40%	LT return on plan assets	6.40%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.75%	LT return on plan assets	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Special Forces Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan				
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.80%	LT return on plan assets	6.80%	LT return on plan assets
British Columbia				
Public Service Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec				
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	6.40%	LT return on plan assets less inflation
Newfoundland				
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets
Nova Scotia				
Nova Scotia Public Service Superannuation Plan (PSSP)	6.75%	LT return on plan assets	6.35%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	6.40%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba				
Civil Service Superannuation Plan	6.00%	LT return on plan assets	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.50%	LT return on plan assets	6.25%	LT return on plan assets

7

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			special payments	
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		

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).

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EY Pension services_ to-date and outstanding.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Shayan Jafrani [Shayan.Jafrani@ca.ey.com]; Uros Karadzic [uros.karadzic@ca.ey.com]
Subject: EY Pension services: to-date and outstanding
Date: Thursday, August 03, 2017 12:09:05
Attachment 1: image003.jpg

Hi Nadine,

As requested, please find below a list of services provided to-date, as well as the outstanding items to the end of September:

Services provided to-date related to year-end reporting and projections for the pension plans:

1. Accrued benefit asset recognition ("asset ceiling test")

a. Reviewed and provided documentation related to accrued benefit asset recognition for OTPP and OPSEUPP (most up-to-date version reflects all proposed changes)

2. Existing OPCD models review

a. Reviewed and provided recommendations on the existing models for year-end reporting and projections, for all Plans (OTPP, OPSEUPP, PSPP, CAATPP, HOOPP, and SRPs)

b. Provided an "audit checklist" for the existing models

c. Reviewed and provided recommendations on MRVA calculations, for all Plans

d. Reviewed and provided recommendations related to year-end adjustments

3. Adjustments

a. Considered and provided recommendations on the approach in determining the portion of the Plan the Province should include for consolidated reporting, all Plans

b. Provided two sets of comparative figures: proposed adjustments reflected as at (i) 1 March 2015 and (ii) 1 March 2016

c. Provided documentation on estimated impacts and narrative for each proposed adjustment

4. Remodeling

a. Updated existing model to reflect the proposed adjustments as at 1 March 2016 for OTPP, PSPP, and OPSEUPP.

b. Updated existing model to reflect the proposed adjustments as at 1 March 2017 for HOOPP and CAATPP.

c. All models were also updated to be more user friendly and improved for projection purposes. Walkthrough with OPCD staff on each of the remodelled workbooks

Other services provided to-date:

1. Other public plans research

a. Provided summary on other public plans in other Provinces (BC, Alberta) and identify ones which are comparable to the Province's

b. Provided a specific criteria checklist and plans for other provinces for further research considerations

2. ELHT (Employee Life and Health Trusts)

a. Provided support related to AG's questions

b. Provided analysis and documentation on the accounting treatment for ELHT, including comparison against shared risk pension plans

Outstanding:

1. Further support and/or changes to the remodelled worksheets upon OPCD/AG review, if any.

2. Preparation and delivery of training to staff (anticipating 3 half days, over the 2nd week of September: Pension accounting 101, PSAB, using the financial reporting and projection models for new hire)

It’s been a pleasure working with you. Wish you the best and maybe our paths will cross again in the near future!

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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To: E-IDservice@tritoncanada.ca [E-IDservice@tritoncanada.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Email Received in error (468bbfe2-a12c-416b-a4b0-85a454a5a3c4)
Date: Thursday, October 27, 2016 12:52:53
Attachment 1: Picture (Device Independent Bitmap) 1.jpg

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Is it possible to send again.
Note that we needed to check first if it was not a fraud email before entering since it appeared to be coming out of nowhere.

Thanks

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services
Deloitte
1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada
Tel / Direct : 514-393-7367
Fax : 514-390-4104
maraymond@deloitte.ca | www.deloitte.ca

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Employee Life and Health Trusts (ELHTs) - accounting treatment.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: Employee Life and Health Trusts (ELHTs) - accounting treatment
Date: Monday, March 27, 2017 17:46:21
Attachment 1: image002.jpg
Attachment 2: ELHTs Accounting Treatment (EY 27 March 2017).pdf

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Hi Nadine,

As requested, we have prepared the attached document discussing the following topics:

1) Accounting treatment related to the provisions of the ELHTs under PSAB 3250/3255 (and the associated risks to the school boards)

2) Comparison of the ELHTs with Shared Risk Pension Plans

Both Shayan and I will be at Queen's Park tomorrow. Let us know if you have any comments. We are available if you would like to discuss prior to our meeting on Wednesday.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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ELHTs Accounting Treatment (EY 27 March 2017).pdf

Ernst & Young LLP
222 Bay Street, P.O. Box 251
Toronto, Ontario M5K 1J7

27 March 2017

Accounting Treatment - Employee Life and Health Trusts

OPCD has asked EY to comment on the accounting treatment related to the provisions of benefits from the Employee Life and Health Trusts ("ELHTs") under the Public Sector Accounting Standards.

Background

Historically, health, life and dental benefits were provided to employees in Ontario's educator sector through a multitude of individual plans administered separately by the Ontario school boards. To improve the cost-efficiency and delivery of benefits, all individual benefit plans are consolidated into six Employee Life and Health Trusts[1], each covering a certain group of employees. Each ELHT is established to meet the definition of an ELHT under the Income Tax Act Sc. 144.1. Benefits are provided through a joint governance structure between the bargaining/employee groups, school board trustees associations and the Government of Ontario under the ELHTs.

The ELHTs are intended to provide benefits to employees during their employment years. There are also separate retiree provisions intended to provide access to benefits for retirees.

Member groups

In order to determine the necessary accounting treatment, it is important to identify the different member groups and their respective benefit entitlements. Three groups of members with different benefit entitlements under the ELHTs are:

- "Active": approximately 211,000 members
- "Pre-August 2013 Retirees"[2]: approximately 5,700 members
- "Post-August 2013 Retirees"[3]: approximately: 1,400+ members

For current Active employees, the contributions by the boards to the ELHTs are fixed and negotiated during bargaining. Annual contribution amounts required from the boards per full-time employee are pre-determined for the period covered by collective bargaining agreements. Upon retirement, active members may be eligible for retiree benefits at full cost and they are not eligible for any cost subsidization (i.e. provisions for Post-August 2013 Retirees).

Certain members who retired prior to August 31, 2013 are eligible for a partial or full subsidization of benefit costs from the board, based on prior arrangements with their employer. The members are eligible to participate in the ELHTs until age 65 (with the exception of a small group who are eligible for lifetime coverage).

All members retiring after 31 August 2013 are eligible to participate in the ELHT through a Voluntary Plan and Separate Account. However, they are responsible for the entire cost of benefits. They are not eligible for any cost subsidization.

[1] OECTA, ETFO, AEFO, OSSTF Trust Agreements have been formally signed; CUPE and PVP/Non-union are to be finalized.
[2] Members retiring prior to 31 August 2013
[3] Members retiring after 31 August 2013

According to the ELHT Trust Agreements Article 6, "*the Trustees may establish any number of Separate Accounts within the Fund. The assets in each Separate Account shall be held as segregated funds and used for the provision of Benefits, in accordance with the terms of a Plan, to a discrete and identifiable group of Participating Employees*". Based on the benefit entitlements described above, presumably, a Separate Account is established for the Active members and a Separate Account is established for the Pre-August 2013 Retirees. Therefore, there is no cross-subsidy. For example, retiree costs are not cross-subsidized by premiums paid in respect of Active employees.

The Trust agreement state that any surpluses in a Separate Account may be used to increase Claims Fluctuations Reserve ("CFR"), enhance benefits, or reduce employee contributions. Conversely, any deficiencies in the trust may require the use of the CFR, amendment to benefit (reduction), or an increase to employee contribution levels.

For the Pre-August 2013 Retirees group, it is our understanding that if there is a funding deficiencies in the Separate Account for this group, the school board will be required to contribute and reimburse the Trust to make up the funding shortfall ("chargeback").

Accounting treatment

Paragraphs 011 – 012 of PSAB 3250 (see Appendix) discuss the classification of benefit plans as Defined Benefit ("DB") or Defined Contribution ("DC"). Further, in accordance with 3250.014, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan.

Considering the different provisions applicable to member groups and PSAB 3250.011 – 3250.012, the benefits provided through the ELHTs include DB provisions in respect of retiree groups, whereas Active member benefits do not fall in the scope of PSA 3250/3255. Specifically:

- *Active:* Benefits/costs relating to current active members does not fall under the scope of PS 3250 (Retirement Benefits) or PS 3255 Retirement Benefits (Post-employment benefits, compensated absences and termination benefits). The scope of these sections cover benefits payable in retirement, after employment but before retirement, or compensated absences or termination benefits. Costs relating to providing benefits to active members during employment would be expensed annually in amounts equal to the fixed contribution. Further, as current active members are not eligible for subsidized benefits upon retirement (i.e. they pay for the entire cost of the post-retirement coverage without any cost to the employer), there is also no post-retirement obligation. To the extent that members on long-term disability are also eligible to receive benefits from the ELHT, a defined benefit obligation may need to be recognized under PS3255 in respect of expected future contributions over the anticipated period of long-term disability in respect of disabled employees.

- *"Pre-August 2013 Retirees:* The provisions relating to certain members who retired prior to 31 August 2013 would be classified as DB provisions as the boards are at risk with respect to the amount of benefits these employees will receive. These risks include the possibility of higher/lower than expected claims, or greater/less than expected longevity. We understand that the school boards have historically reported defined benefit obligations in respect of the ongoing commitment to subsidize retiree benefits for members in this group and will continue to do so subsequent to the transition to the ELHTs. This is appropriate as the ELHTs would be reimbursed by the boards for any contribution requirement to make up for the deficit in providing the coverage for these members.

- *"Post-August 2013 Retirees:* By contrast, there is no cost to the school boards relating to members retiring after 31 August 2013. The entire cost is borne by retirees and the school boards are not required to make any additional contributions in the future in the event of any shortfall. School board contributions are not

subject to any actuarial risk. Rather, all risks are borne by the retirees. In the event that funds are insufficient to pay for benefits, the trust agreements outline measures to address those deficiencies. The measures include the application of reserves, increases to member contributions and a reduction in benefits. None of the measures require any additional contributions from the school boards.

Therefore, we understand there to be a defined benefit obligation only in relation to the benefit entitlement for the subsidies provided to certain members retired prior to 31 August 2013. In addition, there may be a defined benefit obligation in respect of members on long-term disability to the extent that the ELHT covers such members.

Comparison with Shared Risk Pension Plans

In recent years, a number of Canadian provinces have adopted "Shared Risk Pension Plan" legislation. Shared Risk Pension Plans (SRPPs) provide benefits under a defined benefit formula, while putting cost constraints on employer contributions. Employer and employee contributions are often restricted within a band and benefits may be subject to reductions depending on the funded level.

In general, Shared Risk Pension Plans have been viewed as defined benefit plans. Risks are shared by the employer and employees, with the employer usually being subject to some level of actuarial and market risks. There may, however, be instances where DC accounting could be possible. This would be the case when no risk is retained by the employer, i.e. contributions are fixed in all scenarios. As there are many variations of Shared Risk Pension Plans, careful judgment is required to determine the appropriate accounting treatment in each case.

At the request of OPCD, we have compared the key characteristics of the ELHTs established by the Ontario school boards to those of Shared Risk Pension Plans. We have not considered the provisions relating to Pre-August 2013 Retirees, as these are clearly DB provisions under PS 3250/3255.

When comparing the benefits for the Active members under the ELHT with the SRPPS, there are a number of important differences to be considered but the following two are most significant:

- As SRPPs provide post-retirement benefits, they are within the scope of PS3250; however, as demonstrated in the previous section, the benefits provided for the Active members under ELHTs do not fall under the scope of PS3250.
- For SRPPs, the employer is subject to some level of actuarial risks and market risk as future contributions may be increased to pay for past deficiencies. Under ELHTs, the school boards are not subject to any risks: (a) contributions are fixed (as required by a Central Collective Agreement or any applicable Participation Agreement); (b) no additional contributions will be required for the related past service regardless of future actuarial or market experience; (c) the contributions required by the school boards are not dependent on the funding position of the Separate Account. Rather, employee's contributions (or benefits paid) may increase or decrease based on the surpluses/deficiencies of the Separate Accounts.

Further, there is no cost (and therefore, no post-retirement benefits) for members retiring after 31 August 2013 under the ELHTs. For these reasons, we would not expect the same accounting treatment to be applied for the SRPPs and ELHTs.

Appendix – Public Sector Accounting Board ("PSAB") 3250 Retirement Benefits (applicable excerpts)

.011 Two types of benefit plans are addressed in this Section — defined benefit plans and defined contribution plans. A defined benefit plan is one that specifies either the benefits to be received by employees after retirement or the method for determining those benefits. Generally, the amount and value of the benefits to be paid depend on a number of factors and events. These include how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation and retirement age. When a government provides benefits under a defined benefit plan, it is at risk with respect to the amount of the benefit that each employee will receive (actuarial risk) and with respect to the investment returns on any assets set aside to pay for the cost of these benefits (investment risk).

.012 When a government provides benefits under a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. A defined contribution plan (or money purchase plan) is one in which a government's contributions in respect of services rendered by employees are specified. The government is required by the plan to make a specific fixed contribution each period. If that contribution is made, no additional government contributions are required now or in the future for the related service. The employees are at risk. This is generally because the amount of the benefit that will be payable to an employee is dependent upon the funds accumulated for each employee's account and the investment earnings on the accumulated funds.

.013 Because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of a particular plan makes it a defined benefit or a defined contribution plan.

. 014 In some circumstances, a benefit plan may include both defined benefit and defined contribution promises. The plan, for example, may guarantee a basic defined retirement benefit and state that additional benefits, such as inflation protection, will be provided on a defined contribution basis. In such circumstances, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan. Once the type(s) of promise is identified, the accounting and reporting principles in this Section would be followed accordingly.

Appendix – Public Sector Accounting Board ("PSAB") 3255 Post-Employment Benefits (applicable excerpts)

Purpose and scope

.01 This Section establishes standards on how to account for and report obligations for post-employment benefits, compensated absences and termination benefits in government financial statements.

.02 This Section applies to post-employment benefits, compensated absences and termination benefits earned by employees and expected to be provided to them when they are no longer providing active service either on a temporary or permanent basis. For the purposes of this Section:

- *(a) Post-employment benefits are expected to be provided after employment but before retirement to employees and their beneficiaries. These benefits include long- and short-term disability income benefits (including workers' compensation), severance benefits, salary continuation, supplemental unemployment benefits, job training and counselling, and continuation of benefits such as health care benefits and life insurance.*
- *(b) Compensated absences are benefits for employee absences for which employees will be paid. These benefits include parental leaves, accumulated sick days, and sabbaticals that provide compensated, unrestricted time off for past service.*
- *(c) Termination benefits include the following:*
  - *a. Contractual termination benefits are benefits required to be provided to employees under the existing terms of a benefit arrangement when a specific event occurs that results in the downsizing and termination of a group of employees.*
  - *b. Special termination benefits are benefits that are not contractual termination benefits and that are offered to employees for a short period of time, normally not exceeding twelve months, in exchange for employees' voluntary or involuntary termination of employment.*

.03 The glossary in RETIREMENT BENEFITS, Section PS 3250, provides definitions for other relevant terms.

.04 This Section does not apply to short-term employee benefits, which would be accounted for under the general provisions for accruing liabilities. This accounting is generally straightforward because no actuarial assumptions are required and the liabilities are measured on an undiscounted basis.

.05 Examples of such short-term employee benefits are:

- *(a) Salaries, wages, bonuses, fringe benefits and similar items a government provides in the current reporting period or within twelve months thereafter, in exchange for services rendered by employees in the current reporting period; and*
- *(b) Occasional sick days and vacation days that do not vest or accumulate beyond twelve months after the current reporting period.*

Post-employment benefits, compensated absences and termination benefits are liabilities of a government. Accounting for all benefit plans is important because many governments have accumulated significant related liabilities. The fundamental accounting task is to determine the amount of the liability for these benefits and to what periods to attribute the costs.

.07 These standards are consistent with those established in RETIREMENT BENEFITS, Section PS 3250. The standards set out in that Section are appropriate for accounting for and disclosing post-employment benefits, compensated absences and termination benefits of a government. For example, a government providing these types of benefits through a defined contribution plan, multiemployer plan or joint defined benefit plan would refer to the guidance set out in Section PS 3250. This Section sets out those areas where the accounting and reporting are different from Section PS 3250.

Ernst & Young.rtf

From: Virani, Shyrose (TBS) []
To: Askcontractorscreening (TBS) [Askcontractorscreening@ontario.ca]
Subject: Ernst & Young
Date: Wednesday, November 29, 2017 14:49:55

Hi

We have a clearance for:

1. Uros Karadzic – C-0000129813 - exp 07 Feb 22
2. Christina Chan – C-0000130031 – exp 15 Feb 22

Can you please let me know if it is still valid?

Thanks

Shyrose Virani

Ernst & Young.rtf

From: Virani, Shyrose (TBS) []
To: Askcontractorscreening (TBS) [Askcontractorscreening@ontario.ca]
Subject: Ernst & Young
Date: Wednesday, December 06, 2017 14:27:06

Hi

We have a clearance for:

Gregory Winston - C-0000142599 – exp 10-Sep-22

Can you please let me know if it is still valid?

Thanks

Shyrose Virani

Ernst and Young.rtf

From: Virani, Shyrose (TBS) []
To: Askcontractorscreening (TBS) [Askcontractorscreening@ontario.ca]
Subject: Ernst and Young
Date: Monday, February 13, 2017 10:37:23

Can you please let me know if you have a clearance for

Christina Chan from Ernst and Young.

Thanks

Shyrose

Ernst and Young.rtf

From: Virani, Shyrose (TBS) []
To: Askcontractorscreening (TBS) [Askcontractorscreening@ontario.ca]
Subject: Ernst and Young
Date: Monday, February 13, 2017 10:37:23

Can you please let me know if you have a clearance for

Christina Chan from Ernst and Young.

Thanks

Shyrose

Expert Panel - end of work.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]; Christina Chan [Christina.Chan@ca.ey.com]
Subject: Expert Panel - end of work
Date: Monday, March 27, 2017 09:14:11
Attachment 1: image001.gif

Hi Nadine,

I've just submitted my timesheet to Nelson for the Expert Panel work. I believe we are now done, although my understanding is that the official mandate only ends on 31st.

I'm in all-day PSAB Taskforce meetings until Thursday, but following that please let me know if you're now comfortable with me joining Shayan and Christina.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

Expert Panel - writer PO# 228100.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Expert Panel - writer PO# 228100
Date: Tuesday, March 14, 2017 11:01:59

Hi Lucy

One more question on the above

Contract ceiling = $65,000
Billed to date = $19,200 (excluding HST) Estimate to year end (March 31/2017) Will funds be required for 2017/18?

Thanks
Shyrose

Expert Panel -- Next Steps.rtf

From: Veinot, Cindy (TBS) []
To: Murray Gold [mgold@kmlaw.ca]
CC: Tam, Nelson (TBS) [Nelson.Tam@ontario.ca]
Subject: Expert Panel -- Next Steps
Date: Monday, October 24, 2016 07:59:46
Attachment 1: image001.png

Hi Murray,

As we move towards finalization of panel members, there are some information requirements we will need from you re: conflict of interest and security screening.

Nelson Tam, the Project Manager for the Panel, will be in touch re: the forms and completion instructions. Please complete these as soon as possible.

Also, I wanted to let you know that we are in the process of finalizing the per diem amounts. These amounts are public information (filed as an Order-in-Council). If you have any concerns with that, please let me know.

Thanks,

Cindy

Cindy Veinot

Provincial Controller and Assistant Deputy Minister, Office of the Provincial Controller

Treasury Board Secretariat

Frost Building South

7 Queen's Park Crescent East

Toronto, Ontario M7A 1Y7

T: 416-325-8017

E: cindy.veinot@ontario.ca

image001.pdf

TBS

Expert Panel -- Pension Issue.rtf

From: Veinot, Cindy (TBS) []
To: mgold@kmlaw.ca [mgold@kmlaw.ca]
Subject: Expert Panel -- Pension Issue
Date: Monday, October 17, 2016 15:20:47
Attachment 1: image001.png
Attachment 2: Independent Pension Asset Expert Panel _Final_Oct 5 2016.docx

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Hi Mr. Gold,

Scott Thompson passed along the message that you would be interested in assisting with the expert panel the Province is setting up to review the accounting for pension assets. We are now in the process of identifying candidates for the panel.

We have drafted the terms of reference for the panel, which I've attached.

Would you please review these, let me know whether you have any questions and confirm back that you continue to be interested. We can then set up a time for a conversation (assuming you are still interested!)

Regards,

Cindy Veinot

Cindy Veinot

Provincial Controller and Assistant Deputy Minister, Office of the Provincial Controller

Treasury Board Secretariat

Frost Building South

7 Queen’s Park Crescent East

Toronto, Ontario M7A 1Y7

T: 416-325-8017

E: cindy.veinot@ontario.ca

image001.pdf

TBS

Independent Pension Asset Expert Panel _Final_Oct 5 2016.pdf

Independent Pension Asset Expert Panel

Terms of Reference

Background

In connection with the preparation and audit of the 2015-16 Public Accounts, the Auditor General and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors – Ontario Teachers' Pension Plan and Ontario Public Service Employees' Union Pension Plan. The government passed a time-limited regulation to require the accounting for these pension assets align with the interpretation of the Auditor General. This time-limited regulation enabled the professional accounting staff to take responsibility for the preparation of the Public Accounts in accordance with legislation and PSAS.

The government released an annual report and unaudited financial statements on October 3, 2016, and concurrently announced that an expert panel would be formed to review the application of PSAS to these pension assets.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to write off the pension assets.

Governance

An Expert Panel is established as a short-term advisory body appointed by the President of the Treasury Board to review the application of the PSAS to accounting for pension assets and provide advice to government. The final report will be submitted to the President of the Treasury Board and provided to the Auditor General of Ontario, and made public thereafter. The future accounting for the pension assets in the preparation of the Province's financial statements will be guided by the report of the panel.[1]

Mandate

The Expert Panel's mandate is to deliver advice and recommendations to the government on the application of PSAS to the recognition and measurement of pension assets. The Expert Panel's advice and recommendations to the government will consider:

- The requirement regarding control with respect to recognizing a pension asset for a joint defined benefit plan.

[1] The Public Sector Accounting Board established a task force to review the standards on pension plans. Should their review results in changes to the standards, these new standards would be applied by the Province.

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

Timelines

A report to the President of the Treasury Board and the Auditor General of Ontario is due by the end of 2016.

Membership

The membership of the Panel will comprise experts in the areas of jointly sponsored pension plans, actuarial modelling for pension plans and Public Sector Accounting Standards. All members will be appointed by the President of the Treasury Board.

The identified members should attend/participate in the meetings; no substitutes or alternates should attend in place of a member.

Support

The Province will identify individuals to support the Panel and work collaboratively to provide information related to the pension plans sponsored by the Province of Ontario.

Funding

The Province will be responsible for the costs of the appointed members to attend the meetings. The costs of any individuals supporting the work of the Panel will also be borne by the Province.

Expert Panel.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Expert Panel
Date: Friday, December 02, 2016 13:42:39

Hi Lucy.

I have been advised that the necessary approvals and paperwork will be in place for you to start an engagement for the Expert Advisory Panel on Monday, December 5th. Please plan to arrive on Monday around 8:30 am and call Shyrose upon arrival (51448).

Thanks and have a great weekend.

Nadine

Final Report.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
CC: Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]
Subject: Final Report
Date: Sunday, October 02, 2016 11:17:55
Attachment 1: Treasury Board Secretariat 7600 Report FINAL.pdf

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Hi Nadine and Cindy,

Please find attached our final report.

Kind regards,

Matt

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Treasury Board Secretariat 7600 Report FINAL.pdf

Deloitte LLP
Bay Adelaide East
22 Adelaide Street West
Suite 200
Toronto ON M5H 0A9
Canada

Tel: 416-601-6150
Fax: 416-601-6151
www.deloitte.ca

October 2, 2016

Private and confidential

Ms. Karen Hughes
Associate Deputy Minister,
Treasury Board Secretariat,
7 Queen's Park Crescent
Toronto ON M7A 1Y7

Dear Ms. Hughes:

We have been engaged to report on the appropriate application of certain aspects of Canadian public sector accounting standards to the recognition of the accrued benefit asset (also referred to in this report as the Pension Asset or the Asset) related to the Ontario Teachers' Pension Plan (OTPP the Plan) in the Province of Ontario's (also referred to as the Province or the Government of Ontario in this report) accounts as at March 31, 2016. This report is being issued to the Associate Deputy Minister of the Treasury Board Secretariat of the Government of Ontario. Our engagement has been conducted in accordance with Canadian generally accepted standards for such engagements**.**

It should be noted that the responsibility for the proper accounting treatment rests with the preparers of the financial statements, who should consult with their incumbent auditor. Our judgment on the appropriate application of Canadian public sector accounting standards for the specific issue being discussed is based on the facts, circumstances and assumptions provided to us. Should the facts, circumstances or assumptions differ, our conclusion may change.

Statement of facts and assumptions
It should be noted that the following background and facts represent a high level summary of the situation and represent those facts that we considered important in reaching our opinion. They do not purport to be a complete representation of all of the terms of the OTPP or the agreements between the government and the Ontario Teachers' Federation (OTF). Management has acknowledged their agreement with this summary. If these facts are incomplete or incorrect, then our conclusions may change.

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

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

Statement of facts and assumptions (continued)
Through a six-member Partners' Committee, the sponsors jointly:

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

(Source: https://www.otpp.com/corporate/plan-governance)

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

- Teachers' Pension Act (TPA), including Schedule 1
- Partners' Agreement
- Funding Management Policy (FMP)
- Osler's letter dated September 20, 2016; we have not summarized this letter as it should be read in its entirety.

The assets of the pension plan are held by Ontario Teachers' in trust for the beneficiaries of the plan – teachers. The Government does not have unilateral access to the assets of the trust (including changing contribution amounts, taking contribution holidays, or withdrawals). Actions of this nature require negotiation and agreement between the two sponsors.

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

- As a jointly sponsored plan, the Plan meets the definition of a joint benefit plan under S. 3250 of the Public Sector Handbook.
- The actuarial and other assumptions that factored into the valuation used for accounting purposes, before considering the appropriateness of the recognition of an asset or the need for a valuation allowance related to any asset, are appropriate and meet the requirements of PS 3250.
- The Plan's most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website. The OTPP's public financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015. These financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook, which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the funding surplus or deficit.
- As at March 31, 2016, there were no written agreements in place to access the Plan surplus to reduce future minimum contributions or withdraw any amounts from the Plan.
- The OTPP is regulated by the Financial Services Commission of Ontario. Valuation reports must be filed with this regulator to monitor that assets of the fund are reasonably sufficient to meet the liabilities of the pension plan on a continuing basis. Per 78(1) of the Pension Benefits Act: No money that is surplus may be paid out of a pension fund to the employer without the prior consent of the Superintendent.

Statement of facts and assumptions (continued)

- Management has received legal commentary about the role of the Superintendent. From this advice, management has concluded that despite this regulation the Province could utilize a surplus through contribution reductions as "Neither the PBA nor the regulations to the PBA (the "Regulations") require the Superintendent's consent for surplus to be *utilized* for a contribution holiday or to amend the contribution formula under the OTPP." Further, although changes to the OTPP text would be required to be registered with the Superintendent, "The authority of the Superintendent to refuse to register an amendment under the PBA (in whole or in part) is limited to circumstances where the amendment is void or if the pension plan with the amendment would cease to comply with the PBA and the Regulations." (Source: Osler memo dated September 26, 2016).
- The Auditor General's Office provided a letter dated September 26, 2016 setting out their views. We have read and considered the contents of that letter.

Relevant Extracts from the TPA

Section 5 (1.1) of the TPA states that the total amount of contributions payable by the Minister of Education and the employers who contribute under the pension plan in respect of any year shall not exceed the amount of contributions payable by or on behalf of active plan members in respect of credited service for that year. There can be instances where contributions would not be equal between the sponsors, such as the government's payments in connection with forgone inflation adjustments.

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

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

Relevant extracts from the Partners' Agreement

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

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

[1] Partners' Agreement, section 110.

Relevant extracts from the Partners' Agreement (continued)

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

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

Relevant extracts from the FMP

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

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

i) Restoration zone (Article 3 of the FMP) allows for a surplus to be utilized to "restore" foregone indexation and then to either increase benefits to the "run-rate benefit" level (i.e., the long-term target level) or to lower contributions (or a combination of these two options) (Section 3.06(e)).
ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).
iii) Permanent improvement zone is where the Plan is essentially fully funded and has the funding security desired to support permanent changes. Article V (Permanent Improvements) of the FMP provides for permanent actions that can be taken when Plan assets exceed current liabilities by more than 10% of current liabilities. In this regard Section 5.05 provides for actions that can be taken in respect of the amount that assets exceed current liabilities. Such actions can include changes to current benefits, current contributions, or both.

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Partners are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

Relevant extracts from the FMP (continued)
It is our understanding that the Plan is currently in the Restoration Zone. We understand that contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both partners, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Application of accounting principles
Specifically, our report addresses the following questions:

1. Is it necessary for a government to have a legally enforceable right to reduce future contributions in order to recognize a Pension Asset under PS 3250?

2. What is the role of legal uncertainty in assessing the government's expectation of future benefit from a Pension Asset?

Our views in this report are confined to these two questions and do not extend to any earlier reports provided by Deloitte or to any other analysis that may have been presented in draft or in any other manner.

Authoritative literature
In our analysis, we considered the pronouncements and guidance in Section 3250 of the CPA Public Sector Accounting Standards Handbook. What we considered to be the most relevant passages from PS 3250 are reproduced below:

> **The objectives of funding and accounting**
>
> .008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.
>
> .009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. Accordingly, it is necessary to develop accounting estimates of liabilities for retirement benefits and expenses using an actuarial cost method and actuarial assumptions that ensure essential information required for fair presentation of financial condition and results of operations can be reported in government financial statements.

Authoritative literature (continued)

.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.

Actuarial assumptions

.042 Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts. [SEPT. 2001]

Joint defined benefit plans

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

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

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans*. [SEPT. 2001]

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

Disclosure

.083 The notes and schedules integral to the financial statements would disclose the methods and judgments applied in accounting for accrued benefit obligations and expenses. Full disclosure is particularly important for retirement obligations because the measurements depend heavily upon judgments rather than objective evidence.

Limit on the carrying amount of an accrued benefit asset

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

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

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

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

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

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

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

Limit on the carrying amount of an accrued benefit asset (continued)

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

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

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

We also considered the following definitions as set out in the glossary of PS 3250:

- An **accrued benefit asset** is the amount of any asset recognized on a government's statement of financial position in respect of employee retirement benefits before deducting any valuation allowance that may be required. It is the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance).
- The **expected future benefit** is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions. A government determines its expected future benefit as the sum of:
  (a) the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus; and
  (b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations.

Limit on the carrying amount of an accrued benefit asset (continued)

- A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:
  (a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;
  (b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;
  (c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and
  (d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.

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

CONSIDERATION OF QUESTION 1

Application of PS 3250 to Joint Defined Benefit Plans

A joint defined benefit plan is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. We would note that paragraph .081 of PS 3250 clearly states that a government should account for its portion of the plan in accordance with the standards for defined benefit plans. As a result, the Province of Ontario accounts for its proportionate share of OTPP and has historically recorded its share as 50% of the plan.

The Province of Ontario's Public Accounts have included a Pension Asset related to OTPP since fiscal 2001/2002. We have been informed that this situation has arisen because, to this point in time, the government's share of the total contributions to the Plan plus the actual investment returns on the Plan's assets have exceeded the government's share of the accumulated retirement benefit expense. The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by S 3250. S 3250.51 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: "Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons."

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (3250.42) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (3250.41). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. 3250.57 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province of Ontario has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on Plan Assets, which is one of the acceptable references suggested on PS 3250.44. We express no view on the actual rates that were chosen.

Application of the limit on the carrying amount of an accrued benefit asset

PS 3250.50 requires that an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. This comparison between the adjusted benefit asset and the expected future benefit informs whether a valuation allowance is required and if so, how much of a valuation allowance should be recorded. (It should be noted that "accrued benefit asset" and "adjusted benefit asset" are defined terms used in S. 3250. As at March 31, 2016, in this particular case, management has represented to us that these two amounts are the same.)

PS 3250.52 contemplates that there are two ways in which a government can benefit from an accrued benefit asset. A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. As such, an expected future benefit would include the ability to either withdraw plan assets from the plan or reduce future contributions.

PS3250.52 also goes on to consider that an accrued benefit asset may become impaired when there is a plan surplus that the government is not entitled to benefit from fully. The paragraphs in the standard that follow determine how a government would go about considering the extent of any impairment, which would give rise to a valuation allowance. In order to make this determination, the government is required to consider the "expected future benefit", which would effectively create a ceiling for the asset. Here the guidance diverges between benefit expected to be realized through future reductions in contributions and those to be realized through withdrawal of surplus.

Specifically with respect to withdrawal of surplus, PS 3250.59 is very clear that expected future benefit can only be asserted where the government has a current legally enforceable right to withdraw assets from the Plan. We considered whether this guidance should be applied to cases where the expected future benefit related to the Pension Asset is expected to be realized through reduced contributions and concluded that the guidance does not apply in this situation; while PS 3250.59 does introduce the concept of a legally enforceable right, it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions. We believe it reasonable to conclude that if the standard setters had intended legal enforceability to be the test, they would have included that notion throughout the guidance, instead of only raising it in the context of a withdrawal of surplus. In the situation at hand, the Province is not asserting an expected future benefit based on surplus withdrawal. Instead the Province's position is that the future benefit is expected to be realized through future contribution reductions. Therefore, we do not believe that 3250.59 applies in this case.

Additionally, in forming our view on the application of PS 3250 to Joint Defined Benefit Plans, we noted that there is specific guidance (PS 3250.81) that requires the Government to account for a portion of the Plan in accordance with the standards for defined benefit plans.

For the reasons stated above, we are of the view for Question 1, that legal enforceability of a government's right to access a pension plan surplus through future contribution reductions is not necessary to justify recognition of a Pension Asset. We believe that the guidance in PS 3250 is the primary source of GAAP on this topic and, since it is clear, there is no need to look at any other potential sources of GAAP.

CONSIDERATION OF QUESTION 2

Since we have concluded that legal enforceability is not a necessary requirement to support a government's right to access a pension plan surplus through future contribution reductions, we further considered what role legal considerations should play in the measurement of the Pension Asset. We note that PS 3250.52 requires one to consider "uncertainties as to a government's legal right to use a plan's accounting surplus." Our interpretation of this guidance is that it presents a lower threshold than legal enforceability. Specifically, the amount of Pension Asset that gets recorded needs to be subject to considerations around any legal uncertainties. This consideration will involve significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a Pension Asset.

PS 3250.53 to .58 lay out a mathematical calculation that determines the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in PS3250.055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where realization includes a reduction in future contributions. A valuation allowance is recorded against the Pension Asset to limit the asset value, if necessary, based on this analysis.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. This calculation is further described in PS 3250.56(a), which sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per PS 3250.81 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the Pension Asset value to be recorded in the accounts. For example, if the Pension Asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the Pension Asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for judgment in the above calculation is in the determination of future minimum contributions required to be made by the government regardless of any surplus. There is no further guidance in S 3250 as to how this calculation should be performed and what restrictions or parameters should be factored into this calculation.

Determining the number of years of contributions to include should involve consideration of legal uncertainty as set out in PS 3250.52. With respect to this uncertainty, we would observe that there are a number of considerations that may be relevant. As part of this analysis, we reviewed Osler's legal letter of September 20, 2016. That letter makes a number of observations about the Plan agreements and governing documents that we will not reiterate here. Osler's do note that legal enforceability does not exist. However, as noted above we do not believe that legal enforceability is required in this case.

Future reductions in contributions will need to be negotiated and agreed between both sponsors, who are required under the Plan governing documents to bargain in good faith. There are a number of factors to consider and it is possible for reasonable professionals to arrive at different conclusions, even when confronted with the same set of facts and circumstances. These considerations will be highly judgmental.

With respect to these judgments, we offer the following observations. We express no opinion on the completeness of this list of observations or the relative importance of each of these points.

- Plan documents and design contemplates the shared nature of the Plan.
- Section 10 of the Partners agreement require that the partners meet every 3 years to discuss changes to the Plan.
- As described to us by management, there was a long history of sharing surpluses through various mechanisms during the 1990's when funding surpluses were more common. The FMP also contemplates a sharing of surpluses.
- As described to us by management, in addition to the history of surplus utilization noted in the facts and assumptions, it is worth noting that the actions taken around inflation indexation and subsequent restoration of those benefits are a recent example of the sharing philosophy governing operation of the OTPP. Starting in 2011 in response to a deficit situation, it was determined that indexation would be reduced for teachers retiring after 2009. Consistent with the 50/50 approach inherent in the Plan operation, the government agreed to make payments (often referred to as "share the pain" payments) into the Plan that would effectively match the value of benefits foregone by teachers. In 2014, 2015 and 2016, surpluses were used to restore some of the lost indexation. This decision results in a decrease in the Province's "share the pain" payments.
- The FMP explicitly considers the possibility of contribution reductions at different funding levels, although both sponsors need to agree. The OTPP's investment performance has consistently outperformed expectations. If this situation continues the funding surplus can be expected to continue to grow. Modelling could be performed to help estimate when the different funding zones will be reached and probability of contribution reductions may be increased.
- We also note that Canada Revenue Agency establishes limits for pension surpluses. When these limits are breached, steps need to be taken to reduce the surplus. In such a situation, contribution reductions would be one way to reduce the surplus that would need to be negotiated by the parties within their overall framework for negotiation. Again, modelling could be done to develop expectations as to when these CRA limits could be expected to be reached.
- Contributions are generally borne equally by the Province and the teachers. It may be reasonable to presume that teachers will also want to see contribution reductions at some point. Admittedly, increases in benefits could also use any surplus; however, it may be reasonable to expect that the interests of taxpayers and teachers will need to be weighed in the "good faith" bargaining process such that unequal weighting towards increases in benefits may be unlikely.

- In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (PS 2130.03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in PS 2130.13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

However, application and weighting of these and other considerations is a highly judgmental exercise and it is possible that there is a range of reasonable conclusions that may result in a range of reasonable estimates for the valuation allowance to be taken against the Pension Asset. We are unable to opine on whether a valuation allowance is needed, and if so, what a reasonable range of estimates would be.

Given the complexities and degree of judgment involved in these matters, appropriate disclosure is a matter of significance as is recognized in 3250.83 which states, in part, *"Full disclosure is particularly important for retirement obligations because the measurements depend heavily upon judgments rather than objective evidence"*. This importance is also highlighted in the context of joint benefit plans in 3250.93 which requires that the unique nature and terms of any joint plans be disclosed.

We would also note that Deloitte prepared a report dated August 18, 2016 entitled "Asset Ceiling Calculations for the Ontario Teacher's Pension Plan" in conjunction with management that was used by management as part of their analysis to determine that no valuation allowance was required against their Pension Asset as at March 31, 2016. That report was prepared solely to assist management in preparing their own analysis. We were not engaged to and did not express an opinion on the amount of or need for any valuation allowance, nor do we express an opinion on this analysis at this point. Reference to the August 18, 2016 report in this report should in no way be construed to be an opinion on that earlier report.

The ultimate responsibility for the decision on the appropriate application of Canadian Public Sector Accounting Standards for the specific transaction described above rests with management as preparers of the financial statements, who should consult with the Auditor General of Ontario. Our judgment on the appropriate application of Canadian Public Sector Accounting Standards for the specific situation described above is based on the facts, circumstances and assumptions provided to us. Should the facts, circumstances or assumptions differ, our conclusion may change.

This report is intended solely for the information and use of Ms. Karen Hughes and management of the Government of Ontario and is not intended to be and should not be used by anyone other than the above party and the Auditor General of Ontario or for any other purpose. For further clarity, this report should not be distributed to anyone outside those named in the previous sentence, nor should it be quoted from outside this group for any purpose. Please contact Kerry Danyluk, National Director of Accounting Services, regarding any questions about the content of this report (416 775-7183 or kdanyluk@deloitte.ca).

Yours truly,

Deloitte LLP.

Chartered Professional Accountants
Licensed Public Accountants

confidential form and tax form.rtf

From: []
To: maraymond@deloitte.ca [maraymond@deloitte.ca]
Subject: confidential form and tax form
Date:
Attachment 1: confidentiality agreement.doc
Attachment 2: tax declaration form.docx

Hi Raymond

Can you please fill out these two forms and send back to me asap. Please backdate it to the date that you actually started to work.

Thanks
Shyrose

confidentiality agreement.pdf

CONFIDENTIALITY AGREEMENT

Confidentiality Agreement

During and following the term of the Agreement between **Deloitte Inc.** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and Listed Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the *Freedom of Information and Protection of Privacy Act* ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: _____ Signature: _____

Date: _____

Witness: _____ Signature: _____

Date: _____

tax declaration form.pdf

Appendix D – Tax Compliance Declaration Form

The Ontario Government expects all suppliers to meet their Ontario tax obligations on a timely basis. In this regard, proponents are advised that their Ontario tax obligations, if any, must be in good standing in order to be considered for a contract award (see Section 3.2.3 of the RFP). In order to be considered for a contract award, the proponent must submit the following tax compliance status statement and the following consent to disclosure:

Declaration

I/WE hereby certify that **Deloitte Inc**. (the "Proponent") at the time of submitting its proposal, is in full compliance with all applicable Ontario tax statutes, whether administered by the Treasury Board Secretariat or by the Canada Revenue Agency, and that, in particular, all returns required to be filed have been filed and all taxes due and payable under those statutes have been paid or satisfactory arrangements for their payment have been made and maintained; or the Proponent will take all necessary steps prior to being considered for contract award in order to be in full compliance with all applicable Ontario tax statutes.

(Please check applicable box)

The Proponent ❑ is / ❑ is not a corporation subject to Ontario corporate tax under the *Taxation Act, 2007* (Ontario).

(Please insert Proponent's Business Number) _____

Consent to Disclosure

The Proponent consents to the Ministry of Finance releasing the taxpayer information to the Ministry of Finance as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

The Proponent consents to the Ministry of Finance releasing taxpayer information to the Requesting Ministry as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

Dated at _____ this _____ day of _____ 20 _____

_____

(Authorized signing officer)

_____

(Print Name) **(Title)**

I have authority to bind the Proponent.

data request re_ OTPP_OPSEUPP asset ceiling.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]
CC: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: data request re: OTPP/OPSEUPP asset ceiling
Date: Wednesday, March 15, 2017 12:15:11
Attachment 1: image003.jpg

Hi Shyrose, Bharat,

We will require the following documents for each of the Plans to proceed:

1) Actuarial funding valuation reports for each plan – Bharat, would you provide? Would you mind also provide us with a printed copy for each as we do not have access to the printer?

2) Funding policy statement - I believe Shyrose has a reference binder with background materials on these plans that contain this information.

Thank you very much!

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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From: Virani, Shyrose (TBS) []
To: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; cawarburton@deloitte.ca [cawarburton@deloitte.ca]
CC: Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Donaldson, Mark (TBS) [Mark.Donaldson@ontario.ca]; 'Raymond, Martin (CA - Montreal)' [maraymond@deloitte.ca]; 'Colley, Matthew (CA - Toronto)' [mcolley@deloitte.ca]
Subject: debriefing - Deloitte
Date: Monday, December 18, 2017 16:18:44

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

Thank you very much for notifying us of this contract decision. Please can we book a debrief meeting to receive feedback on our response.

Thanks

Cara

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Cara Warburton

Senior Manager | Public Sector

22 Adelaide Street West, Suite 200, Toronto, ON, M5H 0A9, Canada

D: (416) 601 5763 | M: (647) 300 9400

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From: Virani, Shyrose (TBS) []
To: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; cawarburton@deloitte.ca [cawarburton@deloitte.ca]
CC: Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Donaldson, Mark (TBS) [Mark.Donaldson@ontario.ca]; Raymond, Martin (CA - Montreal) [maraymond@deloitte.ca]; Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
Subject: debriefing - Deloitte
Date: Monday, December 18, 2017 15:37:06

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

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From: Virani, Shyrose (TBS) []
To: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; cawarburton@deloitte.ca [cawarburton@deloitte.ca]
CC: Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Donaldson, Mark (TBS) [Mark.Donaldson@ontario.ca]
Subject: debriefing - Deloitte
Date: Friday, December 15, 2017 09:55:38

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

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From: Virani, Shyrose (TBS) []
To: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; cawarburton@deloitte.ca [cawarburton@deloitte.ca]
Subject: debriefing - Deloitte
Date: Wednesday, December 06, 2017 12:40:43

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

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From:	Virani, Shyrose (TBS)
To:	Sun, Alicia (TBS); cawarburton@deloitte.ca
Cc:	Patel, Bharat (TBS); Donaldson, Mark (TBS); "Raymond, Martin (CA - Montreal)"; "Colley, Matthew (CA - Toronto)"
Subject:	debriefing - Deloitte
Start:	January 8, 2018 2:00:00 PM
End:	January 8, 2018 2:30:00 PM
Location:	TBS-R-7 Queen"s Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom, teleconference 416 212 8014 passcode 1474532#

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

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From: Raymond, Martin (CA - Montreal) [maraymond@deloitte.ca]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Gary, Trevor (CA - Toronto) [tgary@deloitte.ca]
Subject: documents to print
Date: Thursday, September 01, 2016 09:34:24
Attachment 1: Picture (Device Independent Bitmap) 1.jpg
Attachment 2: response OAG questions_Aug31_2016.docx
Attachment 3: calculation_EFB_estimate_Sept1_2016_Base Case.pdf
Attachment 4: calculation_EFB_estimate_Sept1_2016_Extr Case.pdf

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Shyrose and Nadine

As discussed with Trevor, Shyrose if you can print the documents it would be appreciated (just finalized it)
Nadine – note that the 3rd document (extr case) is to show until what time the contribution requirement would be needed to get to EFB equal to adjusted benefit asset. This is 2048 and 2050 respectively. This is just to show how far this needs to get compared to the current practice we see for the most restrictive test. I will let you judge if you wish to provide or just keep as a back up.

See you shortly

Thanks

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services
Deloitte
1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada
Tel / Direct : 514-393-7367
Fax : 514-390-4104
maraymond@deloitte.ca | www.deloitte.ca

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response OAG questions_Aug31_2016.pdf

OTPP and OPSEU PP asset ceiling discussion

Separate analysis documents have been prepared to support the OTPP and OPSEU PP asset situation presented on the Province Financial statements. Following the review of the documents, the Ontario AG has submitted 2 questions. The purpose of this document is to provide answers to the questions.

Before moving into the supporting explanation, it is important to highlight the main conclusions of the Province analysis presented in the initial reports and the rationale behind it.

For the OTPP, the main conclusion, based on the facts and circumstances is that the Government is entitled to have access to the surplus related to the share of the plan that it is responsible for. Here are some elements of facts and circumstances that support the Government analysis:

- The plan is a joint sponsored pension plan under the pension legislation
- The contribution requirement of the plan is based on matching employer contributions, hence a 50 / 50 sharing
- There is an agreement that has been reached between employees and Government that defines how surpluses and deficits are to be treated. The document is called the Funding Management Policy (FMP)
- The FMP identifies that the Government can benefit from a surplus position through contribution reduction but also with possible surplus withdrawal. Sections 4.05, 4.06 and 5.05 of the FMP are particularly referring to this
- The idea of the plan is that when good or bad news occur and the employees benefit or are negatively affected by this, the Government also gets a similar impact. In particular, in surplus position, the employees could benefit from improvement to the plan provisions while the Government could benefit from reduction in contribution
- The conclusion of the analysis is therefore that any surplus position to the Government, based on best estimate assumptions as per the accounting standards would represent an economic benefit in the future as per the FMP sharing notion that has been agreed by the parties
- The Partners at OTPP do need to review and confirm on the uses of surplus, but this does not raise the question of the access of the Government that is based on the agreed FMP.

For the OPSEU PP, the main conclusion, based on the facts and circumstances is also that the Government is entitled to have access to the surplus related to the share of the plan that it is responsible for. Here are some elements of facts and circumstances that support the Government analysis:

- The plan is a joint sponsored pension plan under the pension legislation
- The contribution requirement of the plan is based on matching employer contributions, hence a 50 / 50 sharing
- There is an agreement that has been reached between employees and Government that defines how surpluses and deficits are to be treated. The document is called the Funding Policy (FP)
- The FP identifies that the Government can benefit from a surplus position through contribution reduction.
- There is a rate stabilization reserve that is set up for each sponsor, the employees and the Government. This reserve represents the value of unspent past surpluses. The Government does have its own reserve for its share of the plan from which it can

draw to reduce contribution requirements. Gains and losses are affecting the reserve amount. As an illustration, the Government has about $104M of reserve as at December 31, 2014 valuation report (page 4 of the report).

- The FP under 3.3 indicates that the reserve accounts are controlled by the sponsors as per their allocated amounts.
- The idea of the plan is that when good or bad news occur and the employees benefit or are negatively affected by this, the Government also gets a similar impact. In particular, in surplus position, the employees could benefit from improvement to the plan provisions while the Government could benefit from reduction in contribution
- The conclusion of the analysis is therefore that any surplus position to the Government, based on best estimate assumptions as per the accounting standard would represent an economic benefit in the future as per the FP sharing notion that has been agreed by the parties
- Under 5.1 of the FP, it is indicated that the OPTrust recognizes that the decisions on the use of surplus are reserved to the Sponsors (employees and Government). OPTrust has provided principles to help decisions on the use of surplus, but it is still a decision of the employees and the Government on how to use their reserve account
- Under the FP, section 5.1 refers to some options of using surplus. The item 5 of Section 5.1 indicates that it is suggested to consider temporary reduction of contribution as the most predictable way of reducing the surplus. Reduction of contribution is identified as the most predictable way, but likely not the only possible way. Since the idea of the plan is to share 50 / 50 the gains and specifically through reserves identified separately for each sponsor, surplus withdrawals may be expected as one other way of dealing with surplus.

So based on all the facts above, the Province concluded that the accounting surplus measured as the best estimate of the plan situation represents an economic benefit through future contribution reduction or surplus withdrawal. The answers provided to the Ontario AG questions would therefore normally follow be limited to these explanations above. In order to still support the discussion on expected future benefit (especially for the question 2 raised on calculations), we did look at how calculations might be prepared under PS3250 by entities sponsoring plans where the employer would not have such a clear access to surplus, which is not the current situation.

The key elements of the Ontario AG queries are:

1. Could the plan sponsor access a surplus for the purposes of withdrawing some amount of asset in line with PS 3250.059?
2. Provide illustrations of the expected future benefit (EFB) to determine if the adjusted benefit asset should be impaired by a valuation allowance?

The EFB calculation is a sum of 2 parts. One is based on future current service reduction and the other is based on surplus withdrawal. We note that in the calculations for question 2, we have only considered the part of current service reduction and not assumed any value for surplus withdrawal. Although we have indicated that the Government would have some access to it through the policies agreed with the employees, we have excluded the calculation of it since the part of EFB coming from current service cost reduction is sufficient to support the asset position as is illustrated by the calculations.

For the calculation of the EFB of an adjusted benefit asset under PS 3250.050, we have identified 4 levels of calculation to determine the EFB (one additional to the 3 Views of initial report prepared):

- Level 1: A more Liberal/Historical calculation based on a perpetuity of service cost – basically no employer minimum required contribution regardless of any surplus (View 1 in the initial report);
- Level 2: A recent approach seen in some situations used for calculation – employer minimum contribution based on the current funding report period ex 1 to 3 years (View 2 in the initial report);
- Level 3 (a new approach): Another recent approach which we are seeing used – employer minimum contribution based on the current funding report but for the period of contribution requirement (usually more around 10-15 years) and not just the period of the current funding report;
- Level 4: A highly complex approach for calculating EFB which requires stochastic projections of plan situation over significant number of years and large number of generated scenarios (the previous View 3 of the initial report).

The Ontario AG as indicated in question 2 that some calculations along the lines of view 3 (now Level 4) was expected. As indicated in the initial document, we have never seen stochastic approaches used to prepare PS3250 asset ceiling. This would be highly time-consuming and require large number of assumption inputs that are not needed in usual accounting for pension plans. This would require a full stochastic projection which includes identifying the funding policy triggers each year for multiple plan situations. This would require a powerful model and would likely come at a very large cost to the plan which would need to be approved by employees or subsidized by the Government. It also includes significant uncertainty as to how you do project so many valuation results for so many years. The further you get into projections, which is the case in this sort of stochastic modelling, the more the long term results may be questionable. In our situation, the asset ceiling test presumes the plan is maintained permanently, hence a perpetuity calculation. As such, we do not see the real value of this and this is not seen in practice. However, in order to illustrate what the calculations may look like for an approach “along the line” of View 3 questioned by the Ontario AG we have prepared results based on the Level 3 defined above. This would represent what is seen in practice under PS3250 that is the closest to the View 3 spirit for an entity that would not have such a clear access to surplus in an agreement like we have here.

We have therefore performed a calculation in line with Level 3 using the future contributions as per the funding report. For OTPP, we have used the period to 2026 (11 year horizon) referred to on page 15 of the funding report for the special contribution requirement. For the OPSEU PP, we have used a period of 16 years indicated on page 8 of the funding report. We believe this to be a comprehensive calculation to determine the EFB.

Based on the introduction we made on the facts and circumstances linked to the conclusion found in the initial reports, we believe that this calculation is what may represent the very minimum EFB calculation. There are other elements that would generate other EFB such as surplus withdrawal and also the consideration of the excess return coming from the accounting best estimate (6.25%) compared to the funding valuation basis (for instance 4.85% under the OTPP). This would likely have an incidence in reducing the number of years of required employer contribution (11 years and 16 years used in our calculation).

Please find below our responses to the Ontario AG questions.

---

1. The report makes reference to the earlier section of paragraph 59 of PS 3250 but it's not clear to us how the section highlighted in PS 3250.059 has been addressed in the analysis. Were any amounts excluded that were subject to the restrictions identified? Have the approvals been obtained if they were not excluded?

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

OTPP

In our quantitative analysis in section 3 of the report (and the more detailed one provided below to question 2), the EFB from future service accrual is enough to cover the entire plan asset position and thus no amount for surplus withdrawal was considered in the EFB due to the nil impact it would have in regards to the asset ceiling test. However, we note in section 4 of the report the elements that would go into considering a temporary surplus distribution. A few key points is that the plan would need to enter 1 of the top 2 funding zones and also considering Funding management policy (FMP) provisions that refer to access to surplus. This is based on the FMP and the actual event would be triggered by the agreement amongst the partner group (which consists of the Ministry of Education and OTF). The FMP does have protective rights for the Government to ensure access to the surplus and not just to the employees. This supports that surplus distribution has a realistic economic value to the employer and could also be a part of the EFB if needed to support the asset ceiling calculation. We do see an entitlement to the government through the documents that the parties have set up (and agreed) and therefore we identify that the government has a right to surplus as a possible benefit.

OPSEU PP

In our quantitative analysis in section 3 of the report (and the more detailed one provided below to question 2), the EFB from future service accrual is enough to cover the entire plan asset position and thus no amount for surplus withdrawal was considered in the EFB due to the nil impact it would have in regards to the asset ceiling test. However, we note in section 4 of the report the elements that would go into considering a temporary surplus distribution. The Regulations and the Funding Policy (FP) focus on the Sponsors ability to access unused surplus (held in the reserve) to address minimum funding contributions including normal cost. Under the FP, section 5.1 refers to some options of using surplus. The item 5 of Section 5.1 indicates that it is suggested to consider temporary reduction of contribution as the most predictable way of reducing the surplus. Reduction of contribution is identified as the most predictable way, but likely not the only possible way. Since the idea of the plan is to share 50 / 50 the gains and specifically through reserves identified separately for each sponsor, surplus withdrawals may be expected as one other way of dealing with surplus. The idea is that when gains occur, they are shared and used by each sponsor. The contribution reduction is identified as one "predictable way" of using the surplus. Similar to the OTPP, the calculations for OPSEU PP assume no surplus withdrawal value under EFB as non required to support the asset position.

2. We are requesting an EFB calculation that would be along the lines of "View 3" as part of the analysis. We were expecting this type of calculation given the magnitude and complexity of these pension plans. Could you let us know please when we can expect this by as we would like to review the results of this calculation.

We have performed the following calculations in line with the Level 3 described previously.

It does include reference to the plans respective funding valuations. For both plans, the funding reports identify horizon for contributions (11 for OTPP and 16 for OPSEU PP) that we have used in calculation. For service accruals, based on the landscape of the plan being assumed to continue indefinitely, we have taken service cost amounts in perpetuity. This is what we see in practice for an open plan that still accepts new employees. As noted, no distinct surplus withdrawal amount is defined as it is non necessary to support the asset position. Also, we note, that based on the best estimate assumption for asset return, there is also a significant improvement expected in the plan situation for funding that may further reduce the horizon for required contributions, again no specific amount included in the EFB but this would only increase it (just as an illustration, based on the difference between accounting expected return on asset and the funding discount rate used in the determination of the contribution amounts, we obtain about $1.2B annual excess return for OTPP and $37M annual excess return for OPSEU PP).

The various inputs to the calculations are detailed and the source of information identified.

The conclusion for both plans is that even without any surplus withdrawal factored in the EFB or effect of excess return, there is plenty of room to support the asset position. It reflects practice observed recently for few cases along the lines of View 3 shown in the initial report. This is therefore what we believe to be a minimal EFB approach under PS3250 for an entity that would not have such clear access to use the surplus. Other sources of EFB may be supported by the plans facts and circumstances of the OTPP and OPSEU PP, but they are not needed as the conclusion would be unaffected.

calculation_EFB_estimate_Sept1_2016_Base Case.pdf

	Plan OTPP	(in $B)	**Information**
a)	Value of asset - market value used	85,7	*From Excel File*
b)	Value of accounting obligation	58,2	*From Excel File*
c)	Surplus (deficit)	27,5	*a - b*
d)	Unamortized (gains) losses - market value used	-16,2	*From Excel File*
e)	Adjustment for March 31, 2016	-0,9	*From Excel File*
f)	Asset (liability) position	10,4	*c + d + e*
g)	Specific Government adjustment	-0,3	*From Excel File*
h)	Final Asset (liability) position on balance sheet	10,1	*f + g*
i)	Adjusted benefit asset	10,1	*h - max (0 ; d) as per PS3250.053*
j)	Expected future benefit	29,3	*Minimum EFB basis calculation illustrated (k - l + m)*
k)	- Perpetuity of employer service cost	44,6	*r)*
l)	- Minimum funding requirement	15,3	*s), assuming contribution to 2026 as per the report for special contribution, no excess return used for simplicity*
m)	- Surplus withdrawal	0,0	*As per the plan funding policy, the employer would have some access to surplus withdrawal. For simplicity, we have used 0 in the test.*
	TEST : Valuation allowance = max (0 ; i - j)	0,0	*No valuation allowance required, no adjustment to the balance sheet asset position, PS3250.050 and PS3250.054*

Expected Future Benefit Calculations

n)	Total plan service accrual accounting	2,9	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
o)	Employer service accrual share	50%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
p)	Expected return on asset - accounting assumption	6,25%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
q)	Salary increase - accounting assumption	3,00%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
r)	Perpetuity of Employer service cost - accounting	44,6	*n * o / (p - q), present value of all future service cost to the employer (the 50% share)*
s)	Minimum employer funding requirement as at March 31, 2016	15,3	*Sum of the present value of future required contributions (table below), using the funding report and the period of additional contribution requirement (until 2026, funding report page 15)*
t)	Expected Future Benefit	29,3	*r - s, Perpetuity of employer service cost minus the minimum funding requirement as at March 31, 2016*

Year	**Estimated Contributions**[1]	**Present value of each contribution**
2016[2]	1,3	1,2
2017	1,7	1,6
2018	1,8	1,6
2019	1,8	1,5
2020	1,9	1,5
2021	2,0	1,4
2022	2,0	1,4
2023	2,1	1,3
2024	2,1	1,3
2025	2,2	1,3
2026	2,3	1,2

	% assumpt	$B return
Accounting return on asset	*6,25%*	*5,4*
Funding return on asset	*4,85%*	*4,2*
Excess return each year using best estimate		*1,2*

[1] Estimated contributions from funding report (p.16), increased based on salary increase accounting assumption

[2] Remaining contributions used as at March 31,2016 (9 months for 2016)

	Plan OPSEU	(in $M)	**Information**
a)	Value of asset - market value used	9 200	*From Excel File*
b)	Value of accounting obligation	7 778	*From Excel File*
c)	Surplus (deficit)	1 422	*a - b*
d)	Unamortized (gains) losses - market value used	-558	*From Excel File*
e)	Adjustment for March 31, 2016	-292	*From Excel File*
f)	Asset (liability) position	572	*c + d + e*
g)	Specific Government adjustment	-52	*From Excel File*
h)	Final Asset (liability) position on balance sheet	520	*f + g*
i)	Adjusted benefit asset	520	*h - max (0 ; d) as per PS3250.053*
j)	Expected future benefit	2 750	*Minimum EFB basis calculation illustrated (k - l + m)*
k)	- Perpetuity of employer service cost	6 262	*r)*
l)	- Minimum funding requirement	3 511	*s), assuming contribution to 2026 as per the report for special contribution, no excess return used for simplicity*
m)	- Surplus withdrawal	0	*As per the plan funding policy and plan text, it is unclear whether the employer would have some access to surplus withdrawal. For simplicity, we have used 0 in the test.*
	TEST : Valuation allowance = max (0 ; i - j)	0,0	*No valuation allowance required, no adjustment to the balance sheet asset position, PS3250.050 and PS3250.054*

Expected Future Benefit Calculations

n)	Total plan service accrual accounting	407	*From OPSEU Jan 25, 2016 documentation*
o)	Employer service accrual share	50%	*From OPSEU Jan 25, 2016 documentation*
p)	Expected return on asset - accounting assumption	6,25%	*From OPSEU Jan 25, 2016 documentation*
q)	Salary increase - accounting assumption	3,00%	*From OPSEU Jan 25, 2016 documentation*
r)	Perpetuity of Employer service cost - accounting	6 262	*n * o / (p - q), present value of all future service cost to the employer (the 50% share)*
s)	Minimum employer funding requirement as at March 31, 2016	3 511	*Sum of the present value of future required contributions (table below), using the funding report and the period of additional contribution requirement (until 2032)*
t)	Expected Future Benefit	2 750	*r - s, Perpetuity of employer service cost minus the minimum funding requirement as at March 31, 2016*

Year	**Estimated Contributions**[1]	**Present value of each contribution**
2016[2]	204	199
2017	279	259
2018	287	251
2019	296	243
2020	305	236
2021	314	228
2022	323	221
2023	333	215
2024	343	208
2025	353	202
2026	364	196
2027	375	190
2028	386	184
2029	398	178
2030	410	173
2031	422	167
2032	435	162

	% assumpt	$M return
Accounting return on asset	*6,25%*	*575*
Funding return on asset	*5,85%*	*538*
Excess return each year using best estimate		*37*

[1] Estimated contributions from funding report (p.12), increased based on salary increase accounting assumption

[2] Remaining contributions used as at March 31,2016 (9 months for 2016)

calculation_EFB_estimate_Sept1_2016_Extr Case.pdf

	Plan OTPP	(in $B)	**Information**
a)	Value of asset - market value used	85,7	*From Excel File*
b)	Value of accounting obligation	58,2	*From Excel File*
c)	Surplus (deficit)	27,5	*a - b*
d)	Unamortized (gains) losses - market value used	-16,2	*From Excel File*
e)	Adjustment for March 31, 2016	-0,9	*From Excel File*
f)	Asset (liability) position	10,4	*c + d + e*
g)	Specific Government adjustment	-0,3	*From Excel File*
h)	Final Asset (liability) position on balance sheet	10,1	*f + g*
i)	Adjusted benefit asset	10,1	*h - max (0 ; d) as per PS3250.053*
j)	Expected future benefit	10,2	*Minimum EFB basis calculation illustrated (k - l + m)*
k)	- Perpetuity of employer service cost	44,6	*r)*
l)	- Minimum funding requirement	34,4	*s), assuming contribution to 2026 as per the report for special contribution, no excess return used for simplicity*
m)	- Surplus withdrawal	0,0	*As per the plan funding policy, the employer would have some access to surplus withdrawal. For simplicity, we have used 0 in the test.*
	TEST : Valuation allowance = max (0 ; i - j)	0,0	*No valuation allowance required, no adjustment to the balance sheet asset position, PS3250.050 and PS3250.054*

Expected Future Benefit Calculations

n)	Total plan service accrual accounting	2,9	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
o)	Employer service accrual share	50%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
p)	Expected return on asset - accounting assumption	6,25%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
q)	Salary increase - accounting assumption	3,00%	*From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation*
r)	Perpetuity of Employer service cost - accounting	44,6	*n * o / (p - q), present value of all future service cost to the employer (the 50% share)*
s)	Minimum employer funding requirement as at March 31, 2016	34,4	*Sum of the present value of future required contributions (table below), using the funding report and assuming a 33 year period of additional contribution requirement (until 2048)*
t)	Expected Future Benefit	10,2	*r - s, Perpetuity of employer service cost minus the minimum funding requirement as at March 31, 2016*

Year	**Estimated Contributions**[1]	**Present value of each contribution**
2016[2]	1,3	1,2
2017	1,7	1,6
2018	1,8	1,6
2019	1,8	1,5
2020	1,9	1,5
2021	2,0	1,4
2022	2,0	1,4
2023	2,1	1,3
2024	2,1	1,3
2025	2,2	1,3
2026	2,3	1,2
2047	4,2	0,6
2048	4,3	0,6

	% assumpt	$B return
Accounting return on asset	*6,25%*	*5,4*
Funding return on asset	*4,85%*	*4,2*
Excess return each year using best estimate		*1,2*

[1] Estimated contributions from funding report (p.16), increased based on salary increase accounting assumption

[2] Remaining contributions used as at March 31,2016 (9 months for 2016)

	Plan OPSEU	(in $M)	**Information**
a)	Value of asset - market value used	9 200	*From Excel File*
b)	Value of accounting obligation	7 778	*From Excel File*
c)	Surplus (deficit)	1 422	*a - b*
d)	Unamortized (gains) losses - market value used	-558	*From Excel File*
e)	Adjustment for March 31, 2016	-292	*From Excel File*
f)	Asset (liability) position	572	*c + d + e*
g)	Specific Government adjustment	-52	*From Excel File*
h)	Final Asset (liability) position on balance sheet	520	*f + g*
i)	Adjusted benefit asset	520	*h - max (0 ; d) as per PS3250.053*
j)	Expected future benefit	547	*Minimum EFB basis calculation illustrated (k - l + m)*
k)	- Perpetuity of employer service cost	6 262	*r)*
l)	- Minimum funding requirement	5 714	*s), assuming contribution to 2026 as per the report for special contribution, no excess return used for simplicity*
m)	- Surplus withdrawal	0	*As per the plan funding policy and plan text, it is unclear whether the employer would have some access to surplus withdrawal. For simplicity, we have used 0 in the test.*
	TEST : Valuation allowance = max (0 ; i - j)	0,0	*No valuation allowance required, no adjustment to the balance sheet asset position, PS3250.050 and PS3250.054*

Expected Future Benefit Calculations

n)	Total plan service accrual accounting	407	*From OPSEU Jan 25, 2016 documentation*
o)	Employer service accrual share	50%	*From OPSEU Jan 25, 2016 documentation*
p)	Expected return on asset - accounting assumption	6,25%	*From OPSEU Jan 25, 2016 documentation*
q)	Salary increase - accounting assumption	3,00%	*From OPSEU Jan 25, 2016 documentation*
r)	Perpetuity of Employer service cost - accounting	6 262	*n * o / (p - q), present value of all future service cost to the employer (the 50% share)*
s)	Minimum employer funding requirement as at March 31, 2016	5 714	*Sum of the present value of future required contributions (table below), using the funding report and assuming a 35-year period of additional contribution requirement (until 2050)*
t)	Expected Future Benefit	547	*r - s, Perpetuity of employer service cost minus the minimum funding requirement as at March 31, 2016*

Year	**Estimated Contributions**[1]	**Present value of each contribution**
2016[2]	204	199
2017	279	259
2018	287	251
2019	296	243
2020	305	236
2021	314	228
2022	323	221
2023	333	215
2024	343	208
2025	353	202
2026	364	196
2027	375	190
2028	386	184
2029	398	178
2030	410	173
2031	422	167
2032	435	162
2049	718	96
2050	740	93

	% assumpt	$M return
Accounting return on asset	*6,25%*	*575*
Funding return on asset	*5,85%*	*538*
Excess return each year using best estimate		*37*

[1] Estimated contributions from funding report (p.12), increased based on salary increase accounting assumption

[2] Remaining contributions used as at March 31,2016 (9 months for 2016)

FW_ 2011 Funding Decision.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
Subject: FW: 2011 Funding Decision
Date: Monday, September 19, 2016 11:42:40
Attachment 1: image001.jpg

From: Roberto, Nicole (EDU)
Sent: September 19, 2016 10:23 AM
To: Petsche, Nadine (TBS)
Cc: Sekaly, Gabriel (EDU); Killoch, Alex (MOF); Pomykacz, Rob (MOF); Paul, Joshua (EDU); Duffy, Paul (EDU); Franks, Sebastian (EDU)
Subject: FW: 2011 Funding Decision

Yes – contribution rates between the employee and employers are always equal, with one exception of 2008, when the OTF made a portion of the employee contribution. See table:

https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1-d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf

Note: the 1.1% was phased in over 3 years

Year

Up to CPP limit

Above CPP limit

Increase*

2011

10.4%

12.0%

N/A

2012

10.8%

12.4%

0.4%

2013

11.15%

12.75%

0.35%

2014

11.5%

13.1%

0.35%

Total increase

1.1%

* As a percentage of salary

From: Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca>

Sent: Monday, September 19, 2016 9:39 AM

To: Paul, Joshua (EDU); Sekaly, Gabriel (EDU); Killoch, Alex (MOF); Pomykacz, Rob (MOF)

Subject: Fw: 2011 Funding Decision

Please advise. N

From: Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>

Sent: Monday, September 19, 2016 9:38 AM

To: Petsche, Nadine (TBS)

Subject: 2011 Funding Decision

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

Was this contribution rate increase shared by the teachers?

Matthew Colley

Sr. Manager | Audit Advisory

Deloitte LLP

22 Adelaide Street West,

Toronto, Ontario,

M5H 4E3

D: 416-643-8428

mcolley@deloitte.ca | deloitte.ca

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image001.pdf

Deloitte.

NATIONAL
PARTNER

FW_ Analysis of how surplus could reduce future contributions.rtf

From: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: Analysis of how surplus could reduce future contributions
Date: Wednesday, September 14, 2016 23:03:36
Attachment 1: Picture (Device Independent Bitmap) 1.jpg

From: Colley, Matthew (CA - Toronto)
Sent: Wednesday, September 14, 2016 11:03 PM
To: Veinot, Cindy (CA - Toronto) (cveinot@deloitte.ca) <cveinot@deloitte.ca>; Petsche, Nadine (nadine.petsche@ontario.ca) <nadine.petsche@ontario.ca>
Subject: Analysis of how surplus could reduce future contributions

Hi Cindy and Nadine,

Have you performed an analysis that shows how, through the mechanics of the FMP and with regard to the position of the entity at the year end, how the Province could realize the surplus through reducing its contributions?

Based on the key funding decisions from 1990 onwards it appears that there was a contribution reduction in 1993, 1996, 1998 but then nothing since then (although this appears to be due to the fact that we were in a funding shortfall position until 2012). So why is there an expectation that this asset will be recovered through future contribution reductions and what roadblocks stand in the way of this?

This might warrant a discussion rather than a response, and apologies for the tone, but we are asking the questions to strengthen the communication of the analysis that has been given to date.
Thanks

Matt

Matthew Colley
Sr. Manager | Audit Advisory
Deloitte LLP
22 Adelaide Street West,
Toronto, Ontario,
M5H 4E3
D: 416-643-8428
mcolley@deloitte.ca | deloitte.ca

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Picture (Device Independent Bitmap) 1.pdf

Deloitte.

NATIONAL
PARTNER

FW_ As discussed.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: As discussed
Date: Thursday, September 15, 2016 22:22:29

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: September 15, 2016 9:07 PM
To: Petsche, Nadine (TBS)
Subject: Re: As discussed

Thank you Nadine.

I will be in touch tomorrow.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 09/15/2016 08:47 PM
Subject: As discussed

Hi Lucy.
Further to our discussion, below is an outline of the work we discussed. The work relates to the jointly sponsored pension plans (OTPP and OPSEUPP) as reported in the Province's consolidated financial statements.

I’ll look forward to hearing back from you.
Best regards,
Nadine
416 562 9509

The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following

· Taking into account public sector accounting principles, advice and guidance on complex accounting and reporting matters related to accounting for pensions on the Province’s consolidated financial statements.
· The Vendor will participate in meetings as necessary to support the engagement objectives:

· Working with management of OPCD’s Accounting Policy and Financial Reporting Branch (APFR), the provider of complex accounting services related to the following possible areas:
· Develop discussion and analysis material
· Develop draft input/briefing materials/option papers
· Provide accounting advice and guidance related to the accounting for pensions on the Province’s financial statements
· Participate in discussions with internal and external stakeholders, as required

As part of this engagement, the consultant(s) would be expected to provide professional accounting expertise in assessing actuarial assessments for specified plans in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250 (3250.050 to PS3250.059).

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FW_ As discussed.rtf

From: Petsche, Nadine (TBS) []
To: Chen, Raymond (TBS) [Raymond.Chen@ontario.ca]
Subject: FW: As discussed
Date: Friday, September 16, 2016 11:06:08

Good news! n

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: September 16, 2016 11:05 AM
To: Petsche, Nadine (TBS)
Subject: RE: As discussed

Hi Nadine,

I've discussed this internally and we should be able to do something for you. I think it would be helpful for me to give you a call to discuss in more detail and to discuss next steps. I am about to go into a meeting, but I should be able to give you a call around 12pm (or later, if that works better for you). Will I be able to reach you this number - 416 562 9509?

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 09/15/2016 10:22 PM
Subject: RE: As discussed

Thanks Lucy. Nadine

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: September 15, 2016 9:07 PM
To: Petsche, Nadine (TBS)
Subject: Re: As discussed

Thank you Nadine.

I will be in touch tomorrow.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 09/15/2016 08:47 PM
Subject: As discussed

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Best regards,
Nadine
416 562 9509

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complex accounting and reporting matters related to accounting for pensions on the Province’s consolidated financial statements.

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- Develop discussion and analysis material
- Develop draft input/briefing materials/option papers
- Provide accounting advice and guidance related to the accounting for pensions on the Province’s financial statements
- Participate in discussions with internal and external stakeholders, as required

As part of this engagement, the consultant(s) would be expected to provide professional accounting expertise in assessing actuarial assessments for specified plans in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250 (3250.050 to PS3250.059).

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FW_ As previously referenced.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: As previously referenced
Date: Thursday, September 22, 2016 10:40:35

Cindy,

Not sure if we want to do anything here, and if so, what that might be?

From: Colley, Matthew (CA - Toronto) [mailto:mcolley@deloitte.ca]
Sent: September 22, 2016 10:34 AM
To: Petsche, Nadine (TBS)
Cc: Veinot, Cindy (TBS)
Subject: RE: As previously referenced

Thanks Nadine,

Thinking back to yesterday's conversation with the AG, part of the concern was around the audit evidence that has been provided to support that the asset will be recovered. It seemed at one point during the meeting that she might have been able to get to how approximately $8B will be recovered. Maybe you could think about how you could articulate to them how the evidence you have provided or summarize to them how the evidence you provided supports the asset. I am just thinking if there are ways that it could be framed to help get them more comfortable about the audit evidence they have.

Regarding the statement of facts, we did send a communication last night to the AG thanking her for her time yesterday and asking if she could confirm whether they believe them to be accurate and complete, and more formally notifying her that we are engaged to provide an accounting opinion. For the time being we have removed the facts around the impact of restoring inflation indexation, but we have indicated that this assertion made by management will likely be factored into our opinion.

Thanks

Matt

From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Thursday, September 22, 2016 10:25 AM
To: Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Cc: Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>
Subject: As previously referenced
Importance: High

Hi Matt.

Please see last page**

Nadine

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FW_ Draft pension asset deck.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: FW: Draft pension asset deck
Date: Monday, October 31, 2016 09:19:31
Attachment 1: Deck outline (JK) - OTPP Pension Asset Oct 28.docx

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Draft deck as per my earlier email. n

Deck outline (JK) - OTPP Pension Asset Oct 28.pdf

Accounting by the Province of Ontario for the Ontario Teachers' Pension Plan

Preamble

Analysis is specific to OTPP

Constating documents are different than for other pension plans in Ontario and in other provinces

Issue being considered

The Province followed the same accounting for OTPP for the prior 14 years during which the pension accounting standard (Section PS 3250) was the same.

In relation to the 2015-16 public accounts for the Province of Ontario, the OAG disagreed with the Province's accounting for OTPP and OPSEUPP

The OAG disagrees that the surplus in OTPP is a reportable asset to the Province on the basis that:

- there is no legally enforceable right to the asset
- no agreement is in place at March 31, 2016 with the Ontario Teachers' Federation (OTF) to reduce future contributions

Reporting in the 2015-16 Public Accounts

The Province disagrees with the AG's interpretation of PSAB standards.

The Province believes their share of the plan accounting surplus should be recognized as an asset. The Province expects to benefit from the reported pension assets through reduced contributions and has performed the requested pension asset ceiling test to confirm that the Province's estimated asset value is not impaired.

For purposes of the 2015/16 Public Accounts, the Province regulated the accounting treatment for pension assets for the jointly sponsored pension plans (OTPP and OPSEUPP) to reflect the Auditor General's interpretation of PSAB. Since Management does not agree with the AG's interpretation of PSAB as related to the jointly sponsored pension plans, the regulation was necessary to achieve the AG's accounting treatment and to allow management to sign off on the Statement of Responsibility.

Overview of OTPP

A jointly sponsored pension plan (JSPP) as defined in the Pension Benefits Act. The OTPP meets this definition. The sponsors are the Province of Ontario and the OTF.

The sponsors are jointly responsible for decision making, share in contributions, and collectively address any plan funding surplus/deficit (at least every 3 years)

The plan administrator is an independent board of directors and follows the direction of the co-sponsors on all key decisions, which includes plan structure, level of plan benefits, contribution rates, funding levels and contingency reserves and changes to the plan documents.

Prior accounting for OTPP by the Province

Since 2001-2002, the Province has recorded its portion (50%) of the pension asset of OTPP in accordance with Section PS 3250

With regards to expected future benefit of the surplus, the Province would not expect to withdraw any surplus, but through reduced future contributions

The Province and OTF have a history of equally sharing the benefits of surplus utilization as demonstrated from the time OTPP became a JSPP to the date the Funding Management Policy in 2003 was established (include in appendix only)

Question 1 – Recognition of a pension asset

First we address why the surplus of OTPP is an asset to the Province

Applicability of Section PS 3250 to OTPP

The purpose and scope of Section PS 3250 is included in paragraph .001 which states "This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements".

Obligations for retirement benefits result from a promise by a government to provide these benefits to employees because of retirement in return for their services (paragraph .03).

Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

Definition of JDBP

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

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

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

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

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

The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan (glossary to Section PS 3250).

Primary sources of GAAP

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity.

PS 3250 provides clear guidance that a JDBP is accounted for using PS 3250 and therefore is the primary source of GAAP that must be applied.

Other standards in PSAS including the Financial Statements Concepts should be referred to if PS 3250 does not provide specific guidance for a circumstance.

Concept of shared control and asset recognition

Section PS 3250 requires the government to account for its portion (as there is shared control) of a JDBP following the accounting requirements for a defined benefit plan within PS 3250; no distinction is made as to whether the plan is in a surplus or deficit position. In a JDBP the risks and rewards of a plan are equitably shared, so the Province's portion of the plan includes its share of any asset as well as its share of any liability

The Financial Statement Concepts definition of an asset includes "control" over an economic resource. Despite the conceptual framework not directly addressing "Shared control" it is included in other standards in PSAS, for example relating to government partnerships (Section PS 3060) which existed prior to PS 3250

Conclusion on recognition

Section PS 3250 on its own is sufficient to assess the accounting for OTPP by the Province

OTPP is appropriately classified as a JDBP under Section PS 3250

Section PS 3250 requires recognition by the Province of 50% of the plan assets of OTPP

Unilateral control is not necessary for asset recognition (as also seen with government partnerships); shared control is appropriate for a JDBP

Uncertainty relating to OTPP's pension surplus relates to measurement, not uncertainty regarding expected future benefits for the Province

Question 2 – Measurement of a pension asset

Second we address how to measure the pension asset of OTPP in the Province's financial statements

Guidance in Section PS 3250 on measurement

An overview of the pension accounting for a defined benefit plan (and therefore a JDBP) in Section PS 3250 includes:

An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance for any excess of the adjusted benefit asset over the expected future benefit (paragraph .050)

An accrued benefit asset is the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance) (Glossary).

A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions (paragraph .052).

To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset which is the accrued benefit asset less net unamortized actuarial losses (paragraph .053).

The adjusted benefit asset is then compared to the expected future benefit. The objective is to limit a government's accrued benefit asset to the amount it can realize in the future (paragraphs .054 and .055).

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

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

b) the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations (referred to as the asset ceiling test - paragraph .056).

Guidance on measurement as applicable to OTPP

The Province expects future benefits from OTPP's plan surplus to be realized through reduced future contributions, not withdrawals. There is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'.

Expectations of benefitting from the surplus are based on:

1. The Teachers' Pension Act requires equal contributions from the Province and from plan members of OTPP;

2. The history of surplus utilization for OTPP demonstrates sharing of the financial benefit between sponsors;
3. No sponsor of OTPP can unilaterally utilize the plan's surplus; and
4. If the sponsors of OTPP cannot agree on how to utilize the pension surplus, the matter can be submitted to arbitration.

The Province considers that the uncertainties around how and when to utilize the surplus do not result in an inability or lack of entitlement to utilize the surplus

Calculating the limit on the carrying amount of an accrued benefit asset (asset ceiling test)

Calculation of the asset ceiling test involves professional judgement. As a reminder Section PS 3250 indicates the expected future benefit to be recorded by the government is the sum of:

a. The present value of its expected future accrual for service for the current number of active employees less the present value of minimum contributions the government is required to make regardless of any surplus; plus
b. The amount of the plan surplus that can be withdrawn in accordance with the existing plan and any laws and regulations.

The next slides will consider this calculation relative to the Province's 50% share of OTPP

Through withdrawal of the surplus (Part b of the asset ceiling test)

The Province does not consider there to be expected future benefit available through withdrawal of any plan surplus.

Section PS 3250 specifies that an amount for withdrawal of surplus is only included when a government has a legally enforceable right of withdrawal.

In accordance with the Funding Management Policy for OTPP, the parties must negotiate in order for a withdrawal of the surplus to happen, therefore the Province does not have a signed agreement with OTF regarding the withdrawal of the surplus.

Through reducing future contributions (Part a of the asset ceiling test)

While Section PS 3250 states that legal enforceability is required to include an amount for a withdrawal of the plan surplus it does not include a similar requirement in respect of the ability to benefit through future contribution reductions. The Province has an expectation that they will benefit fully from the asset by exercising their current rights under the plan arrangements to negotiate the use of surpluses in the form of contribution holidays.

The present value of its expected future accrual for service is typically calculated based on the Province's share (50% for OTPP) of the current service cost reported in the most recent actuarial valuation taken into perpetuity

There is very limited guidance in PSAS on determining the present value of minimum contributions the government is required to make regardless of any surplus; professional judgement is required. The Province engaged consultants to calculate this value for OTPP considering different assumptions on future minimum contributions. Considered was the contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. The key scenarios considered include

- TBD.(Pauline)

For purposes of OTPP in the 2015-16 public accounts, 11 years was used by the Province reflecting management's best estimate of the number of future years for which current minimum contributions are to be made until the Income Tax Act limits are reached

Based on the Province's best estimate calculation of the expected future benefit, no valuation allowance was deemed necessary in relation to the pension asset of OTPP at March 31, 2016

Other guidance in PSAS on measurement

Section PS 2130 provides guidance on dealing with measurement uncertainty

Measurement uncertainty in pension plan accounting exists for example in the estimation of the valuation allowance and in the determination of the discount rate (which is often management's best estimate of the rate of return on plan assets)

Historical rates of return on plan assets have supported the past discount rates used by the Province in relation to OTPP

Comparability of Ontario's accounting for JDBPs to other Provinces

Provinces such as British Columbia and New Brunswick do not report assets for their provincial joint sponsored pension plans or alternatively provide a valuation allowance to reduce the pension asset balance to nil

The difference in accounting versus the Province of Ontario (for OTPP) results from these other provinces not having any access to the pension surpluses unlike in Ontario

Conclusion on measurement

The Province's position is that the attributes of the JDBP arrangements for OTPP entitle the Province to access its portion of the plan surplus through the right to negotiate its use of the Province's benefit through future reduced contributions

Significant professional judgement and estimation is involved in determining the valuation allowance under Section PS 3250; the Province has applied reasonable estimates

Based on the result of modelling performed in relation to the asset ceiling test, the Province concluded that no valuation allowance was necessary to the pension asset that would have otherwise be reported on the Province's books as at March 31, 2016.

FW_ Employee Life and Health Trusts (ELHTs) - accounting treatment.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
CC: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]; Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]; Hosick, Sarah (TBS) (Sarah.Hosick@ontario.ca) [Sarah.Hosick@ontario.ca]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]
Subject: FW: Employee Life and Health Trusts (ELHTs) - accounting treatment
Date: Monday, March 27, 2017 22:17:55
Attachment 1: ELHTs Accounting Treatment (EY 27 March 2017).pdf
Attachment 2: image001.jpg

Cindy,

Please see attached documentation from EY on ELHT. I've advised Christina and Shayan that we can plan to discuss on our call on Wednesday.

Nadine

From: Christina Chan [mailto:Christina.Chan@ca.ey.com]
Sent: March-27-17 5:46 PM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani
Subject: Employee Life and Health Trusts (ELHTs) - accounting treatment

Hi Nadine,

As requested, we have prepared the attached document discussing the following topics:

1) Accounting treatment related to the provisions of the ELHTs under PSAB 3250/3255 (and the associated risks to the school boards)

2) Comparison of the ELHTs with Shared Risk Pension Plans

Both Shayan and I will be at Queen's Park tomorrow. Let us know if you have any comments. We are available if you would like to discuss prior to our meeting on Wednesday.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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ELHTs Accounting Treatment (EY 27 March 2017).pdf

Ernst & Young LLP
222 Bay Street, P.O. Box 251
Toronto, Ontario M5K 1J7

27 March 2017

Accounting Treatment - Employee Life and Health Trusts

OPCD has asked EY to comment on the accounting treatment related to the provisions of benefits from the Employee Life and Health Trusts ("ELHTs") under the Public Sector Accounting Standards.

Background

Historically, health, life and dental benefits were provided to employees in Ontario's educator sector through a multitude of individual plans administered separately by the Ontario school boards. To improve the cost-efficiency and delivery of benefits, all individual benefit plans are consolidated into six Employee Life and Health Trusts[1], each covering a certain group of employees. Each ELHT is established to meet the definition of an ELHT under the Income Tax Act Sc. 144.1. Benefits are provided through a joint governance structure between the bargaining/employee groups, school board trustees associations and the Government of Ontario under the ELHTs.

The ELHTs are intended to provide benefits to employees during their employment years. There are also separate retiree provisions intended to provide access to benefits for retirees.

Member groups

In order to determine the necessary accounting treatment, it is important to identify the different member groups and their respective benefit entitlements. Three groups of members with different benefit entitlements under the ELHTs are:

- "Active": approximately 211,000 members
- "Pre-August 2013 Retirees"[2]: approximately 5,700 members
- "Post-August 2013 Retirees"[3]: approximately: 1,400+ members

For current Active employees, the contributions by the boards to the ELHTs are fixed and negotiated during bargaining. Annual contribution amounts required from the boards per full-time employee are pre-determined for the period covered by collective bargaining agreements. Upon retirement, active members may be eligible for retiree benefits at full cost and they are not eligible for any cost subsidization (i.e. provisions for Post-August 2013 Retirees).

Certain members who retired prior to August 31, 2013 are eligible for a partial or full subsidization of benefit costs from the board, based on prior arrangements with their employer. The members are eligible to participate in the ELHTs until age 65 (with the exception of a small group who are eligible for lifetime coverage).

All members retiring after 31 August 2013 are eligible to participate in the ELHT through a Voluntary Plan and Separate Account. However, they are responsible for the entire cost of benefits. They are not eligible for any cost subsidization.

[1] OECTA, ETFO, AEFO, OSSTF Trust Agreements have been formally signed; CUPE and PVP/Non-union are to be finalized.
[2] Members retiring prior to 31 August 2013
[3] Members retiring after 31 August 2013

According to the ELHT Trust Agreements Article 6, "*the Trustees may establish any number of Separate Accounts within the Fund. The assets in each Separate Account shall be held as segregated funds and used for the provision of Benefits, in accordance with the terms of a Plan, to a discrete and identifiable group of Participating Employees*". Based on the benefit entitlements described above, presumably, a Separate Account is established for the Active members and a Separate Account is established for the Pre-August 2013 Retirees. Therefore, there is no cross-subsidy. For example, retiree costs are not cross-subsidized by premiums paid in respect of Active employees.

The Trust agreement state that any surpluses in a Separate Account may be used to increase Claims Fluctuations Reserve ("CFR"), enhance benefits, or reduce employee contributions. Conversely, any deficiencies in the trust may require the use of the CFR, amendment to benefit (reduction), or an increase to employee contribution levels.

For the Pre-August 2013 Retirees group, it is our understanding that if there is a funding deficiencies in the Separate Account for this group, the school board will be required to contribute and reimburse the Trust to make up the funding shortfall ("chargeback").

Accounting treatment

Paragraphs 011 – 012 of PSAB 3250 (see Appendix) discuss the classification of benefit plans as Defined Benefit ("DB") or Defined Contribution ("DC"). Further, in accordance with 3250.014, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan.

Considering the different provisions applicable to member groups and PSAB 3250.011 – 3250.012, the benefits provided through the ELHTs include DB provisions in respect of retiree groups, whereas Active member benefits do not fall in the scope of PSA 3250/3255. Specifically:

- *Active:* Benefits/costs relating to current active members does not fall under the scope of PS 3250 (Retirement Benefits) or PS 3255 Retirement Benefits (Post-employment benefits, compensated absences and termination benefits). The scope of these sections cover benefits payable in retirement, after employment but before retirement, or compensated absences or termination benefits. Costs relating to providing benefits to active members during employment would be expensed annually in amounts equal to the fixed contribution. Further, as current active members are not eligible for subsidized benefits upon retirement (i.e. they pay for the entire cost of the post-retirement coverage without any cost to the employer), there is also no post-retirement obligation. To the extent that members on long-term disability are also eligible to receive benefits from the ELHT, a defined benefit obligation may need to be recognized under PS3255 in respect of expected future contributions over the anticipated period of long-term disability in respect of disabled employees.

- *"Pre-August 2013 Retirees:* The provisions relating to certain members who retired prior to 31 August 2013 would be classified as DB provisions as the boards are at risk with respect to the amount of benefits these employees will receive. These risks include the possibility of higher/lower than expected claims, or greater/less than expected longevity. We understand that the school boards have historically reported defined benefit obligations in respect of the ongoing commitment to subsidize retiree benefits for members in this group and will continue to do so subsequent to the transition to the ELHTs. This is appropriate as the ELHTs would be reimbursed by the boards for any contribution requirement to make up for the deficit in providing the coverage for these members.

- *"Post-August 2013 Retirees:* By contrast, there is no cost to the school boards relating to members retiring after 31 August 2013. The entire cost is borne by retirees and the school boards are not required to make any additional contributions in the future in the event of any shortfall. School board contributions are not

subject to any actuarial risk. Rather, all risks are borne by the retirees. In the event that funds are insufficient to pay for benefits, the trust agreements outline measures to address those deficiencies. The measures include the application of reserves, increases to member contributions and a reduction in benefits. None of the measures require any additional contributions from the school boards.

Therefore, we understand there to be a defined benefit obligation only in relation to the benefit entitlement for the subsidies provided to certain members retired prior to 31 August 2013. In addition, there may be a defined benefit obligation in respect of members on long-term disability to the extent that the ELHT covers such members.

Comparison with Shared Risk Pension Plans

In recent years, a number of Canadian provinces have adopted "Shared Risk Pension Plan" legislation. Shared Risk Pension Plans (SRPPs) provide benefits under a defined benefit formula, while putting cost constraints on employer contributions. Employer and employee contributions are often restricted within a band and benefits may be subject to reductions depending on the funded level.

In general, Shared Risk Pension Plans have been viewed as defined benefit plans. Risks are shared by the employer and employees, with the employer usually being subject to some level of actuarial and market risks. There may, however, be instances where DC accounting could be possible. This would be the case when no risk is retained by the employer, i.e. contributions are fixed in all scenarios. As there are many variations of Shared Risk Pension Plans, careful judgment is required to determine the appropriate accounting treatment in each case.

At the request of OPCD, we have compared the key characteristics of the ELHTs established by the Ontario school boards to those of Shared Risk Pension Plans. We have not considered the provisions relating to Pre-August 2013 Retirees, as these are clearly DB provisions under PS 3250/3255.

When comparing the benefits for the Active members under the ELHT with the SRPPS, there are a number of important differences to be considered but the following two are most significant:

- As SRPPs provide post-retirement benefits, they are within the scope of PS3250; however, as demonstrated in the previous section, the benefits provided for the Active members under ELHTs do not fall under the scope of PS3250.
- For SRPPs, the employer is subject to some level of actuarial risks and market risk as future contributions may be increased to pay for past deficiencies. Under ELHTs, the school boards are not subject to any risks: (a) contributions are fixed (as required by a Central Collective Agreement or any applicable Participation Agreement); (b) no additional contributions will be required for the related past service regardless of future actuarial or market experience; (c) the contributions required by the school boards are not dependent on the funding position of the Separate Account. Rather, employee's contributions (or benefits paid) may increase or decrease based on the surpluses/deficiencies of the Separate Accounts.

Further, there is no cost (and therefore, no post-retirement benefits) for members retiring after 31 August 2013 under the ELHTs. For these reasons, we would not expect the same accounting treatment to be applied for the SRPPs and ELHTs.

Appendix – Public Sector Accounting Board ("PSAB") 3250 Retirement Benefits (applicable excerpts)

.011 Two types of benefit plans are addressed in this Section — defined benefit plans and defined contribution plans. A defined benefit plan is one that specifies either the benefits to be received by employees after retirement or the method for determining those benefits. Generally, the amount and value of the benefits to be paid depend on a number of factors and events. These include how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation and retirement age. When a government provides benefits under a defined benefit plan, it is at risk with respect to the amount of the benefit that each employee will receive (actuarial risk) and with respect to the investment returns on any assets set aside to pay for the cost of these benefits (investment risk).

.012 When a government provides benefits under a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. A defined contribution plan (or money purchase plan) is one in which a government's contributions in respect of services rendered by employees are specified. The government is required by the plan to make a specific fixed contribution each period. If that contribution is made, no additional government contributions are required now or in the future for the related service. The employees are at risk. This is generally because the amount of the benefit that will be payable to an employee is dependent upon the funds accumulated for each employee's account and the investment earnings on the accumulated funds.

.013 Because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of a particular plan makes it a defined benefit or a defined contribution plan.

. 014 In some circumstances, a benefit plan may include both defined benefit and defined contribution promises. The plan, for example, may guarantee a basic defined retirement benefit and state that additional benefits, such as inflation protection, will be provided on a defined contribution basis. In such circumstances, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan. Once the type(s) of promise is identified, the accounting and reporting principles in this Section would be followed accordingly.

Appendix – Public Sector Accounting Board ("PSAB") 3255 Post-Employment Benefits (applicable excerpts)

Purpose and scope

.01 This Section establishes standards on how to account for and report obligations for post-employment benefits, compensated absences and termination benefits in government financial statements.

.02 This Section applies to post-employment benefits, compensated absences and termination benefits earned by employees and expected to be provided to them when they are no longer providing active service either on a temporary or permanent basis. For the purposes of this Section:

- *(a) Post-employment benefits are expected to be provided after employment but before retirement to employees and their beneficiaries. These benefits include long- and short-term disability income benefits (including workers' compensation), severance benefits, salary continuation, supplemental unemployment benefits, job training and counselling, and continuation of benefits such as health care benefits and life insurance.*
- *(b) Compensated absences are benefits for employee absences for which employees will be paid. These benefits include parental leaves, accumulated sick days, and sabbaticals that provide compensated, unrestricted time off for past service.*
- *(c) Termination benefits include the following:*
  - *a. Contractual termination benefits are benefits required to be provided to employees under the existing terms of a benefit arrangement when a specific event occurs that results in the downsizing and termination of a group of employees.*
  - *b. Special termination benefits are benefits that are not contractual termination benefits and that are offered to employees for a short period of time, normally not exceeding twelve months, in exchange for employees' voluntary or involuntary termination of employment.*

.03 The glossary in RETIREMENT BENEFITS, Section PS 3250, provides definitions for other relevant terms.

.04 This Section does not apply to short-term employee benefits, which would be accounted for under the general provisions for accruing liabilities. This accounting is generally straightforward because no actuarial assumptions are required and the liabilities are measured on an undiscounted basis.

.05 Examples of such short-term employee benefits are:

- *(a) Salaries, wages, bonuses, fringe benefits and similar items a government provides in the current reporting period or within twelve months thereafter, in exchange for services rendered by employees in the current reporting period; and*
- *(b) Occasional sick days and vacation days that do not vest or accumulate beyond twelve months after the current reporting period.*

Post-employment benefits, compensated absences and termination benefits are liabilities of a government. Accounting for all benefit plans is important because many governments have accumulated significant related liabilities. The fundamental accounting task is to determine the amount of the liability for these benefits and to what periods to attribute the costs.

.07 These standards are consistent with those established in RETIREMENT BENEFITS, Section PS 3250. The standards set out in that Section are appropriate for accounting for and disclosing post-employment benefits, compensated absences and termination benefits of a government. For example, a government providing these types of benefits through a defined contribution plan, multiemployer plan or joint defined benefit plan would refer to the guidance set out in Section PS 3250. This Section sets out those areas where the accounting and reporting are different from Section PS 3250.

image001.pdf

EY

FW_ Follow up.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]
Subject: FW: Follow up
Date: Wednesday, November 02, 2016 15:16:23

Hi Matt.
I haven't heard back yet on the matter related to sharing the accounting opinion. Can you please follow up and advise. Nadine

-----Original Message-----
From: Danyluk, Kerry (CA - Toronto) [mailto:kdanyluk@deloitte.ca]
Sent: October 26, 2016 3:29 PM
To: Petsche, Nadine (TBS)
Cc: Colley, Matthew (CA - Toronto); Jesty, Paula (CA - Toronto)
Subject: RE: Follow up

Hi, Nadine. I think you knew that Matt is away this week on vacation? However, I believe that he has organized someone on his team to get in touch with you about the other pension analysis. Maybe she has already done so?

Regarding the question of permission for the opinion, I am still working through that question and what caveats we might want to put on it.

Please let me know if you wish to discuss.

Kerry

--
Kerry Danyluk
Partner | National Accounting and Assurance
D: +1 (416) 775 7183
kdanyluk@deloitte.ca | deloitte.ca
--
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Please consider the environment before printing.

-----Original Message-----
From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Wednesday, October 26, 2016 5:40 AM
To: Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>
Subject: Follow up

Hi Kerry.
I'm just following up on a couple of items that I talked to Matt about last week...
1) permission to share the accounting opinion with the Pension Asset Expert Advisory Panel -. Please confirm if such permission is granted and advise of any related considerations with regards to such sharing.
2). Extended pension analysis for OPSEUPP, HOOPP, CAATPP. As discussed with Matt, we are expediting acctg analysis for the remaining 3 plans wrt accounting for plan assets on the Province's books. Matt had indicated that staff would be assigned, and we assume that work is underway or to be started shortly. Completed analysis is considered important as input to the Panel. We would like to touch base on status and next steps (note; we have not yet received any requests for infoirmation).
Please let me know when you might be a available to discuss.

Thanks.
Nadine
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FW_ Interim invoice.rtf

From: Petsche, Nadine (TBS) []
To: uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Interim invoice
Date: Monday, June 19, 2017 16:15:07
Attachment 1: image001.gif
Attachment 2: Invoice-C100093008.pdf

Thanks Uros.

We'll commence the payment process.

Nadine

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: June 19, 2017 1:50 PM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani; Christina Chan; Sarah Anderton
Subject: Interim invoice

Hi Nadine,

Further to your discussion with Shayan, here is the invoice for $65k. As you know, our work is on-going. We are also mailing a hard copy of this invoice today, but I thought you'd appreciate receiving a soft copy too.

If it is at all possible to process the payment before the end of the month (our year-end) that would be greatly appreciated.

Many thanks,

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

Invoice-C100093008.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100093008.pdf (243550 Bytes).

FW_ Meeting on employee future benefits.rtf

From: Sun, Alicia (TBS) []
To: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]; Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]
CC: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Meeting on employee future benefits
Date: Friday, June 09, 2017 12:40:06

Hi Shayan/Christina,

Ministry of Education (School Boards, ELHT related) would like to schedule a call with the school board auditors (Deloitte and KPMG in this case) to have a further discussion on the liability for employees on LTD.

EDU would like your counterpart from the accounting side to join the call and lead the discussion with the school boards auditors.

Please let me know whether you can reach out to your colleagues and let me know a time that will work for them.

Thanks,

Alicia

FW_ NPP comments on draft position paper.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: FW: NPP comments on draft position paper
Date: Saturday, October 22, 2016 21:38:39
Attachment 1: Draft Pension Asset Position Paper Oct 22 np to ld with responses np2.docx
Attachment 2: TPP rates of return (performance vs discount rates).xlsx

---

Hi Lucy.

Just heard from Cindy. She won't be able to look at the memo until tomorrow due to a family emergency. Thanks again for all of your help. N

From: Petsche, Nadine (TBS)
Sent: October-22-16 9:32 PM
To: 'lucy.durocher@ca.pwc.com'
Cc: Veinot, Cindy (TBS)
Subject: RE: NPP comments on draft position paper

Thanks Lucy. My responses are enclosed. Looks really good from my perspective. I've also remembered to attach the rate experience doc this timeJ

Nadine

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: October-22-16 4:58 PM
To: Petsche, Nadine (TBS)
Cc: Veinot, Cindy (TBS)
Subject: Re: NPP comments on draft position paper

Hi Nadine,

Here are my responses to your comments.

Regards,
Lucy

Lucy Durocher

PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Veinot, Cindy (TBS)" <Cindy.Veinot@ontario.ca>
Date: 10/22/2016 03:49 PM
Subject: NPP comments on draft position paper

Hi Lucy.
Thanks again for your efforts to create the draft paper for review this weekend. You'll find my suggested edits and comments attached. I also shared your original draft with Cindy, but I'm not sure of the status of her review. As we await her comments, I thought it would be best to share my feedback with you directly, and to cc her on my note so that she might add any additional comments to this version if she has not already started her review.
You will see that there is one section in particular, related to the minimum contribution period that I think would benefit from some review and edit. As this is the Province's position paper, I think we can convey a stronger message that downplays any suggestion that there are mandatory minimum payments required into perpetuity.
Thanks again.
Nadine
p.s. the second attachment reflects my edits in your original track changes version, and the first attachment reflects them against your clean version. [attachment "Draft Pension Asset Position Paper Oct 22 np to ld.docx" deleted by Lucy Durocher/CA/ABAS/PwC] [attachment "Outline of position paper to JK PF tab2 v5 - PwC edits Version 3np.docx" deleted by Lucy Durocher/CA/ABAS/PwC]

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Draft Pension Asset Position Paper Oct 22 np to ld with responses np2.pdf

Position paper for Ontario Teachers' Pension Plan

Preamble

This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP.

As described in PSAS, a pension asset arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. Contributions reflect the funding objectives of the plan. The benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (or plan surplus for accounting purposes) in OTPP and OPSEUPP are an asset to the province and it is suitable to reflect them in the financial results.

The OAG disagrees with this position. The OAG 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 Ontario Teachers' Federation (OTF) with respect to how the surplus would be utilized such that it would provide a benefit to the Province, a pension asset in the Public Accounts is not appropriate.

Ontario had followed the same pension accounting treatment for all of the past 14 years. This had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals. There has been no change to the relevant PSAS (i.e. RETIREMENT BENEFIT, Section PS 3250) over the past 14 years.

A regulation was made to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The Province filed a time-limited regulation, which legislates the accounting for pension assets of its two jointly-sponsored

pension plans for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The impact of the change resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to write off the pension assets. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

What is being asked of the Expert Advisory Panel

The Expert Advisory Panel is being asked to review and deliver advice and recommendations to the government as to the application of PSAS to Ontario's pension assets. The future accounting by the Government of its pension assets will be guided by the report of the Expert Advisory Panel.

The Expert Advisory Panel 's advice and recommendations to the government will address:

- The requirement regarding control (or shared control) with respect to recognizing a pension asset for a defined benefit plan, as it relates to the pension plans reported by the Province of Ontario, including OTPP, OPSEUPP, HOOPP, and CAAT.
- Appropriate valuation techniques to measure a pension asset that take into consideration future decision making authority by plan sponsors.
- Recommendations to the Employment Benefits Task Force of the Public Sector Accounting Board (PSAB) regarding issues that should be considered in their review of the retirement and post-employment benefits standards.

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1.

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
1. It provides defined benefits.
2. The defined benefits are contributory benefits.

DRAFT

Position paper for Ontario Teachers' Pension Plan

The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the Ontario Teachers' Federation represented by its Executive (the ”OTF") (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners Agreement (FMP);
f) The Ontario Teachers' Pension Plan; and
g) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

3. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
4. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).

With respect to the cost-sharing principle referred to in #3 above, the TPA 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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5] The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (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, 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 inception of the plan in 1917). [7] 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. [8] 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 a JSPP, 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.

DRAFT

[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).
[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/101791209401-l5e47lc2b-23f1-44e6-b5cld22e3e50dbc3lHow+ Contribution+Rates*HaverEvolved.pdf As noted above, for the period from January l, 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%/11.20lo versus l0.4yo/l2Vo, respectively). It ~~is~~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.
[8] See, for example, Section 3.09 and 3.11 of the FMP.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix E. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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 funding surpluses that may arise under the plan.

4. When negotiations occur as laid out in the Partners' Agreement. The Partner's Agreement requires that any actuarial funding valuation submitted to the pension regulators must be "actuarially balanced" (Section 57 of the Partners' Agreement). This must occur at least once every three years, but can occur every year if the partners agree. If a preliminary funding valuation shows a funding surplus or deficit then the joint sponsors must negotiate how this surplus or deficit is resolved prior to filing the funding valuation.

Commented [NP1]: Last part not entirely clear

LD response – suggested changes. Npp - thx

Commented [NP2]: Should the relevant context be discussed…no mandatory minimum contributions (in perpetuity)

LD response – This is background information so I had kept it relatively facts based, rather than interpretive to the standard, which is included later in the paper. More of the interpretation could be brought forward if management feel that it helps the paper. Npp – ok.

Accounting for OTPP by the Province

Since fiscal year 2001-2002, the Province has recorded a pension asset for OTPP on the Statement of Financial Position. A pension asset has arisen because the government's share (50%) of the total contributions to OTPP plus the actual investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense. The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

With regards to any comparisons between asset amounts reported in the Province's financial statements verses the OTPP's financial statements or funding reports, it is important to acknowledge the different objectives of funding and accounting for a pension plan which are also explicitly addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit*

Commented [NP3]: Note: An implicit assumption exists that at the time that the new pension standard was implemented, the Controller's office and the OAG would have reviewed the appropriateness of reflecting an asset based on the constating agreements which have not substantially changed over time. Similarly, the requirement to perform an asset ceiling test would have presumably been considered as part of the initial discussions when implementing the standard. At no time prior to the 2015/16 Public Accounts audit did the OAG raise any concerns regarding the appropriateness of the interpretation of PSAB standards in relation to the jointly sponsored plans, nor the lack of asset ceiling tests. That said, OPCD does acknowledge that an asset ceiling test to validate if the assets are impaired, is prudent and in accordance with PSAB. The results of the test conducted as part of the 2015/16 Public Accounts concluded that no impairment existed and therefore no valuation adjustment was required.

In addition to raising issues with regards to the interpretation and application of PSAB standards to the joint benefit plans, the AG has referenced comparative surplus/deficit results reported by OTPP both for financial reporting and funding purposes.

LD response – Noted – I see the additional paragraph added in this section to reflect the above points.

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expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.

Paragraph PS 3250.051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: "Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…"

OTPP's most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website. The Province's relative portion of this surplus would be $6.6 billion. The OTPP's public financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015, for which the Province's portion would be a deficit of $900 million. The following background helps to clarify the reasons for these different results. OTPP's financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook ("Part IV"), which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the net surplus or deficit for funding purposes. Accounting for employee future benefits requires the use of assumptions and methodologies to calculate both the obligation incurred to date and the value of the assets already set aside to meet those obligations. Accounting frameworks differ in standards that must be applied in determining appropriate assumptions and methodologies. Further, the assumptions and methodologies used in developing a "funding valuation" on a going concern basis may also differ from those required by accounting standards. These differences result in a number of different valuations for the same plan, depending on the purpose of the valuation and can be affected by certain choices made between acceptable options within each framework. A summary of the main differences between the methodologies used to calculate a going concern funding valuation, OTPP's accounting valuation and the Province's accounting valuation is shown in Appendix H.

Specifically, the discount rate has a significant impact on the overall position of the plan. A lower discount rate results in a higher liability and a higher discount rate results in a lower liability, all else being equal. Put another way, a higher estimate of the time-value of money makes the promises made today that will be paid out in the future cheaper. Both the PSAS accepted discount rate based on the expected asset return and the IFRS required discount rate of corporate/government bonds are "best estimate" rates. They must both be based on management's best estimate of the applicable discount rate. In both cases the estimates must be supportable. The difference results not from one being more "right" or "wrong" relative to the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.

The rationale for using a corporate or government bond approach is that a pension promise is akin to a bond as it is a promise to pay a series of cash flows in the future regardless of what the asset returns actually are (which could be higher or lower than expected). The rationale for using an asset return approach is that it represents the amount of contributions that, combined with investment returns, should be sufficient to pay the promised benefits, particularly as pension plans will often invest in higher risk/higher return assets then simple corporate bonds. Typically the funding discount rate falls between

Commented [NP4]: In fact, experience on OTPP demonstrates that returns have on average continued to exceed management's long term estimates reflected in the discount rate.

Wonder if it would be worthwhile to include the historical results for background. (attached summary of performance to response email)

LD response – Continued experience of returns exceeding the discount rate would indicate that the expected asset returns (and therefore the discount rate) are not actually high enough. These increased returns would come through as actuarial gains, eventually amortized to the income statement. Perhaps I am missing what the point would be of including the historical results? How does it help the arguments?

Npp – comment is with reference to the AG's suggestion that the discount rate used by the Province should actually be lower (match OTPP's used for f/s purposes)…the discount rate used by the province as management's best estimate of return might be argued to be conservative when compared to actual return experience. Not sure if there might be a relevant place to include this observation or not.

the bond discount rate and the expected asset return, but it differs in that it does not purport to be the "best estimate" of the discount rate, but is designed to indicate the contributions that are required to fund the promised benefits, with an additional conservative margin for adverse deviations. Note that over the long term the difference between funding valuations and accounting valuations would diminish as the impact of the discount rate unwinds and the asset valuation methods converge.

In practice, the discount rates used in the financial statements of government sponsored and joint defined benefit pension plans prepared under Part IV of the CPA Canada Handbook (Section 4600) use diverse methodologies. For example, in Alberta 7 plans prepare their financial statements under Part IV with reference to IFRS (same framework as OTPP). Of these none use a government bond discount rate and all use a discount rate calculated with some reference to a rate of return on invested assets, which may include factors for expenses, diversification and rebalancing. The analysis of a number of government sponsored plans is included as Appendix [**G**]. The analysis demonstrates that a significant number of government sponsored plans use a discount rate aligned to an asset investment return rather than a bond discount rate. OTPP is in the minority of plans that choose to use the rate required by IFRS, resulting in a lower discount rate and higher liability.

The above analysis discusses the impact of different discount rates on the net surplus/deficit reported on OTPP's financial statements, OTPP funding reports and the Province's financial statements. The fact that OTPP reports a deficit on its financial statements, or that the net surplus reported by OTPP for funding purposes is lower than the surplus reported on the government's financial statements under PSAB standards is of no consequence or relevance to this analysis.

To further clarify, that that that there is a deficit reported in the OTPP financial statements while the Province of Ontario calculates a surplus under PSAS requirements does not mean that there is no accounting surplus and therefore no reportable asset for the Province. In fact, if the OTPP would have accepted a rate more consistent with its counterparts in other jurisdictions (see Appendix G) that would also be acceptable under the Part IV framework as an accounting policy choice (e.g. a discount rate based on an asset return which would be closer to that used by the Province), it would eliminate much of the existing differences between the reported net surplus/deficit amounts between the OTPP statements and the Province's share of OTPP reported for accounting purposes in the Public Accounts.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. Unqualified audit reports have been received for each of the years from the OAG on the Public Accounts.

RETIREMENT BENEFIT, Section PS 3250 of the PSA Handbook addresses the accounting of obligations for employee retirement benefits in government financial statements. The Province has followed this standard over the prior 14 years. Over this period of time, there have been no consequential changes to Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years. The pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years is reflected in Appendix F.

Although OPCD has not been able to substantiate decisions made at the time that the Province implemented PS 3250 in 2001, it is assumed that the Controller's Office and the Office of the Auditor General would have engaged in more specific and detailed discussions related to the interpretation and application of the standard with regards to the joint sponsored pension plan at the time. The presumed outcome of those discussions would have supported the Province's share of the surplus being reported on the Province's books based on the shared control over the plan as evidence by the constating documents. It is uncertain whether the need to perform asset ceiling tests on a regular, on-going basis was discussed at the time and there is no evidence of any having been performed previously. The pension accounting adopted by the Province for OTPP since 2001 had been implicitly accepted by the current Auditor General for the last two years and by the three previous Auditors Generals for the prior years.

History regarding the PSA standards

As mentioned, the financial statements for the Province have been prepared over the prior 14 years in accordance with the PSA Handbook, reflecting decisions made by the Provincial Controller at the time that PS 3250 was implemented and which were accepted by the Office of the Auditor since that time.

Completeness of PS 3250 in assessing appropriate accounting for pension assets

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150 prescribes that, in developing and applying accounting policies, all primary sources of GAAP should be applied. Primary sources of GAAP are Sections PS 1200-PS 3510, Public Sector Guidelines and appendices and illustrative material to those pronouncements. Only when there are no primary sources of GAAP that relate to the transactions or events under consideration, or more specific guidance is needed, does an entity consider other primary sources of GAAP dealing with similar issues and also the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000. Section PS 1000 is not, however, a "primary source of GAAP" under the PSA Handbook.

The primary sources of GAAP specific to the accounting for pension assets is RETIREMENT BENEFITS, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, Section PS 3250 which was based on Accounting Statement No. 5).

Other primary sources of GAAP that deal with similar issues might also be considered where additional interpretation or guidance may be required. For the issues dealt with in this paper - recognition and measurement of a joint defined benefit plan - this could include standards that relate to joint control, as OTPP is a joint defined benefit plan, standards that relate to the definition of an asset and standards that relate to measurement uncertainty:

- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015, effective from April 1, 2017)
- MEASUREMENT UNCERTAINTY, Section PS 2130 (issued in April 2005)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 which is more recent and will be effective in for periods beginning on or after April 1, 2017. Section PS 3210 provides additional guidance on the various components of the existing asset definition found in Section PS 1000; it does not change the definition.

Accounting Analysis

Question 1 – Recognition of a pension asset

The analysis below addresses whether the Province's share of the pension surplus in OTPP, calculated in accordance with PSA standards under PS 3250, represents a reportable asset to the Province of Ontario in the Public Accounts.

Standards in the PSA Handbook

The focus of the following analysis is on the accounting requirements in RETIREMENT BENEFIT, Section PS 3250 as this standard is a primary source of GAAP which specifically addresses the accounting for pension assets. The following highlights some key concepts and guidance contained in this standard.

RETIREMENT BENEFIT, Section PS 3250 – Purpose and Scope

The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250, paragraph .003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

RETIREMENT BENEFIT, Section PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*
>
> *(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;*
>
> *(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and*
>
> *(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.*
>
> *The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.*

Additional guidance on identifying Joint Defined Benefit Plans (JDBPs) is in PS 3250 paragraphs .79 to .80 which similarly highlight the importance of both shared control and shared risks and rewards in a JDBP:

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

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

A JDBP is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. The OTPP is a contractual arrangement between the Province and OTF in which:

(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees (addressed in paragraph 8 of the Partners' Agreement for example);

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example).

There is no uncertainty regarding the joint control of OTPP shared by the Province of Ontario and the Ontario Teachers Federation. The TPA, the Partners' Agreement and the plan text collectively set out this shared control and that the Province of Ontario has an equitable sharing of the risks and rewards (surpluses and deficits) of the plan based on the definition of a joint defined benefit plan.

As noted above, the classification of OTPP as a JDBP by the Office of the Provincial Controller has been consistent since 2001 and had been consistently and without question accepted by the Office of the Auditor General prior to the 2015/16 Public Accounts.

RETIREMENT BENEFIT, Section PS 3250 – Accounting for a JDBP

RETIREMENT BENEFITS, Section PS 3250 paragraphs .081 to .082 provide guidance on the accounting for a JDBP in the financial statements of the government sponsor. As OTPP meets the definition of a JDBP for the reasons noted above, the relevant guidance for the Province for purposes of reporting retirement benefits in the Public Accounts includes:

> *.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]*
>
> *.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.*

Section PS 3250.81 clearly states that "The government should account for its portion of the plan in accordance with the standards for defined benefit plans". It is clear from this that only the government's portion of the plan is included in the government's financial statements consistent with the requirements of Section PS 3250 (recognition) and the measurement of that portion is based on the requirements of Section PS 3250 (measurement). It is also then clear that the requirements of the standard for recognition and measurement, including the Limit of the Carrying Amount of an Accrued Benefit Asset guidance, are designed to be applied to a joint control situation and not only to situations where there is unilateral control. If it was intended that no pension asset could be recognized because the asset was subject to joint control and not unilateral control paragraph .081 would have made this clear. This paper discusses the two elements of recognition and measurement separately.

Commented [NP5]: Should we point out that the standard does not require unilateral control?

LD response – have added in a sentence to reflect this. Npp - thx

The balance sheet recognition guidance for retirement benefits is stated in Section PS 3250.016 to .017:

> *.016 The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date. [SEPT. 2001]*
>
> *.017 The components of the retirement benefit liability are:*
>
> > *(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;*
> >
> > *(b) plan assets, if any; and*
> >
> > *(c) unamortized actuarial gains and losses.*

As the OTPP is a funded plan there are plan assets that are recognized as part of the retirement benefit liability. When plan assets and the impact of unamortized actuarial gains and losses exceed the accrued benefit obligation then there is an "Accrued benefit asset" (ABA). An ABA is defined in Section PS 3250 as follows:

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

Accordingly, the portion of the government's plan to be recognized includes their share of the accrued benefit obligation and also their share of the plan assets. In the case of the Province's portion of OTPP there is no uncertainty regarding the *existence* of an ABA for the government's portion of the plan, based on the best estimate assumptions used in measuring the accrued benefit obligation and plan assets, measured in accordance with Section PS 3250 guidance for these items. As noted above an ABA is defined as the government's sum of the accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance). For a jointly sponsored plan this is the government's accumulated cash contributions less the sum of the government's share of the current and prior years' benefit expenses that are attributable to the government under the joint defined benefit plan. The Province's portion of OTPP resulted in an ABA of $10.1 billion as at March 31, 2016. There is no uncertainty regarding the occurrence of the cash contributions made (including interest earned thereon) measured in accordance with Section PS 3250 and the existence of the government's obligation. As Paragraph 3250.80 *requires* a government to account for its portion of the plan in accordance with the standards for defined benefit plans, this would include the recognition of any asset that meets the definition of an ABA under the standard.

Further, Section PS 3250 paragraph 3250.50 refers to the presentation of the ABA; this amount is presented in the financial statements, net of any valuation allowance. This indicates that an ABA should be recognized in the financial statements, but measured in reference to the limit on the carrying amount of the asset - essentially a measurement requirement rather than a recognition requirement, as an ABA could be measured at anything from $nil to its full amount. Note that the *measurement* of any net asset is subject to guidance in Section PS 3250 paragraphs .50-.59 and is discussed later in this paper.

To recognize only their share of the liability and not their share of the plan assets, or to recognize only a net liability (accrued benefit obligation exceeds plan assets) but never a net asset (when plan assets exceeds the accrued benefit obligation, subject to the valuation allowance guidance discussed in the Measurement section below), would indicate that the ~~government~~ Province does not share equitably in the risks and rewards of the ~~plan~~ OTPP because they bear only the risk of increased liabilities without being able to bear any ~~the~~ rewards of investment returns on the plan assets and under this interpretation the plan would not therefore be a joint defined benefit plan.

Commented [NP6]: Might be a good place to make reference to relevance of specific terms and conditions of the OTPP arrangement, and lack of comparability with plans in other jurisdictions which may have different terms & conditions.

LD response – I wasn't sure where to put the comparison to other province's section. I am open to it being here or where it is (at the end). If you think it flows better here, then it would be a good place. Npp - some suggested wording edits.

Concept of Shared Control and Asset Recognition

Included in the definition of a JDBP is the concept of shared control. Points (c) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of Shared Control resulting in a recognition of an asset could on the surface appear to conflict with the definition of an asset under FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210, as part of the definition of an asset under PS 1000 would suggest that the government must control the economic resource and access to the future economic benefits. Since joint control does not equate to control, there is a need to consider whether the recognition of any asset under PS 3250 is appropriate where there is only shared control.

The Province's position is that PSAS does not preclude asset recognition for assets under joint control and specifically for plan assets of joint defined benefit plans for the following reasons:

- As discussed above GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity. Section PS 3250 is a primary source of GAAP for dealing specifically with joint defined benefit plans and, as noted above, requires the government to account for their portion of the plan – both the accrued benefit obligation and plan assets in accordance with Section PS 3250. As such, reference to Section PS 3250 is sufficient to indicate that the recognition criteria are met for joint defined benefit plan assets, no further source of PSAS guidance need be considered.

- Similarly, if other primary sources of GAAP are considered then it is relevant to consider GOVERNMENT PARTNERSHIPS, Section PS 3060 which also includes the concept of shared control. Under Section PS 3060, joint control is sufficient for asset recognition.

- The concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. On the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that PSAB did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

Commented [NP7]: Necessary? Perhaps move up to earlier discussion of PS 1000?

LD response – I see your point. I had seen this as being more of a "conclusion" on the share control point as to why it was not inconsistent with the framework, but I think it also works as a bullet point here to emphasize that reference to 3210 and 1000 is difficult to a shared control concept.

Npp – ok.

- The Province's reporting of a pension asset for the JDBP is therefore consistent with these primary sources of GAAP, subject to measurement guidance including impairment considerations.

The similarities between the definitions of a JDBP and a government partnership under PSAS are demonstrated in Appendix B to this paper, and further support PS 3060 as being a relevant primary source of GAAP dealing with similar circumstances, should it be considered necessary to go outside of the requirements of Section PS 3250 to look for further clarification and guidance on recognition.

Under Section PS 3060 a critical condition for a Government partnership is shared control. Section PS 3060 explicitly acknowledges that under shared control "none of the partners is in a position to exercise unilateral control over the government partnership" (PS 3060.20), yet the accounting model required by Section PS 3060 for non- GBPs[9] is that of proportionate consolidation which is the picking up of a pro rata share of assets, liabilities, revenues and expenses of the partnership. Joint defined benefit plans are excluded from the scope of Section PS 3060 on the basis that control is shared with employees rather than with a party outside of the reporting entity (3060.06 footnote 3). This reason indicates that such plans are excluded because of a closer relationship between the government and the other party than normally exists for government partnerships. Even when an independent third party shares control, Section PS 3060 still requires the recognition of a share in an asset subject to joint control, indicating that the PSAS framework does not require unilateral control in order to support asset recognition when there is joint control. It would not be appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3060 for proportionate consolidation, and similarly it is not appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3250 to account for the government's portion of a joint defined benefit plan.

Conclusion on recognition

Therefore the Province has concluded that PSAS permits the conceptual recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets must be subject to unilateral control. The Province's share of OTPP's pension surplus meets the definition of an Accrued Benefit Asset under Section PS 3250. The measurement of that accrued benefit asset is determined by reference to the guidance in PS 3250 regarding the Limit on the Carrying Amount of an Accrued Benefit Asset, which is discussed in Question 2 of this position paper.

[9] Government business partnerships (GBPs) are accounted for under the modified equity method rather than proportionate consolidation.

Question 2 – Measurement of a pension asset

For an asset to be recognized it must be reliably measureable. Section PS paragraphs 3250.050 to .059 address how to measure a pension asset. "When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit." Paragraphs .052 to .059 go on to explain what the standard means by expected future benefit and how a government may benefit from the ABA. Section PS 3250.50-.59 are included here for completeness and ease of reference:

Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)

.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]

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

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

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

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

.055 The objective of the standard in paragraph PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated

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amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

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

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

Note that for purposes of Section PS 3250.053 the Province has determined that no pension valuation adjustment is necessary and as such that the accrued benefit asset equals the adjustment benefit asset (due to unamortized actuarial gains exceeding unamortized actuarial losses).

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Paragraph .052 states that a government may benefit from an ABA by either i) withdrawing surplus assets from the plan or ii) by taking a contribution holiday or receiving a refund of contributions. It is an explanatory paragraph on how a government may benefit from an accrued benefit asset and why a valuation allowance may be needed, rather than detailing the test to be applied. Part of this justification is to note that that an ABA may be impaired when "the government is not entitled to benefit from [the ABA] fully". Examples of when a government may not be entitled to benefit from the ABA fully are given, such as a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

The Province's expected future benefits to the surplus is intended to be through reduced future contributions, and not through withdrawal of pension surplus. As such, PS 3250.059 is not considered relevant to the analysis when performing the asset ceiling test. When considering the ability to realize expected future benefits, the Province's legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability which is not explicitly required by the standard to support recognition and measurement of JDBP pension assets. Specifically, the amount of pension asset that gets recorded needs to take into account considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a pension asset in the Public Accounts.

It is acknowledged that the Province does not have a unilateral legal right to reduce its contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to joint control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Paragraph .052 does not state that being "entitled to benefit" means having a legally enforceable right as at the reporting date to take contribution holidays or withdraw surplus. Under the Plan and Partners' Agreement, if funding surpluses occur the partners are required to negotiate the use of the funding surplus (at least once every three years) and the Province is entitled to negotiate a reduction in contributions in respect of its share of the surplus. Under the Partners' Agreement any funding surplus must be dealt with so that the funding valuation becomes actuarially balanced. *In other words when there is a funding surplus over a certain range the "status quo" cannot be maintained, the surplus must be reduced by a combination of reductions in contributions, increases in benefits or withdrawals of surplus*. While the Province might choose to accept an increase in member benefits rather than to reduce funding, any such decision is at the Province's discretion since the OTF cannot force the Province to increase benefits instead of reducing contributions. In other words it is at the Province's discretion whether to address the actuarial balancing requirements by allowing its portion of the surplus to be utilized through increased benefits. Therefore, the Province is entitled to negotiate their share of the JDBP and take contribution holidays in future negotiations and can effectively use their power in negotiations to benefit from the ABA. Note that while the negotiations are based on funding surplus amounts rather than accounting surplus amounts any differences would be captured in the mechanics of the calculation of the expected future benefit rather than precluding an ability to benefit from any of

the accounting surplus. ~~, and the measurement of the pension asset reported on the Province's books would not be impacted.~~

Further, paragraph PS 3250.055 indicates "The objective of the standard in paragraph PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Many generally accepted accounting frameworks use "expected" in a number of principles and is typically used in the probabilistic sense – something is expected when it is probable at some level, it does not equate to certainty. ~~nor does it require legal enforceability to be in place at year end.~~ The Province has an expectation that they will benefit fully from the ABA by exercising their current rights under the plan arrangements to negotiate the use of current and future surpluses in the form of contribution holidays. This position is supported by the review of the constating documents and past history of negotiations that indicate:

1. The TPA 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). 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.
2. 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 (refer to Appendix G for a history of surplus utilization for OTPP). 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.
3. 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.
4. 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. Under the plan contributions are generally borne equally by the Province and the employees. Employees benefit economically from both an increase in benefits and from a reduction of contributions. The Province benefits economically directly from a reduction in contributions. This makes it reasonable that at least some contribution reductions would be agreed to by the joint sponsors as a highly unequal weighting towards increases in benefits would not balance the interests of taxpayers and

Commented [NP8]: Lucy – please check

LD response – I'm not sure what you mean. Contribution holidays under the plan are predicated on there being funding surpluses – without a funding surplus it seems unlikely that the Province would be able to negotiate a reduction in contributions. Therefore I could not say whether the measurement of the pension asset reported on the Province's books would not be impacted because it really depends on how you are calculating your minimum contributions and what assumptions you are using. Npp - removed

Commented [NP9]: Lucy – check please

LD response – I've always thought of legal enforceability as relating more to the control or past transaction elements of the definition of an asset rather than the "expected future benefits" part, so while I can't say the additional comment is wrong it seems a bit incongruous to me as the two concepts just don't seem to belong together in my view. Npp - removed

Commented [NP10]: Also supported by positive working history of negotiations on use of surplus in the past, and the 'zones' which also refer to future benefits of reduced contributions on a temporary or permanent basis

LD response – added that both documents and past history support the position.
Npp – ok.

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therefore may be unlikely to be a reasonable outcome of "good faith" negotiations between the Province and the OTF.

This is further supported by the historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed in respect of conditional indexing, a decrease in benefits by the employees were offset by an increase in payments by the Province. Similarly as the sponsors agreed to restore indexation, this increase in benefits resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.98 for the 2015 change, and $1.68 for the 2014 change). This demonstrates that historically and over the long term an equitable sharing of the deficits and surpluses has resulted in changes in the Province's contributions, even when there are decreases or increases to benefits for employees.

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).

Commented [NP11]: Thought that mediation was the first step, then arbitration?

LD response – this was Jim's wording, so he may be better to ask regarding what he intended to convey.

Npp – Jim is not at all familiar with the agreements. Do you think it would be useful to insert reference to the mediation aspects as an interim measure before arbitration? We could get legal to review wording and edit.

Further to the discussion in Section PS 3250.052 regarding entitlement to benefits, PS 3250.059 provides further guidance where such benefits are expected to be realized through an entitlement to withdraw surplus. "A key factor in determining a government's expected future benefit from a defined

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benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal." PS 3250.59 is clear that expected future benefit available from surplus withdrawal can only be asserted where the government has a current legally enforceable right to withdraw assets from the Plan. Section PS 3250.59 introduces the concept of a legally enforceable right, however it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions. Had PSAB intended legal enforceability to be the test, they would have included that notion throughout the guidance (for example in paragraph .052), instead of only raising it in the context of a withdrawal of surplus.

The Province would not envision realizing any expected benefits through a withdrawal of surplus, but rather through contribution reductions or holidays. As such, from the Province's perspective, PS 3250.059 which deals with the situation of surplus withdrawals is not considered pertinent to the pension asset recognition or measurement analysis.

Based on the above analysis, the Province believes that the uncertainties around how and when to utilize a surplus in the OTPP do not result in an inability or lack of entitlement to utilize the surplus in accordance with Section PS 3250.52.

Calculating the limit on the carrying amount of an accrued benefit asset

PS 3250.53 to .58 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in PS3250.055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where actual realization of the benefit would be reflected in a reduction in future contributions. A valuation allowance is recorded against the Pension Asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test under PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as that expected future benefit is defined in paragraph .56.

Therefore in accordance with PS 3250.56 the Province calculated the expected future benefit as the sum of:

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

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

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Each of these is discussed separately.

Through withdrawal of the surplus (Section PS 3250.056 (b)

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, paragraph 3250.059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

The TPA for OTPP does not provide for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution, the Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

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The Province's position is that there is no amount of expected future benefit included in respect of withdrawable plan surplus as government does not have any intention to realize future benefits through surplus withdrawals..

Through reducing future contributions (Section PS 3250.056 (a))

PS 3250.56(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per PS 3250.81 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the Pension Asset value to be recorded in the accounts. For example, if the Pension Asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the Pension Asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. It is therefore relatively straightforward and is typically calculated based on the Province's share of the current service cost reported in the actuarial valuation taken into perpetuity unless there is evidence to indicate the workforce will significant diminish over time (for example a closed plan).

The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for judgment in the above calculation is in the determination of future minimum contributions required to be made by the government regardless of any surplus. Note that consistent with the calculation of the expected future accruals for service no amounts are considered for employee contributions as these relate to the OTF's portion of the plan. There is no further guidance in S 3250 as to how this calculation should be performed and what restrictions or parameters should be factored into this calculation.

Commented [NP12]: Include any reference to above statement that only the gov's ½ of the obligation and contributions factor into the calc?

LD response – Stated in the first paragraph of this section, but have added a sentence again to reinforce.

Npp-thx.

Determining the number of years of contributions to include should involve an assessment of the facts and circumstances of the plan and should consider uncertainty. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the contractual agreements between the Sponsors that provide for the sharing of risks

and benefits and specifically in respect of assessing the minimum contributions required by the plan agreements the following:

- One view of minimum contributions might be that the agreed upon level of contributions are the minimum contributions until they are altered in the plan text. As this can only happen with agreement from OTF it cannot be assumed that changes will be made and therefore that the contribution formula as stated in the current agreements will continue in perpetuity. This view provides the most conservative view of minimum payments. However as the current contribution amounts are greater than the government's share of the annual current service cost for the existing workforce this indicates that continued contributions at this rate will result in ever increasing surpluses. Extrapolating the surpluses, at a certain point other requirements that are currently incorporated into the plan text, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan will apply to reduce the contributions. The effect of these caps on contributions would have to be estimated but cannot be ignored as they form part of the current contribution arrangements. Modelling could be performed to develop expectations as to when these CRA limited could be expected to be reached assuming no changes in the contribution levels. As is the most conservative view (highest minimum contributions) the impact of this has been considered, as discussed below.
- An alternative view of the minimum contributions required by the plan is that there is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'. On this basis it could be argued that any agreed upon contribution levels are mandatory for only a three year period, after which the contributions must be renegotiated to stay the same, increase or decrease, such that the stated contribution level in the plan text constitute minimum payments for only three years. It should be noted that the plan text requires an actuarially balanced funding valuation, so to the extent that a funding deficit currently existed a contribution holiday (contributions lower than the annual cost of the plan) could not be negotiated. However because there funding situation at the time of future negotiations is not known it could be argued that no amount is a fixed "minimum contribution" in this context, because all of the contribution amount is subject to future changes in funding and negotiation by the joint sponsors.
- Other views of what the minimum contributions are would fall between these two views, such as that the current funding level is set to ensure that there is no funding deficit over a 11 year period and after that changes in contributions would be negotiated. This view has been used in calculating the actuarial calculation of the asset ceiling as noted in the table below.
- Another consideration might be the specific framework within the Funding Management Plan for OTPP which contemplates specified funding zones and expectations ~~regarding possible~~regarding possible contribution reductions by the sponsors. Informed stochastic modelling would be necessary to estimate when the different funding zones will be reached and probability of contribution reductions may be increased.

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Commented [NP13]: I don't think we agree with this. There is a requirement that they negotiate every 3 years…not likely that status quo would remain.

LD response – We could remove this, but I added it in because reference was made to the calculations of the Income Tax caps that kick in when you use this basis, so it seemed relevant to support why those calculations were being referred to. I thought the point of those calculations was to show that even if this view was taken there would still be recognition of a benefit. I think if you are going to refer to these calculations you need to acknowledge this possible interpretation, even while noting that this is not a realistic scenario.
Strategically it's a matter of whether acknowledging this view and then noting why an asset can still be supported is more effective than putting one strong argument for the position over minimum contributions. I think both are valid strategies – Management should decide which way they want to go.

Npp – thx. Agree that it should be included, but was just sensitive to the wording. Will await CV comments.

Commented [NP14]: Where there is a surplus, the parties are also mandated to negotiate. To avoid confusion for the Panel, suggest that this section should be restated.
If some element of this very conservative view is to be included, perhaps as the last item but then dismissed.

Commented [NP15]: When we say that the status quo would not remain, I think that the key point is that there would not be a mandated minimum amount that must be paid. The wording in this section will be very important and would benefit from rephrasing/repositioning. Key here is that we want to make a case for 'no perpetual' stream of minimum contributions.

LD response – good point, have added an extra sentence on this.
Npp – thx.

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- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to use some of the funding surplus to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change, $1.98 for the 2015 change, and $1.68 for the 2014 change).

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (PS 2130.03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in PS 2130.13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

Commented [NP16]: Consideration in gauging reasonability that the Province would ever expect to benefit from reduced contributions.

LD response – I am not sure what this comment means?

Npp – please ignore.

As part of the 2015/16 Public Accounts audit, the Office of the Provincial Controller engaged external experts to conduct asset ceiling tests to assess the requirement for a valuation allowance. The results of those reports are summarized here:

Plan	Asset recorded by Province (in billions)	Asset ceiling computed (in billions) and assumption re: years of contributions	Number of years contributions could be made without resulting in a valuation allowance
OTPP	$ 10.1	$29.3 (based on 11 years of contributions noted in the funding report as the period additional contributions are required)	33

The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (3250.56(a)). There is no guidance on the meaning of minimum contributions for purposes of this calculation in PS 3250.

Commented [NP17]: Moved this comment after the next section.

Under the Partners' Agreement, the parties are mandated to negotiate benefits and contributions every three years as a minimum and if agreement is not reached, it is reasonable to expect that a change in contributions might occur rather than the 'status quo' being retained.

For purposes of the OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

in addition to the above calculations, the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan should also be considered. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that no valuation allowance is required.

Commented [LD18]: This is the bit where it is assumed that contributions are unchanged and therefore minimum contributions are maintained to perpetuity.
This bit would have to be re-worked if the perpetual minimum contributions section was re-worked.

The determination of the ~~the~~ minimum contribution levels required as input to ~~the calculation~~the calculation ~~of the~~of the expected future benefit involves significant judgements, estimation and assumptions about future funding surplus levels. These judgements, estimates and ~~assumptions should~~assumptions should be made on a consistent basis with best estimates used in developing the accrued benefit obligations and plan asset amounts. Regardless of the need to apply judgements, estimates and assumptions for the calculation, this does ~~not imply~~not imply that no asset can be recognized or that it cannot be reliably measured. In fact, pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "~~expected future~~expected future benefit". From the Province's perspective, 'expected' does not equate to 'certainty'.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (3250.42) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (3250.41). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. 3250.57 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that

used to determine the accrued benefit obligation itself. The Province has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on Plan Assets, which is one of the acceptable references suggested on PS 3250.44.

The OAG and the Government differ regarding whether it needs to be "expected" that the Government will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in paragraph .059. The Government considers that it needs to be expected that future economic benefits are to be obtained as reflected in the definition of an asset in Section PS 1000 and as reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to use a plan surplus.

Other guidance in the PSA Handbook on measurement

Furthermore MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe would be a useful addition to the current year financial statements. PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.*
>
> *.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.*

We acknowledge that the estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans

Commented [NP19]: Insert reference to past history where actual returns have exceeded this rate?

LD response – see earlier comment.
Npp – if not helpful to insert, no need.

Commented [NP20]: Delete? Already addressed earlier in the paper

LD response – could do. I thought this was acting as a bit of a summary of the positions, but I agree it is repetitive and could be removed.

Npp – if summaries (as above) are to be included, then consistency is impt and ok with leaving.

Commented [NP21]: Addressed anywhere?

LD response – not sure what the concern is?
Npp – please ignore

involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is permissible under PSAB and consistent with rates followed by other senior Canadian governments. Historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets on the Province's books.

Impact of valuation allowance

The current AG's view challenges previous interpretations of the Provincial Controller and former Auditor Generals regarding the interpretation and application of PS 3250 to those JDBPs where the government is a joint sponsor. The impact of the OAG's view is that no pension accounting surplus could ever be recognized in the Province's Public Accounts for JDBPs until the joint sponsor agrees to a change in the plan text for the Province to provide for unilateral authority to access surplus or reduce future contributions to enters into an agreement by year-end enabling the government to take a contribution holiday. Any ABA would therefore be fully provided for through a valuation allowance, impacting each ~~year's statement~~year's statement of operations by the amount by which the asset would otherwise increase in value. These results are counterintuitive with pension expense being higher in years in ~~which funding~~which funding requirements are higher and assets are therefore increasing or when greater investments returns are recorded. In contrast, under the AG's view, the Province's annual surplus/deficit would ~~reflect a~~reflect a gain (income) in years when there are less than expected investment returns. **NTD – statements to be supplement by the visual aid requested by the Minister]**

For information purposes, refer to Appendix D for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS. Of particular note is the impact in 2008 when the deficit would have be lower by $3 billion in a year when pension asset values fell significantly because of the financial crisis.

Comparability of Ontario accounting for JDBPs to other Provinces

For your information, included in Appendix C is the legal opinion prepared by lawyers, Koskie Minsky, comparing access to the pension surplus of OTPP relative to JDBPs in British Columbia. The Province of British Columbia does not report a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the

Commented [NP22]: Suggest moving some of this discussion earlier in the document – reference to Appendix G above identifies OTPP discount rate as an outlier.

LD response – do the results corroborate the discount rates or exceed the discount rates?

Sorry- forgot to include the attachment. Will include it with the next response for your review and consideration of relevance as a reference in the doc.

Commented [NP23]: Consider referencing the appendix here and specific mention of the 2008 result which would have lowered the deficit by $3B.

LD response – Appendix D is referenced in the following paragraph. Have added a sentence here to highlight 2008.

independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

Insert New Brunswick?

Any info on SK or QC? (seem to recall mention of these at some point as well)

Conclusion on measurement

As discussed, there is significant professional judgement and ~~estimation in~~estimation in determining how to measure the valuation allowance under Section PS 3250, including the determination of the minimum contributions required by the current plan arrangements. It is the Province's position that the attributes of the joint defined benefit plan arrangements for the OTPP entitle the Province to access to its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surplus through reduced contributions.

The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of those models to date no valuation allowance appears to be required and the OTPP pension assets should continue to be recorded on the books of the Province.

Commented [NP24]: Can this be clarified? This likely refers to the 33 years noted in the above table. Can we tie it in to clarify.

LD response – This is a summary of the above arguments. I'm not sure what estimates management actually applied in coming up with the support for the valuation allowance (33 years vs 11 years and all the underlying projections), so I'm not sure how best to tie this in.

Npp Management's decision should be documented in this position paper. CV to advise.

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Appendix A – Guidance in the PSA Handbook - FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210

Guidance in FINANCIAL STATEMENT CONCEPTS, Section PS 1000
.35 **Assets** are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.
.36 Assets have three essential characteristics:
(a) they embody future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows;
(b) the public sector entity can control the economic resource and access to the future economic benefits; and
(c) the transaction or event giving rise to the public sector entity's control has already occurred. [Former paragraph PS 1000.36 retained in Archived Pronouncements.]
.37 An item is not an asset of a government if it lacks one or more of the essential characteristics listed in the preceding paragraph. Thus, for example, an item does not qualify as an asset of a government if the item involves:
(a) no future economic benefit;
(b) future economic benefit, but the government cannot obtain it; or
(c) future economic benefit that the government may obtain, but the events or circumstances that give the government control of the benefit have not yet occurred.
(paragraph PS 1000.38 deleted) [Former paragraph PS 1000.38 retained in Archived Pronouncements.]
.39 **Financial assets** are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations.
.40 A financial asset is any asset that is:
(a) cash;
(b) a realizable asset that is convertible to cash;
(c) a contractual right to receive cash or another financial asset from another party;
(d) a contractual right to exchange financial instruments with another party under conditions that are potentially favourable to the government;
(e) an equity instrument of another entity;
(f) an investment in a government business enterprise or government business partnership;
(g) a financial claim on an outside organization or individual; or
(h) an inventory or item for sale that meets the criteria in FINANCIAL STATEMENT PRESENTATION, paragraph PS 1201.055. [Former paragraph PS 1000.40 retained in Archived Pronouncements.]
.41 Non-financial assets include tangible capital assets, and other assets such as prepaid expenses and

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inventories of supplies.

.42 **Non-financial assets** are acquired, constructed or developed assets that do not normally provide resources to discharge existing liabilities, but instead:

(a) are normally employed to deliver government services;

(b) may be consumed in the normal course of operations; and

(c) are not for sale in the normal course of operations.

RECOGNITION

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

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

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

.55 The recognition criteria are as follows:

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

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

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

.57 Purchased natural resources and Crown lands are recognized in government financial statements. However, when natural resources and Crown lands have been inherited by the government in right of the Crown and have not been purchased, they are not given accounting recognition as assets in

government financial statements. These items are not recognized as assets because the costs, benefits and economic value of such items cannot be reasonably and verifiably quantified using existing methods. Similarly, art and historic treasures are also not recognized as assets.

.58 In the absence of appropriate public sector recognition and measurement criteria for intangibles, all intangibles, including those that have been purchased, developed, constructed or inherited in right of the Crown, are not recognized as assets in government financial statements. The intangible often called "human capital" that embodies the talent or intellectual capital of government employees is not recognized as an asset under existing accounting principles.

.59 Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting. The accrual basis of accounting recognizes the effect of transactions and events in the period in which the transactions and events occur, regardless of whether there has been a receipt or payment of cash or its equivalent. Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied. Accrual accounting recognizes an asset until the future economic benefit underlying the asset is partly or wholly used or lost.

MEASUREMENT

.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

.61 Present value is the discounted amount of future cash flows expected to be received from an asset or required to settle a liability. Present value is not a basis of measurement, but a valuation technique that may be used within historical cost-based or current-value models. This technique is used in the government reporting model, for example, to estimate the cost of retirement benefits, when determining the estimated total expenditure for closure and post-closure care of a solid waste landfill site, and when determining the "grant portion" of concessionary loans and portfolio investments.

.62 Government financial statements are prepared on the basis that recognized economic resources used up are measured in financial terms with no adjustments made for the effect of a change in the general purchasing power of the currency during the period. Although a government's performance in the management of its service potential 2 is generally a focus more appropriate to the nature and objectives of government, it cannot entirely be measured in financial terms.

2. Service potential embodies both the quality of service provided and the efficiency with which it is provided.

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.63 Financial statements are prepared on the assumption that the government is a going concern, meaning it will continue in operation, and will be able to realize assets and discharge liabilities and meet its statutory obligations in the normal course of operations for the foreseeable future.

Guidance in ASSETS, Section PS 3210

Economic resources

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

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

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

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

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

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

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

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

.09 Economic resources can be:

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

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

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

Future economic benefits

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

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

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

public sector resources generate cash inflows because they have user fees associated with them.

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

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

Control

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

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

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

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

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

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

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

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

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

.22 Control of an economic resource and of access to the future economic benefits are essential characteristics of an asset, whereas possession or ownership is not. For example, a public sector entity may control the economic resource and access to the future economic benefits through a capital lease arrangement yet not own the economic resource.

.23 A public sector entity's ability to regulate an economic resource does not, in and of itself, constitute control of an asset. A public sector entity may establish the regulatory environment in an

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industry or sector within which organizations operate and impose conditions or sanctions on their operations. For example, a pollution control authority may have the ability to close down the operations of entities that are not complying with environmental regulations. However, this power does not constitute control because the pollution control authority's interest extends only to the regulatory use of the economic resources and does not include the ability to control access to the future economic benefits.

.24 A public sector entity may act as trustee when it administers trusts on behalf of the beneficiaries specified in the agreement or statute. As trustee, the public sector entity merely administers the assets, following the terms and conditions set out in the agreement. It does not control the asset because it does not have access to the future economic benefits. Those benefits flow to the beneficiaries.

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Appendix B - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the	Consistent in concept with the definition of a GP focusing on investments in the partnership and the

		non-government sponsor;	definition of a JDBP focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix C – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

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In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[10] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[10] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

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to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

We trust that these comments have been of assistance to you. Should you have any questions in regard to them, please do not hesitate to contact the undersigned.

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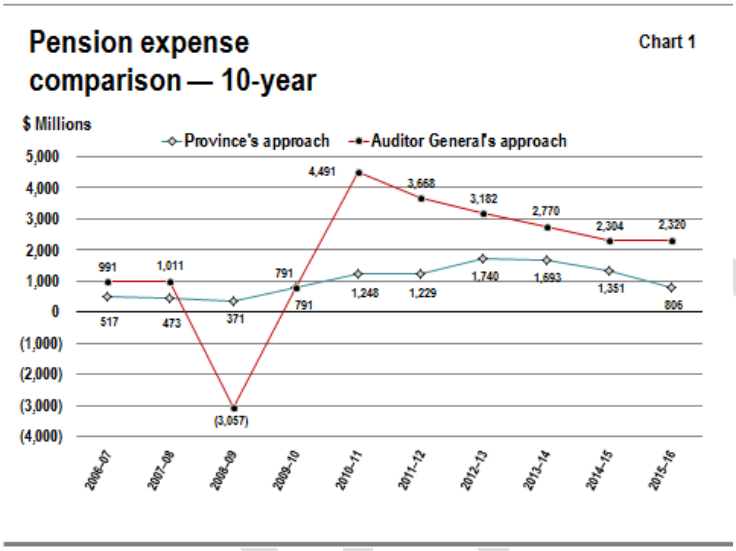
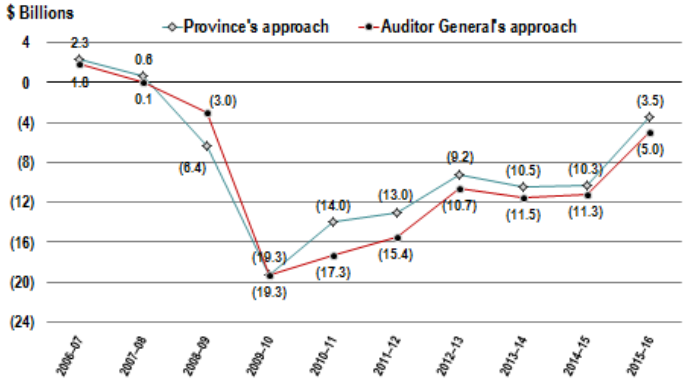
Appendix D - Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.



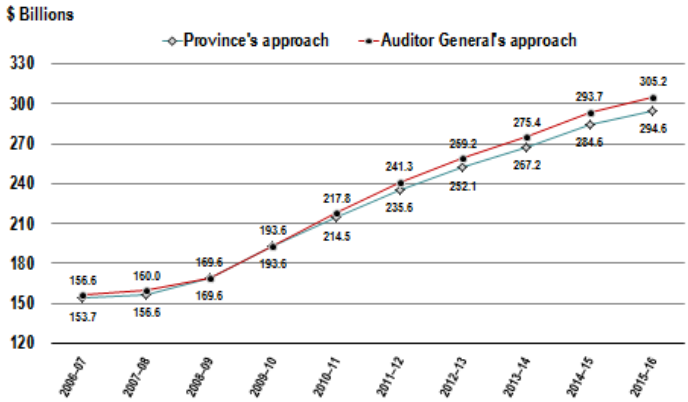
Surplus/(deficit) comparison — 10-year

Chart 2

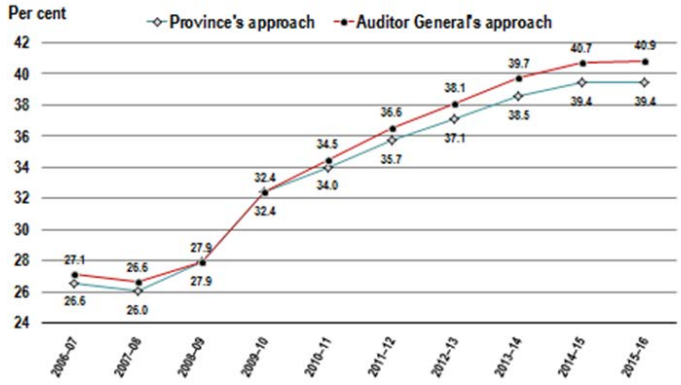


Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year Chart 4



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Appendix E – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. By contrast, section 19 of the Partners Agreement sets out the ~~responsibilities of~~responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ~~ongoing surpluses~~ongoing ~~either~~surpluses either to ~~improve benefits~~improve benefits or ~~reduce contributions~~reduce contributions. Only the Sponsors to the OTPP have the authority to utilize ongoing surpluses. The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners'

Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

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

Funding Management Policy (FMP)

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The FMP is an appendix to the Partners' Agreement that speaks to how the Plan should be funded and how surpluses should be utilized by both parties. The protocol for the use of a surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP.
The FMP sets out a complex series of considerations surrounding funding management and the use of any excess of assets over liabilities. The FMP sets out a number of "funding zones", depending on the level of funding in the Plan. The following three are most relevant to addressing surpluses:
i) Restoration zone (Article 3 of the FMP) allows for a surplus to be utilized to "restore" foregone indexation and then to either increase benefits to the "run-rate benefit" level (i.e., the long-term target level) or to lower contributions (or a combination of these two options) (Section 3.06(e)).
ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).
iii) Permanent improvement zone is where the Plan is essentially fully funded and has the funding security desired to support permanent changes. Article V (Permanent Improvements) of the FMP provides for permanent actions that can be taken when Plan assets exceed current liabilities by more than 10% of current liabilities. In this regard Section 5.05 provides for actions that can be taken in respect of the amount that assets exceed current liabilities. Such actions can include changes to current benefits, current contributions, or both.

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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Appendix F – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix G - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	5.95%	LT return on plan assets
Alberta				
Teachers' Post-1992 Pension Plan	7.00%	LT return on plan assets	7.25%	LT return on plan assets
Universities Academic Pension Plan	6.10%	LT return on plan assets	6.25%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)				
Local Authorities Pension Plan	5.80%	LT return on plan assets	5.80%	LT return on plan assets
Public Service Pension Plan	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Management Employees Pension Plan	6.40%	LT return on plan assets	6.40%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.75%	LT return on plan assets	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Special Forces Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan				
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.80%	LT return on plan assets	6.80%	LT return on plan assets
British Columbia				
Public Service Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec				
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	6.40%	LT return on plan assets less inflation
Newfoundland				
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets
Nova Scotia				
Nova Scotia Public Service Superannuation Plan (PSSP)	6.75%	LT return on plan assets	6.35%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	6.40%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba				
Civil Service Superannuation Plan	6.00%	LT return on plan assets	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.50%	LT return on plan assets	6.25%	LT return on plan assets

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			special payments	
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		

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).

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Appendix H – Summary of different valuation methodologies for pension valuations

The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits and pension obligations.	Measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered.
Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market -related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate.	In measuring a pension obligation amount, the defined benefit obligation amount determined by the	Not specified. However two methods are specifically acknowledged – a)

	For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.[11] The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

[11] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

TPP rates of return (performance vs discount rates).pdf

Ontario Teacher's Pension Plan
Rate Comparison

	OTPP Annual Performance	OTPP Filed Discount Rate *	Province Economic Assumpition for Nominal Return
2005	17.2%	6.48%	7.00%
2006	13.2%		7.00%
2007	4.5%		6.75%
2008	-18.0%	5.65%	6.75%
2009	13.0%	5.00%	6.75%
2010	14.3%		6.75%
2011	11.2%	5.40%	6.75%
2012	13.0%	5.30%	6.75%
2013	10.9%		6.75%
2014	11.8%	4.95%	6.75%
2015	13.0%	4.85%	6.50%
2016	n/a	n/a	6.25%

* The plan does not file a valuation annually. Under the Pension Benefits Act, plans must file at least every three years

Ontario Teacher's Pension Plan
Plan Perfomrance

Historic Returns	
2015	13.0%
2014	11.8%
4 - Year	12.2%
10- year	8.2%
Inception	10.3%

OTPP Board Projected Annual Real Return for period 2016-2046	4.50%

FW_ New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 08:29:35
Attachment 1: image001.png
Attachment 2: calculation_EFB_estimate_Sept_23_2016.xlsx
Attachment 3: Valuation_allowance_projection.xlsx

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-23-16 3:13 PM
To: Petsche, Nadine (TBS)
Cc: allan.shapira@aonhewitt.com; Killoch, Alex (MOF); Pomykacz, Rob (MOF); Colley, Matthew (CA - Toronto)
Subject: RE: New Model Output

Here are the 2 files

One for projection of plan situation

One for the expected future benefit and asset ceiling test

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Envoyé : 23 septembre 2016 15:10
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : New Model Output
Importance : Haute

Martin,

We are on a call with Matt and he is describing your most recent model run for the OTPP. Can you please share that with Allan Shapira and cc. Alex Killoch and Rob Pomykacz as soon as possible.

Thanks.

Nadine

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calculation_EFB_estimate_Sept_23_2016.pdf

	Plan	OTPP	(in $B)
a)	Value of asset - market value used		85.7
b)	Value of accounting obligation		58.2
c)	Surplus (deficit)		27.5
d)	Unamortized (gains) losses - market value used		-16.2
e)	Adjustment for March 31, 2016		-0.9
f)	Asset (liability) position		10.4
g)	Specific Government adjustment		-0.3
h)	Final Asset (liability) position on balance sheet		10.1
i)	Adjusted benefit asset		10.1
j)	Expected future benefit		22.3
k)	- Perpetuity of employer service cost		44.6
l)	- Minimum funding requirement		22.3
m)	- Surplus withdrawal		0.0
	TEST : Valuation allowance = max (0 ; i - j)		0.0

Expected Future Benefit Calculations

n)	Total plan service accrual accounting	2.9
o)	Employer service accrual share	50%
p)	Expected return on asset - accounting assumption	6.25%
q)	Salary increase - accounting assumption	3.00%
r)	Perpetuity of Employer service cost - accounting	44.6
s)	Minimum employer funding requirement as at March 31, 2016	22.3
t)	Expected Future Benefit	22.3

Reduction in Gov contr based on projection	**Year**	**Estimated Contributions[1]**	**Contribution required considering use of 50% of the surplus in excess of ITA excess surplus threshold**	**Present value of each contribution required**
0.0%	2016[2]	1.3	1.3	1.2
0.0%	2017	1.7	1.7	1.6
0.0%	2018	1.8	1.8	1.6
0.0%	2019	1.8	1.8	1.5
0.0%	2020	1.9	1.9	1.5
0.0%	2021	2.0	2.0	1.4
0.0%	2022	2.0	2.0	1.4
0.0%	2023	2.1	2.1	1.3
0.0%	2024	2.1	2.1	1.3
-2.5%	2025	2.2	2.1	1.2
-62.5%	2026	2.3	0.8	0.5
-65.4%	2027	2.3	0.8	0.4
-66.7%	2028	2.4	0.8	0.4
-67.7%	2029	2.5	0.8	0.4
-68.6%	2030	2.5	0.8	0.3
-69.5%	2031	2.6	0.8	0.3
-70.4%	2032	2.7	0.8	0.3
-71.2%	2033	2.8	0.8	0.3
-72.1%	2034	2.9	0.8	0.3

-72.9%	2035	3.0	0.8	0.2
-73.6%	2036	3.0	0.8	0.2
-74.4%	2037	3.1	0.8	0.2
-75.1%	2038	3.2	0.8	0.2
-75.8%	2039	3.3	0.8	0.2
-76.5%	2040	3.4	0.8	0.2
-77.2%	2041	3.5	0.8	0.2
-77.8%	2042	3.6	0.8	0.2
-78.4%	2043	3.7	0.8	0.2
-79.0%	2044	3.9	0.8	0.1
-79.5%	2045	4.0	0.8	0.1
-80.0%	2046	4.1	0.8	0.1
-80.5%	2047	4.2	0.8	0.1
-80.9%	2048	4.3	0.8	0.1
-81.3%	2049	4.5	0.8	0.1

Information

From Excel File
From Excel File
a - b
From Excel File
From Excel File
c + d + e
From Excel File
f + g

h - max (0 ; d) as per PS3250.053

Minimum EFB basis calculation illustrated (k - l + m)
r)
s), assuming contribution based on use of 50% of the excess surplus as per the Income Tax Act
As per the plan funding policy, the employer may have some access to surplus withdrawal. For simplicity, we have used 0 in the test.

No valuation allowance required, no adjustment to the balance sheet asset position, PS3250.050 and PS3250.054

From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation
From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation
From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation
From AON Memorandum (August 2, 2016) and OTPP Jan 26, 2016 documentation

*n * o / (p - q), present value of all future service cost to the employer (the 50% share)*

Sum of the present value of future required contributions (table below), using the funding report, projections and assuming the Government uses 50% of the surplus above Income Tax Act excess surplus threshold for contribution holiday and the employees use the other 50%

r - s, Perpetuity of employer service cost minus the minimum funding requirement as at March 31, 2016

	% assumpt	$B return
Accounting return on asset	*6.25%*	*5.4*
Funding return on asset	*4.85%*	*4.2*
Excess return each year using best estimate		*1.2*

[1] Estimated contributions from funding report (p.16), increased based on salary increase accounting assumption
[2] Remaining contributions used as at March 31,2016 (9 months for 2016)

Valuation_allowance_projection.pdf

accounting best estimate
funding report page 29
accounting best estimate
accounting best estimate
based on recent experience average (data input)

funding report page 9 for service rendered and 100% CPI
data input sheet
data input sheet

data input sheet
= (gg) assuming employees use same % of the ITA excess surplus
data input sheet
= (gg)
data input sheet
looking at the PV of future service / PV future contribution (funding report page 9)
data input sheet

= (f) x (b) + (l) x (b) x 50% + (k) x (b) x 50%
= (g) x (c) + (m) x (c) x 50% + (k) x (c) x 50%
= (h) x (a) + (i -1) x (a) x 50% + (j - 1) x (a) x 50% + (i -2) x (a) x 50% + (j - 2) x (a) x 50% + (k) x (a) x 50%

= (f) + (l) + (k) + (n)
= (g) + (m) + (k) + (o)
= (h) + (i -1) + (j - 1) + (i -2) + (j - 2) + (k) + (p)
= (s) - (ee)

= (s) - (q)
= (s) - (r)
= (t) - (q)

= (s) / (q)
= (s) / (r)
= (t) / (q)

Market-related value calculation
expected return for the year at 4.85% = (p) / (a) * (b)
actual return for the year = (p)
gain (loss) on asset return = (bb) - (aa)
spread over 3 years = (cc) / 3
3-year adjustment to get market related value = (dd) + (dd) previous year

Going-concern surplus in excess of 125% from the Income Tax Act = (t) - 125% x (q)
Reduction required in Government contribution assuming uses 50% of excess surplus = min (50% x (ff) ; (j -1) form
Asuming employees get the other 50% of excess surplus through cont reduction

% reduction in the Government contribution

		Calendar year	2015	2016	2017
	a	Return on plan asset	6.25%	6.25%	6.25%
	b	Interest rate on funding obligation	4.85%	4.85%	4.85%
	c	Interest rate on accounting obligation	6.25%	6.25%	6.25%
	d	Increase in salary (used for cont)	3.00%	3.00%	3.00%
	e	Increase in benefit	4.00%	4.00%	4.00%
		Total Plan			
		Beginning of calendar year			
	f	Funding obligation - 100% CPI	142,569	148,197	154,003
	g	Accounting obligation - 100% CPI	113,801	116,367	120,785
	h	Asset fair value	154,476	171,420	179,701
	i - 1	Employee contributions	1,615	1,663	1,713
	i - 2	Employee reduction in cont			
	j - 1	Government contributions	1,684	1,735	1,787
	j - 2	Government reduction in contribution			
	k	Benefit payments	(5,536)	(5,757)	(5,987)
129.7%	l	Funding service cost	4,280	4,408	4,540
	m	Accounting service cost	2,902	2,989	3,079
	n	Funding obligation interest	6,884	7,155	7,434
	o	Accounting obligation interest		7,186	7,458
	p	Asset return for the year	19,181	10,640	11,154
			12.4%		
		End of year			
	q	Funding obligation - 100% CPI	148,197	154,003	159,990
	r	Accounting obligation - 100% CPI	116,367	120,785	125,335
	s	Asset fair value	171,420	179,701	188,368
	t	Market related value			186,741
		Surplus (Deficit) in $M			
	u	Going concern (using fair value)	23,223	25,698	28,378
	v	Accounting	55,053	58,916	63,033
	w	Going concern (using market related)			26,751
		Ratio in %			
	x	Going concern (using fair value)	115.7%	116.7%	117.7%
	y	Accounting	147.3%	148.8%	150.3%
	z	Going concern (using market related)			116.7%
	aa			8,257	8,656
	bb			10,640	11,154
	cc			2,383	2,498
	dd			794	833
	ee				1,627

	ff	0
next year)	gg	0
	hh	0.0%

2018	2019	2020	2021	2022	2023	2024	2025
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
159,990	166,162	172,522	179,072	185,817	192,759	199,902	207,248
125,335	130,018	134,835	139,787	144,875	150,100	155,461	160,958
188,368	197,438	206,930	216,863	227,258	238,136	249,519	261,430
1,764	1,817	1,872	1,928	1,986	2,046	2,107	2,170
0	0	0	0	0	0	0	(56)
1,841	1,896	1,953	2,012	2,072	2,134	2,198	2,264
0	0	0	0	0	0	0	(56)
(6,226)	(6,475)	(6,734)	(7,003)	(7,283)	(7,574)	(7,877)	(8,192)
4,676	4,816	4,960	5,109	5,262	5,420	5,583	5,750
3,171	3,266	3,364	3,465	3,569	3,676	3,786	3,900
7,722	8,019	8,324	8,639	8,963	9,297	9,640	9,992
7,738	8,026	8,322	8,626	8,939	9,259	9,588	9,926
11,691	12,254	12,842	13,458	14,103	14,777	15,483	16,218
166,162	172,522	179,072	185,817	192,759	199,902	207,248	214,798
130,018	134,835	139,787	144,875	150,100	155,461	160,958	166,592
197,438	206,930	216,863	227,258	238,136	249,519	261,430	273,779
195,732	205,142	214,989	225,294	236,078	247,363	259,171	271,412
31,276	34,408	37,791	41,441	45,377	49,617	54,182	58,981
67,420	72,095	77,076	82,383	88,036	94,058	100,472	107,187
29,570	32,620	35,917	39,477	43,319	47,461	51,923	56,614
118.8%	119.9%	121.1%	122.3%	123.5%	124.8%	126.1%	127.5%
151.9%	153.5%	155.1%	156.9%	158.7%	160.5%	162.4%	164.3%
117.8%	118.9%	120.1%	121.2%	122.5%	123.7%	125.1%	126.4%
9,072	9,509	9,965	10,443	10,944	11,467	12,015	12,585
11,691	12,254	12,842	13,458	14,103	14,777	15,483	16,218
2,619	2,745	2,877	3,015	3,159	3,310	3,468	3,633
873	915	959	1,005	1,053	1,103	1,156	1,211
1,706	1,788	1,874	1,964	2,058	2,156	2,259	2,367

0	0	0	0	0	0	111	2,915
0	0	0	0	0	0	56	1,458
0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	-2.5%

2026	2027	2028	2029	2030	2031	2032	2033
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
214,798	222,556	230,523	238,701	247,092	255,696	264,513	273,544
166,592	172,360	178,262	184,296	190,458	196,746	203,156	209,683
273,779	283,808	294,021	304,489	315,222	326,231	337,513	349,071
2,235	2,302	2,371	2,442	2,515	2,590	2,668	2,748
(1,458)	(1,570)	(1,650)	(1,726)	(1,801)	(1,879)	(1,960)	(2,043)
2,332	2,402	2,474	2,548	2,624	2,703	2,784	2,868
(1,458)	(1,570)	(1,650)	(1,726)	(1,801)	(1,879)	(1,960)	(2,043)
(8,520)	(8,861)	(9,215)	(9,584)	(9,967)	(10,366)	(10,781)	(11,212)
5,923	6,101	6,284	6,473	6,667	6,867	7,073	7,285
4,017	4,138	4,262	4,390	4,522	4,658	4,798	4,942
10,355	10,727	11,109	11,502	11,904	12,316	12,739	13,172
10,271	10,625	10,987	11,356	11,733	12,118	12,510	12,909
16,897	17,510	18,137	18,779	19,438	20,113	20,806	21,514
222,556	230,523	238,701	247,092	255,696	264,513	273,544	282,789
172,360	178,262	184,296	190,458	196,746	203,156	209,683	216,322
283,808	294,021	304,489	315,222	326,231	337,513	349,071	360,904
281,335	291,452	301,828	312,466	323,378	334,560	346,015	357,744
61,252	63,498	65,788	68,130	70,535	73,000	75,527	78,115
111,448	115,759	120,193	124,764	129,485	134,357	139,388	144,582
58,779	60,929	63,127	65,374	67,682	70,047	72,471	74,955
127.5%	127.5%	127.6%	127.6%	127.6%	127.6%	127.6%	127.6%
164.7%	164.9%	165.2%	165.5%	165.8%	166.1%	166.5%	166.8%
126.4%	126.4%	126.4%	126.5%	126.5%	126.5%	126.5%	126.5%
13,112	13,588	14,074	14,573	15,084	15,608	16,145	16,695
16,897	17,510	18,137	18,779	19,438	20,113	20,806	21,514
3,785	3,922	4,063	4,206	4,354	4,505	4,661	4,819
1,262	1,307	1,354	1,402	1,451	1,502	1,554	1,606
2,473	2,569	2,661	2,756	2,853	2,953	3,056	3,160

3,140	3,299	3,452	3,601	3,758	3,919	4,085	4,258
1,570	1,650	1,726	1,801	1,879	1,960	2,043	2,129
-62.5%	-65.4%	-66.7%	-67.7%	-68.6%	-69.5%	-70.4%	-71.2%

2034	2035	2036	2037	2038	2039	2040	2041
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
282,789	292,247	301,917	311,797	321,885	332,176	342,666	353,352
216,322	223,067	229,911	236,844	243,858	250,941	258,081	265,265
360,904	373,010	385,389	398,038	410,955	424,135	437,572	451,260
2,830	2,915	3,002	3,092	3,185	3,281	3,379	3,480
(2,129)	(2,218)	(2,308)	(2,402)	(2,498)	(2,598)	(2,700)	(2,805)
2,954	3,043	3,134	3,228	3,325	3,425	3,528	3,634
(2,129)	(2,218)	(2,308)	(2,402)	(2,498)	(2,598)	(2,700)	(2,805)
(11,660)	(12,126)	(12,611)	(13,115)	(13,640)	(14,186)	(14,753)	(15,343)
7,504	7,729	7,961	8,200	8,446	8,699	8,960	9,229
5,090	5,243	5,400	5,562	5,729	5,901	6,078	6,260
13,614	14,067	14,530	15,003	15,485	15,977	16,479	16,989
13,315	13,727	14,144	14,567	14,994	15,425	15,859	16,295
22,240	22,982	23,740	24,515	25,306	26,112	26,934	27,771
292,247	301,917	311,797	321,885	332,176	342,666	353,352	364,227
223,067	229,911	236,844	243,858	250,941	258,081	265,265	272,477
373,010	385,389	398,038	410,955	424,135	437,572	451,260	465,193
369,743	382,012	394,549	407,352	420,415	433,732	447,299	461,108
80,763	83,472	86,241	89,070	91,959	94,906	97,908	100,966
149,943	155,478	161,194	167,097	173,194	179,491	185,995	192,716
77,496	80,095	82,752	85,467	88,239	91,066	93,947	96,881
127.6%	127.6%	127.7%	127.7%	127.7%	127.7%	127.7%	127.7%
167.2%	167.6%	168.1%	168.5%	169.0%	169.5%	170.1%	170.7%
126.5%	126.5%	126.5%	126.6%	126.6%	126.6%	126.6%	126.6%
17,258	17,834	18,422	19,024	19,637	20,263	20,901	21,550
22,240	22,982	23,740	24,515	25,306	26,112	26,934	27,771
4,982	5,148	5,318	5,491	5,669	5,849	6,033	6,221
1,661	1,716	1,773	1,830	1,890	1,950	2,011	2,074
3,267	3,377	3,489	3,603	3,720	3,840	3,961	4,085

4,435	4,616	4,803	4,996	5,195	5,400	5,609	5,825
2,218	2,308	2,402	2,498	2,598	2,700	2,805	2,913
-72.1%	-72.9%	-73.6%	-74.4%	-75.1%	-75.8%	-76.5%	-77.2%

2042	2043	2044	2045	2046	2047	2048	2049
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
364,227	375,285	386,517	397,915	409,470	421,169	432,999	444,946
272,477	279,701	286,917	294,105	301,242	308,302	315,258	322,078
465,193	479,361	493,757	508,367	523,179	538,181	553,354	568,679
3,584	3,692	3,803	3,917	4,035	4,156	4,281	4,409
(2,913)	(3,022)	(3,136)	(3,253)	(3,371)	(3,493)	(3,618)	(3,744)
3,743	3,855	3,971	4,090	4,213	4,339	4,469	4,603
(2,913)	(3,022)	(3,136)	(3,253)	(3,371)	(3,493)	(3,618)	(3,744)
(15,957)	(16,595)	(17,259)	(17,949)	(18,667)	(19,414)	(20,191)	(20,999)
9,506	9,791	10,085	10,388	10,700	11,021	11,352	11,693
6,448	6,641	6,840	7,045	7,256	7,474	7,698	7,929
17,509	18,036	18,572	19,116	19,666	20,223	20,786	21,354
16,733	17,170	17,607	18,041	18,471	18,896	19,313	19,721
28,623	29,488	30,367	31,259	32,162	33,077	34,001	34,934
375,285	386,517	397,915	409,470	421,169	432,999	444,946	456,994
279,701	286,917	294,105	301,242	308,302	315,258	322,078	328,729
479,361	493,757	508,367	523,179	538,181	553,354	568,679	584,138
475,150	489,418	503,898	518,578	533,446	548,483	563,670	578,991
104,076	107,240	110,452	113,709	117,012	120,355	123,733	127,144
199,660	206,840	214,262	221,937	229,879	238,096	246,601	255,409
99,865	102,901	105,983	109,108	112,277	115,484	118,724	121,997
127.7%	127.7%	127.8%	127.8%	127.8%	127.8%	127.8%	127.8%
171.4%	172.1%	172.9%	173.7%	174.6%	175.5%	176.6%	177.7%
126.6%	126.6%	126.6%	126.6%	126.7%	126.7%	126.7%	126.7%
22,211	22,883	23,565	24,257	24,958	25,668	26,385	27,109
28,623	29,488	30,367	31,259	32,162	33,077	34,001	34,934
6,412	6,605	6,802	7,002	7,204	7,409	7,616	7,825
2,137	2,202	2,267	2,334	2,401	2,470	2,539	2,608
4,211	4,339	4,469	4,601	4,735	4,871	5,009	5,147

6,044	6,272	6,505	6,741	6,985	7,235	7,488	7,749
3,022	3,136	3,253	3,371	3,493	3,618	3,744	3,875
-77.8%	-78.4%	-79.0%	-79.5%	-80.0%	-80.5%	-80.9%	-81.3%

2050	2051	2052	2053	2054	2055	2056	2057
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
456,994	469,126	481,321	493,557	505,811	518,057	530,267	542,410
328,729	335,175	341,376	347,287	352,861	358,046	362,785	367,017
584,138	599,706	615,361	631,074	646,814	662,548	678,242	693,856
4,541	4,677	4,817	4,962	5,111	5,264	5,422	5,585
(3,875)	(4,006)	(4,141)	(4,280)	(4,420)	(4,562)	(4,706)	(4,853)
4,741	4,883	5,029	5,180	5,335	5,495	5,660	5,830
(3,875)	(4,006)	(4,141)	(4,280)	(4,420)	(4,562)	(4,706)	(4,853)
(21,839)	(22,713)	(23,622)	(24,567)	(25,550)	(26,572)	(27,635)	(28,740)
12,044	12,405	12,777	13,160	13,555	13,962	14,381	14,812
8,167	8,412	8,664	8,924	9,192	9,468	9,752	10,045
21,927	22,503	23,081	23,661	24,241	24,820	25,397	25,969
20,118	20,502	20,869	21,217	21,543	21,843	22,115	22,354
35,874	36,820	37,771	38,724	39,678	40,630	41,579	42,521
469,126	481,321	493,557	505,811	518,057	530,267	542,410	554,451
335,175	341,376	347,287	352,861	358,046	362,785	367,017	370,676
599,706	615,361	631,074	646,814	662,548	678,242	693,856	709,347
594,419	609,933	625,505	641,103	656,694	672,245	687,717	703,067
130,580	134,040	137,517	141,003	144,491	147,975	151,446	154,896
264,531	273,985	283,787	293,953	304,502	315,457	326,839	338,671
125,293	128,612	131,948	135,292	138,637	141,978	145,307	148,616
127.8%	127.8%	127.9%	127.9%	127.9%	127.9%	127.9%	127.9%
178.9%	180.3%	181.7%	183.3%	185.0%	187.0%	189.1%	191.4%
126.7%	126.7%	126.7%	126.7%	126.8%	126.8%	126.8%	126.8%
27,838	28,572	29,310	30,050	30,790	31,529	32,265	32,996
35,874	36,820	37,771	38,724	39,678	40,630	41,579	42,521
8,036	8,248	8,461	8,674	8,888	9,101	9,314	9,525
2,679	2,749	2,820	2,891	2,963	3,034	3,105	3,175
5,287	5,428	5,569	5,711	5,854	5,997	6,139	6,280

8,012	8,282	8,559	8,840	9,123	9,412	9,705	10,004
4,006	4,141	4,280	4,420	4,562	4,706	4,853	5,002
-81.7%	-82.0%	-82.3%	-82.6%	-82.8%	-83.0%	-83.1%	-83.2%

2058	2059	2060	2061	2062	2063	2064	2065
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%	4.85%
6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%	6.25%
3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
554,451	566,353	578,076	589,577	600,809	611,721	622,256	632,356
370,676	373,689	375,976	377,454	378,030	377,605	376,071	373,312
709,347	724,666	739,763	754,582	769,063	783,144	796,752	809,811
5,753	5,926	6,104	6,287	6,476	6,670	6,870	7,076
(5,002)	(5,153)	(5,305)	(5,459)	(5,612)	(5,767)	(5,923)	(6,078)
6,005	6,185	6,371	6,562	6,759	6,962	7,171	7,386
(5,002)	(5,153)	(5,305)	(5,459)	(5,612)	(5,767)	(5,923)	(6,078)
(29,890)	(31,086)	(32,329)	(33,622)	(34,967)	(36,366)	(37,821)	(39,334)
15,256	15,714	16,185	16,671	17,171	17,686	18,217	18,764
10,346	10,656	10,976	11,305	11,644	11,993	12,353	12,724
26,536	27,095	27,645	28,183	28,708	29,215	29,704	30,170
22,557	22,717	22,831	22,893	22,898	22,839	22,709	22,500
43,455	44,377	45,283	46,171	47,037	47,876	48,684	49,456
566,353	578,076	589,577	600,809	611,721	622,256	632,356	641,956
373,689	375,976	377,454	378,030	377,605	376,071	373,312	369,202
724,666	739,763	754,582	769,063	783,144	796,752	809,811	822,239
718,246	733,205	747,888	762,235	776,185	789,665	802,601	814,911
158,313	161,687	165,005	168,254	171,423	174,496	177,455	180,283
350,977	363,787	377,128	391,033	405,539	420,681	436,499	453,037
151,893	155,129	158,311	161,426	164,464	167,409	170,245	172,955
128.0%	128.0%	128.0%	128.0%	128.0%	128.0%	128.1%	128.1%
193.9%	196.8%	199.9%	203.4%	207.4%	211.9%	216.9%	222.7%
126.8%	126.8%	126.9%	126.9%	126.9%	126.9%	126.9%	126.9%
33,721	34,437	35,140	35,829	36,501	37,152	37,779	38,378
43,455	44,377	45,283	46,171	47,037	47,876	48,684	49,456
9,734	9,940	10,143	10,342	10,536	10,724	10,905	11,078
3,245	3,313	3,381	3,447	3,512	3,575	3,635	3,693
6,420	6,558	6,694	6,828	6,959	7,087	7,210	7,328

10,305	10,610	10,917	11,224	11,534	11,845	12,156	12,466
5,153	5,305	5,459	5,612	5,767	5,923	6,078	6,233
-83.3%	-83.3%	-83.3%	-83.2%	-83.0%	-82.8%	-82.6%	-82.3%

2066
6.25%
4.85%
6.25%
3.00%
4.00%
641,956
369,202
822,239
7,288
(6,233)
7,608
(6,233)
(40,907)
19,327
13,106
30,612
22,206
50,188
650,988
363,607
833,950
826,510
182,962
470,343
175,522
128.1%
229.4%
127.0%
38,946
50,188
11,242
3,747
7,440

12,775
6,388

-81.9%

FW_ New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 10:35:55
Attachment 1: image001.png

Share with Martin et. Al?

From: Allan Shapira [mailto:allan.shapira@aonhewitt.com]
Sent: September-24-16 10:15 AM
To: Veinot, Cindy (TBS)
Cc: Killoch, Alex (MOF); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Subject: Re: New Model Output

It would definitely be in the temporary zone and may even be in the permanent zone. I would have to take some time today to figure that out if that is important.

It seems like the AG is hung up on the fact that the government needs agreement of another party, the other joint sponsor to use surplus. That is the essence of a joint plan and it plays out in both increasing contributions when necessary and reducing then when there is an opportunity to do so. I should remind everyone that the temporary zone was introduced in response to the concerns of the member sponsor that with what they view as conservative funding the surplus would grow very large with only a permanent zone and they would not get access to it early enough. Clearly that reflects their desire to use the surplus and they can only do so if the government gets its 50% share.

Allan

Sent from my iPhone

On Sep 24, 2016, at 9:01 AM, Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca> wrote:

> Thanks everyone for looking at this so quickly.

One question on #3 – does the math work such that the plan would be in permanent zone when it is estimated to hit the ITA limit? In other words, based on one of the scenarios provided by Martin Raymond, does this mean that based on continued expected returns, one model suggests that the plan would be in the permanent zone in 15 years?

From: Killoch, Alex (MOF)
Sent: September-24-16 8:57 AM
To: Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)
Subject: Re: New Model Output

I talked to Allan last night.

The answer to number 1 is that the rule applies to joint plans.

Number 2 is that the rule applies to the employer only. But under the terms of the plan it would be both parties that need to determine how to to reduce surplus.

There is no rule other than the FMP for dealing with surplus. And Raymond is correct that the plan would never get to the ITA maximum. The otf would never allow it to get through the temp and permanent zones, (and I doubt gov't would either)

Alex

From: Petsche, Nadine (TBS)

Sent: Saturday, September 24, 2016 8:35 AM

To: Killoch, Alex (MOF); Pomykacz, Rob (MOF)

Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)

Subject: RE: New Model Output

Alex/Rob,

Just wondering what the plan is w.r.t. the questions posed below? Thx. n

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-23-16 4:44 PM
To: Petsche, Nadine (TBS)
Cc: allan.shapira@aonhewitt.com; Killoch, Alex (MOF); Pomykacz, Rob (MOF); Colley, Matthew (CA - Toronto)
Subject: RE: New Model Output

After a discussion with Matthew, find enclosed the following questions that might be needed to review with the use of Income Tax Act excess surplus for contribution reduction.

1- Is the Income Tax Act excess surplus still applicable to a joint plan? I believe it does since the idea is to avoid excess use of pension plans as tax free deferral vehicles and therefore should apply to all types of employer provided pension plans

2- Is the Income Tax Act only requiring the employer to reduce contribution even in a joint plan ? if so, our estimate of using 50% of the excess surplus would move to 100%. However, we have used 50% of the excess surplus as a benefit to the employer knowing that under the plan, the sharing principle would lead to employees and employer reducing both their contributions to meet the requirement of the Income Tax Act

3- Finally, is there a plan provision (I did not see if one applies) that would force the employer to modify the plan benefits and therefore prevent of taking a contribution reduction that is otherwise applicable as per the Income Tax Act. I did not see one, and this is likely to be logic that the plan does not need one since the idea would generally be to deal with surplus through the Temporary and Permanent zones in the sharing of surplus and therefore not getting into the excess surplus position. However, for our illustration we assume that no surplus is used through the Temporary and Permanent zones, considering no agreement and therefore we end up dealing with the excess surplus situation.

Regards

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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<image001.png>

De : Raymond, Martin (CA - Montreal)
Envoyé : 23 septembre 2016 15:13

À : 'Petsche, Nadine (TBS)' <Nadine.Petsche@ontario.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : RE: New Model Output

Here are the 2 files

One for projection of plan situation

One for the expected future benefit and asset ceiling test

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Partner – Audit – Actuarial services

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De : Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Envoyé : 23 septembre 2016 15:10
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : New Model Output
Importance : Haute

Martin,

We are on a call with Matt and he is describing your most recent model run for the OTPP. Can you please share that with Allan Shapira and cc. Alex Killoch and Rob Pomykacz as soon as possible.

Thanks.

Nadine

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image001.pdf

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FW_ New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
CC: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 09:01:03
Attachment 1: image001.png

Good morning Martin. Sorry, I should have copied you on the message below. Nadine

From: Petsche, Nadine (TBS)
Sent: September-24-16 9:00 AM
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca); Danyluk, Kerry (CA - Toronto)
Cc: Veinot, Cindy (TBS)
Subject: FW: New Model Output

Matt/Kerry,

Please see answers to the Q's below. Sorry for the delay. There was confusion as to who was going to respond. N

From: Killoch, Alex (MOF)
Sent: September-24-16 8:57 AM
To: Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)
Subject: Re: New Model Output

I talked to Allan last night.

The answer to number 1 is that the rule applies to joint plans.

Number 2 is that the rule applies to the employer only. But under the terms of the plan it would be both parties that need to determine how to to reduce surplus.

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Alex

From: Petsche, Nadine (TBS)

Sent: Saturday, September 24, 2016 8:35 AM

To: Killoch, Alex (MOF); Pomykacz, Rob (MOF)

Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)

Subject: RE: New Model Output

Alex/Rob,

Just wondering what the plan is w.r.t. the questions posed below? Thx. n

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-23-16 4:44 PM
To: Petsche, Nadine (TBS)
Cc: allan.shapira@aonhewitt.com; Killoch, Alex (MOF); Pomykacz, Rob (MOF); Colley, Matthew (CA - Toronto)
Subject: RE: New Model Output

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needed to review with the use of Income Tax Act excess surplus for contribution reduction.

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Regards

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

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De : Raymond, Martin (CA - Montreal)
Envoyé : 23 septembre 2016 15:13
À : 'Petsche, Nadine (TBS)' <Nadine.Petsche@ontario.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : RE: New Model Output

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Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Envoyé : 23 septembre 2016 15:10
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : New Model Output
Importance : Haute

Martin,

We are on a call with Matt and he is describing your most recent model run for the OTPP. Can you please share that with Allan Shapira and cc. Alex Killoch and Rob Pomykacz as soon as possible.

Thanks.

Nadine

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FW_ New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
CC: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 09:01:03
Attachment 1: @

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Good morning Martin. Sorry, I should have copied you on the message below. Nadine

From: Petsche, Nadine (TBS)
Sent: September-24-16 9:00 AM
To: Colley, Matthew (CA - Toronto) (mcolley@deloi
Attachments:
image001.png (5 KB)
https://ctsbigdcapmvs05.cihs.ad.gov.on.ca/EnterpriseVault/ViewMessage.asp?VaultId=184971630C5FAB646A01170AFB6CF78EC1110000ctsbigdcapmvs01&SavesetId=201706288682009~201609241301030000~Z~D0FAAB65534826EB912567C1B863A0E1&AttachmentId=1image001.png

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To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 09:00:13
Attachment 1: image001.png

Matt/Kerry,

Please see answers to the Q's below. Sorry for the delay. There was confusion as to who was going to respond. N

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Sent: September-24-16 8:57 AM
To: Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)
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Sent: Saturday, September 24, 2016 8:35 AM

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Subject: RE: New Model Output

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Fax : 514-390-4104

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From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 08:29:42
Attachment 1: image001.png

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-23-16 4:44 PM
To: Petsche, Nadine (TBS)
Cc: allan.shapira@aonhewitt.com; Killoch, Alex (MOF); Pomykacz, Rob (MOF); Colley, Matthew (CA - Toronto)
Subject: RE: New Model Output

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Regards

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De : Raymond, Martin (CA - Montreal)
Envoyé : 23 septembre 2016 15:13
À : 'Petsche, Nadine (TBS)' <Nadine.Petsche@ontario.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
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FW_ New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 10:37:45
Attachment 1: image001.png

Fyi. Sorry, I forgot to cc you again. Need more coffee. N…

From: Petsche, Nadine (TBS)
Sent: September-24-16 10:36 AM
To: Danyluk, Kerry (CA - Toronto); Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)
Subject: FW: New Model Output

FYI. Nadine

From: Allan Shapira [mailto:allan.shapira@aonhewitt.com]
Sent: September-24-16 10:15 AM
To: Veinot, Cindy (TBS)
Cc: Killoch, Alex (MOF); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Subject: Re: New Model Output

It would definitely be in the temporary zone and may even be in the permanent zone. I would have to take some time today to figure that out if that is important.

It seems like the AG is hung up on the fact that the government needs agreement of another party, the other joint sponsor to use surplus. That is the essence of a joint plan and it plays out in both increasing contributions when necessary and reducing then when there is an opportunity to do so. I should remind everyone that the temporary zone was introduced in response to the concerns of the member sponsor that with what they view as conservative funding the surplus would grow very large with only a permanent zone and they would not get access to it early enough. Clearly that reflects their desire to use the surplus and they can only do so if the government gets its 50% share.

Allan

Sent from my iPhone

On Sep 24, 2016, at 9:01 AM, Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca> wrote:

Thanks everyone for looking at this so quickly.

One question on #3 – does the math work such that the plan would be in permanent zone when it is estimated to hit the ITA limit? In other words, based on one of the scenarios provided by Martin Raymond, does this mean that based on continued expected returns, one model suggests that the plan would be in the permanent zone in 15 years?

From: Killoch, Alex (MOF)
Sent: September-24-16 8:57 AM
To: Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)
Subject: Re: New Model Output

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Sent: Saturday, September 24, 2016 8:35 AM

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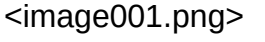

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To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: New Model Output
Date: Saturday, September 24, 2016 10:37:45
Attachment 1: image001.png

Fyi. Sorry, I forgot to cc you again. Need more coffee. N…

From: Petsche, Nadine (TBS)
Sent: September-24-16 10:36 AM
To: Danyluk, Kerry (CA - Toronto); Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)
Subject: FW: New Model Output

FYI. Nadine

From: Allan Shapira [mailto:allan.shapira@aonhewitt.com]
Sent: September-24-16 10:15 AM
To: Veinot, Cindy (TBS)
Cc: Killoch, Alex (MOF); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Subject: Re: New Model Output

It would definitely be in the temporary zone and may even be in the permanent zone. I would have to take some time today to figure that out if that is important.

It seems like the AG is hung up on the fact that the government needs agreement of another party, the other joint sponsor to use surplus. That is the essence of a joint plan and it plays out in both increasing contributions when necessary and reducing then when there is an opportunity to do so. I should remind everyone that the temporary zone was introduced in response to the concerns of the member sponsor that with what they view as conservative funding the surplus would grow very large with only a permanent zone and they would not get access to it early enough. Clearly that reflects their desire to use the surplus and they can only do so if the government gets its 50% share.

Allan

Sent from my iPhone

On Sep 24, 2016, at 9:01 AM, Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca> wrote:

Thanks everyone for looking at this so quickly.

One question on #3 – does the math work such that the plan would be in permanent zone when it is estimated to hit the ITA limit? In other words, based on one of the scenarios provided by Martin Raymond, does this mean that based on continued expected returns, one model suggests that the plan would be in the permanent zone in 15 years?

From: Killoch, Alex (MOF)
Sent: September-24-16 8:57 AM
To: Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)
Subject: Re: New Model Output

I talked to Allan last night.

The answer to number 1 is that the rule applies to joint plans.

Number 2 is that the rule applies to the employer only. But under the terms of the plan it would be both parties that need to determine how to to reduce surplus.

There is no rule other than the FMP for dealing with surplus. And Raymond is correct that the plan would never get to the ITA maximum. The otf would never allow it to get through the temp and permanent zones, (and I doubt gov't would either)

Alex

From: Petsche, Nadine (TBS)

Sent: Saturday, September 24, 2016 8:35 AM

To: Killoch, Alex (MOF); Pomykacz, Rob (MOF)

Cc: allan.shapira@aonhewitt.com; Veinot, Cindy (TBS)

Subject: RE: New Model Output

Alex/Rob,

Just wondering what the plan is w.r.t. the questions posed below? Thx. n

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-23-16 4:44 PM
To: Petsche, Nadine (TBS)
Cc: allan.shapira@aonhewitt.com; Killoch, Alex (MOF); Pomykacz, Rob (MOF); Colley, Matthew (CA - Toronto)
Subject: RE: New Model Output

After a discussion with Matthew, find enclosed the following questions that might be needed to review with the use of Income Tax Act excess surplus for contribution reduction.

1- Is the Income Tax Act excess surplus still applicable to a joint plan? I believe it

does since the idea is to avoid excess use of pension plans as tax free deferral vehicles and therefore should apply to all types of employer provided pension plans

2- Is the Income Tax Act only requiring the employer to reduce contribution even in a joint plan ? if so, our estimate of using 50% of the excess surplus would move to 100%. However, we have used 50% of the excess surplus as a benefit to the employer knowing that under the plan, the sharing principle would lead to employees and employer reducing both their contributions to meet the requirement of the Income Tax Act

3- Finally, is there a plan provision (I did not see if one applies) that would force the employer to modify the plan benefits and therefore prevent of taking a contribution reduction that is otherwise applicable as per the Income Tax Act. I did not see one, and this is likely to be logic that the plan does not need one since the idea would generally be to deal with surplus through the Temporary and Permanent zones in the sharing of surplus and therefore not getting into the excess surplus position. However, for our illustration we assume that no surplus is used through the Temporary and Permanent zones, considering no agreement and therefore we end up dealing with the excess surplus situation.

Regards

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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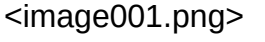

De : Raymond, Martin (CA - Montreal)
Envoyé : 23 septembre 2016 15:13
À : 'Petsche, Nadine (TBS)' <Nadine.Petsche@ontario.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : RE: New Model Output

Here are the 2 files

One for projection of plan situation

One for the expected future benefit and asset ceiling test

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Envoyé : 23 septembre 2016 15:10
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : allan.shapira@aonhewitt.com; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : New Model Output
Importance : Haute

Martin,

We are on a call with Matt and he is describing your most recent model run for the OTPP. Can you please share that with Allan Shapira and cc. Alex Killoch and Rob Pomykacz as soon as possible.

Thanks.

Nadine

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image001.pdf

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FW_ OPCD Support on Pension Work.rtf

From: Petsche, Nadine (TBS) []
To: pjesty@deloitte.ca [pjesty@deloitte.ca]
Subject: FW: OPCD Support on Pension Work
Date: Wednesday, October 26, 2016 10:01:40
Attachment 1: Picture (Device Independent Bitmap) 1.jpg

Hi Paula.

At the same time as I was sending my note, Pina was sending the attached to me. I'll plan to touch base with her regarding the pension work.

With regards to release of the accounting opinion, when I spoke with Matt he mentioned that the request was being reviewed internally. As the Panel is expected to be announced shortly, it would be good to know if we will be able to share the opinion.

Thanks in advance.

Nadine

From: Colavecchia, Pina (CA - Toronto) [mailto:pcolavecchia@deloitte.ca]
Sent: October 26, 2016 9:53 AM
To: Petsche, Nadine (TBS)
Subject: OPCD Support on Pension Work

Hi Nadine,

I hope that you are doing well. It has been a while since we have worked together!

Matt Colley has asked me to reach out to you regarding support on the pension work. He is on vacation this week.

Can we have a short call today to discuss the scope of this work and your expectations

on the deliverable from Deloitte?

I am available anytime today except from 10:30 to 11:45. Let me know if I should call your or if you want to contact me directly. My direct line is **416 601 5838**

Thanks,

Pina

--

Pina Colavecchia CPA, CA

Senior Manager | Public Sector

Deloitte LLP

400 Applewood Crescent, Suite 500, Vaughan, ON, L4K 0C3, Canada

D: +1 (416) 601 5838

pcolavecchia@deloitte.ca | deloitte.ca

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Picture (Device Independent Bitmap) 1.pdf

FW_ OTPP FMP questions.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; Lucy Durocher (CA - ASR) (lucy.durocher@pwc.com) [lucy.durocher@pwc.com]
Subject: FW: OTPP FMP questions
Date: Sunday, September 18, 2016 12:05:13
Attachment 1: image001.gif
Attachment 2: image002.png
Attachment 3: image003.png
Attachment 4: image004.png
Attachment 5: image005.png
Attachment 6: image006.png
Attachment 7: FMP history - updated September 29 by MC new format.pdf
Attachment 8: FMP Coles Notes.pdf
Attachment 9: OTPP JSPP Afreement final March 2013.pdf
Attachment 10: Report on Funding.pdf

Lucy,

Thought you might also benefit from these docs (some of which you may already have). Will send the history doc shortly as well. n

From: Barbara Zvan <Barbara_Zvan@otpp.com>

Sent: Saturday, September 17, 2016 2:16 PM

Subject: RE: OTPP FMP questions

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 viaspecials, 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
www.otpp.com

Ontario Teachers' Pension Plan
5650 Yonge Street, Toronto, Ontario M2M 4H5, Canada

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ONTARIO
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PENSION PLAN

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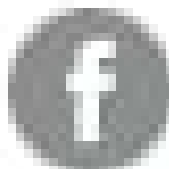

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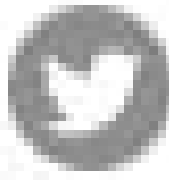

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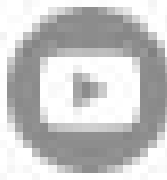

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FMP history - updated September 29 by MC new format.pdf

ONTARIO TEACHERS' PENSION PLAN

The Plan Sponsors'

Funding Management Policy

Structure and Historical Context

Strategy & Risk

HISTORICAL CONTEXT

OTPP is jointly sponsored by the Ontario government, through the Minister of Education, and the Ontario Teachers' Federation (OTF). The Sponsors are jointly-responsible for two key decisions: a) what pension benefits the Plan will provide, and b) the contribution rate needed to ensure the Plan's benefits are fully funded over the long term. In doing so, the Sponsors negotiate the use of surplus funds and, when there is a funding shortfall, both share responsibility for eliminating it.

In March 2003, the Sponsors adopted a Funding Management Policy (FMP) as a supplement to the Partners' Agreement, with the objective to provide a guidance framework for decision making when there is a funding surplus or shortfall. A key component in the creation of the FMP was the concept of 'funding zones', each defined by a range. The funding zones provide a point of reference for whether action is required by the Sponsors, and if so, guidance is provided on how to use any surplus funds or resolve any shortfall – specifically, answering the question of when is it prudent to increase or decrease benefits[1], raise or lower contribution rates, or simply conserve assets for an uncertain time. While the FMP outlines preferred mechanisms associated with its various funding zones, it is ultimately the Sponsors' responsibility to decide what actions to take.

The FMP has important implications from an investment perspective, as the decisions guided by the FMP impact our strategic asset allocation decisions through the Plan's ability to absorb risk. The OTPP Board cannot change benefits or contribution rates; however, they (along with Plan management) work closely with the Sponsors to ensure they have a strong and timely understanding of the financial position of the Plan and current economic and market realities via analytical expertise, and provide information and perspective as they deliberate on plan amendments[2].

The platform for ongoing dialogue between OTPP and the Sponsors is the Partners' Consultative Committee (established in 2008). Examples of important changes since 2003 were the inclusion of a maximum contribution rate in 2006 and the inclusion of Conditional Inflation Protection as an additional funding lever in 2008.

Before creation of the FMP, the Plan was considered "fully funded" if the ratio of assets to the cost of future pensions was 1:1, or 100%. That meant that if the Plan's funding status was below 100% when a valuation was filed, it would trigger an immediate contribution rate increase (by law) unless the Plan Sponsors decided to implement a reduction of future benefits. Conversely, when the funding status was above 100%, even by a small margin, there was opportunity to improve benefits on a permanent basis, even if the Plan's economic and market outlook did not support the added cost.

This practice had very practical pitfalls. The most obvious is that it provided false comfort that even a marginal surplus of assets over the cost of future benefits was enough cause to increase benefits. In the absence of a guidance plan, the opportunity to spend surplus was used. From 1998-2001, the Sponsors spent a total of $18.7 billion in surplus created in the late 1990s/early 2000s (~22% of the Jan 1, 2001 net liability) to eliminate special payments by the Province[3] and permanently improve pension benefits. However, the economic and funding conditions that drove the level of surpluses during this period were not sustainable, and because of how the funds were spent, what followed in the mid/late 2000s (and beyond) was a persistent and growing funding shortfall driven by pension benefits that were too expensive to be supported by our demographically maturing plan[4], in the midst of a historically challenging financial environment.

[1] The value of accrued pension benefits is protected under the Ontario Pension Benefits Act. Accordingly, the FMP contemplates changes to future benefits only.

[2] An important example of these deliberations was the introduction of Conditional Inflation Protection, which provided a systematic approach to reducing future benefits that could be restored in "good" times.

[3] To amortize the pre-1990 unfunded liability.

[4] For further detail into the demographic challenges faced by our mature plan, see *Plan Design Demographics and Investment Implications.*

CURRENT FMP STRUCTURE

Funding Zones

Under the FMP, the Plan is considered "Fully Funded" when its projected assets are within a range of the projected cost of the net liability[5] (depicted in yellow in Figure 1). The lower end of the funding range is defined as projected assets being equal to the projected cost of the net liability, employing a discount rate referred to as the "Restoration Basis". The upper end of the range is defined as projected assets equal to 110% of the projected cost of the net liability, employing a discount rate referred to as the "Distribution Basis". The Distribution Basis is a more conservative (lower) spread[6] than the Restoration Basis, and thus implies a higher projected cost for the net liability. The two bases are described further below.

When the funding position is within the fully funded range, FMP guidance is that the Plan is adequately funded to provide base benefits (including full inflation indexation) supported by the base contribution rate (average base contribution rate is 11% per Plan Sponsor). Given the volatility of market factors and the assumptions embedded in the funding valuation, no action toward benefit improvements or lower contributions is recommended. In other words, the guidance is to conserve the assets to protect against any uncertain times.

When the Plan is in a strong financial position, FMP guidance is for the Distribution Basis spread of 0.5% to be applied. Using the more conservative spread helps ensure that the Plan can afford the use of any surplus over the long term. When assets exceed the projected cost of future benefits (valued under the distribution basis) by more than 10%, the Plan is considered to be in the "Usable Surplus" zone (see blue zone in Figure 1) and the surplus can be used to lower contribution rates, permanently improve future benefits, or a combination of the two. The additional 10% threshold and lower basis are intended to create a buffer in 'good times' to cushion the Plan when economic conditions are less favourable. The higher standard for what constitutes a usable surplus aims to help the Plan avoid benefit improvements or unrealistic contribution reductions that could jeopardize the long-term health of the Plan.

In March 2015, a zone for Temporary Plan Improvements (depicted in green in Figure 1) was added to the FMP, to allow for temporary contribution decreases, surplus distribution and/or benefit improvements (so long as they do not increase the long-term cost of the Plan) when assets exceed the projected cost of future benefits when valued using the Temporary Basis. The basis for the Temporary Plan Improvements zone is the Reference Rate plus a spread of 1.25%, employing the lesser of the smoothed[7] or market value of the funding position. Temporary plan changes are implemented on a one-year lag, and are committed to for at least three years (until the next required filing). Uses of surplus in this zone are paced, amortized over a period between three and 10 years, with an annual spending limit applied to amortization terms shorter than 10 years. The zone includes a provision that temporary improvements cease if a significant market event occurs.

When the Plan has a funding shortfall[8], the Restoration Basis spread of 1.55% is applied according to the FMP (orange and red zones in Figure 1). Funding valuations that show a shortfall prepared on this basis require the Plan Sponsors to rebalance the Fund before filing with the regulators by raising contribution rates (the FMP dictates a maximum contribution rate of 14% (although formally documented as 15% of salary above YMPE), lowering future inflation indexing for service accrued after 2009, lowering other future benefits, or a combination of these options. The higher 1.55% spread helps absorb short-term market volatility, allowing the Plan to avoid the need for frequent changes to contribution or benefit levels to keep Plan assets and costs in balance.

See Appendix I for a summary of the FMP document, including the provisions associated with each defined funding zone.

[5] The projected cost of the net liability refers to the projected value of benefits already accrued plus the projected benefits to be earned by today's members less their future contributions.

[6] Spread over the Reference Rate (the rate chosen by the Board to represent Government of Canada nominal and real return bond yields).

[7] Any losses held back by smoothing are not available for temporary improvements.

[8] The cost of future benefits exceeds the Plan's net assets.

Real Discount Rate Guidance

The FMP guidance for the real discount rate assumption used in the annual funding valuation is documented as the Reference Rate plus a spread of either the Distribution (0.5%), Temporary (1.25%) or Restoration (1.55%) Basis. Which basis is used depends on the Plan's financial health. The Board has chosen its interest rate to be the 36-month average Government of Canada 30-year real-return bonds (intended to reflect the risk-free real returns being provided by the market). If the Board were to diverge from the FMP guidance in determining its interest rate, they would have a dialogue with the Partners prior to implementation.

While the FMP provides guidance, OTPP's Board is accountable for setting the real discount rate assumption. The FMP-guided rate essentially defines the starting point, upon which the Board overlays a thorough 'building block' analysis to assess future real returns less expenses and less provisions for risk, to assess whether the FMP-guided rate is acceptable for the purposes of the valuation in question, or whether it requires modification[9]. If the Board chooses to use a real discount rate above what is prescribed by the FMP (which, historically, it has) there is generally no concern from the Sponsors. However, if the Board uses a discount rate different from that outlined in the FMP and this discount rate is more conservative (that is, produces a larger deficit or a smaller surplus), the FMP becomes void in 12 months unless both Partners notify the Board otherwise.

Given the importance and impact of the real discount rate assumption in a funding valuation, the Sponsors, under certain conditions, can request an independent review by a Hearing Officer of the real discount rate proposed by the Board for a filing. This process, referred to at OTPP as the 'Discount Rate Review', can be invoked if a preliminary valuation shows a shortfall based on a real discount rate lower than 3.575%. The conditions for the review, as well as the process for selecting a Hearing Officer and timelines, are defined in the annual consultative process between OTPP and the Plan Sponsors.

Partners' Strategic Guidance Statement

In planning its investment strategy and making other long-term arrangements, OTPP management has made a series of assumptions about the Partners' tolerance for risk, and consequently their willingness to make adjustments in CIP, contributions or other aspects of the Plan. In 2014, a tripartite Sponsor's Task Force (facilitated by Dr. Harry Arthurs) created the *Partners' Strategic Guidance Statement,* which outlines the Partners' objectives, including intergenerational equity and desired risk tolerance in terms of contribution, indexing and other benefit changes.

This document is an important resource in our working relationship with the Partners, particularly in guiding discussion on funding issues over time. The *Partners' Strategic Guidance Statement* provides a disciplined framework for discussion, particularly with respect to addressing key principles such as plan sustainability and intergenerational equity. Recognizing the continuous evolution of the Plan's characteristics over time, the statement serves as a 'living' document, where its principles reflect our current state but can also be revisited in the future. The Partners' Committee is committed to its periodic review (at a minimum of every five years) to ensure it remains relevant and reflective of the Plan, while maintaining a formal and collective understanding of the important underlying principles. See Appendix II for the *Partners' Strategic Guidance Statement* and a pictographic depiction of the tolerance levels within the Partners' Strategic Guidance Statement with respect to the current FMP levers.

[9] The review process undertaken by the Board in setting the real discount rate is discussed in detail in the document *Discount Rate for OTPP's Funding Valuation*.

FMP Coles Notes.pdf

FIGURE 1. FUNDING MANAGEMENT POLICY (FMP) FRAMEWORK DESCRIPTION

Valuation Basis

Assets = 110% of Liabilities valued at interest rates + 0.5%

Zone:	**Permanent Plan Improvements (Usable Surplus)**
Mechanism:	**Improve benefits as negotiated**
Funding Risk:	Plan is essentially fully funded at Government of Canada long bond rates. Funding security is desired to ensure the Plan can support these benefits continually in the future. The impact of new teachers is important as they will create losses.

That is, Assets ~ 133% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.25%

Zone:	**Temporary Plan Improvements**
Mechanism:	**Improve benefits or lower contributions as negotiated[1]**
Funding Risk:	Plan is well funded and can afford changes that temporarily provide a benefit enhancement (as long as it does not create a long term cost) and/or lower the contributions being paid into the Plan.

[1] Amortization period used to determine temporary benefit

That is, Assets ~ 107% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.55%

Zone:	**Fully Funded (Do Nothing)**
Mechanism:	**Maintain Base Benefits and Contributions**
Funding Risk:	Plan is adequately funded to provide base benefits supported by the base contributions. Given the volatility of market factors and the numerous assumptions in the funding valuation, "fully funded" is considered a range.

Zone:	**Additional Support Required From Current FMP Levers**
Mechanism:	**Raise Contribution Rates and/or Invoke Conditional Inflation Protection as negotiated**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions. An increase to the contribution rate (within FMP maximum) and/or a decrease to the level of indexing being provided are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Zone:	**Additional Support Required From New/Additional Changes**
Mechanism:	**Negotiate other plan changes**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions and CIP is fully invoked and contribution rates are increased to maximum outlined in FMP. Plan changes are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
Application (Article I):	**Section 1.01 and 1.02** ▪ Requires the Board to use Board's "best estimates assumptions," including a margin for adverse deviation in the case of the discount rate. ▪ Sets out what best estimates economic assumptions may be based on. ▪ Requires the Board to maintain indices to record inflation adjustments for post-2009 service. **Sections 1.03 and 1.04** ▪ If the Board uses a discount rate different from that outlined in the FMP and this discount rate is more conservative (that is, produces a larger deficit or a smaller surplus), the FMP becomes void in 12 months unless both Partners notify the Board otherwise. These sections serve as an "exit" provision for the Partners. **Section 1.05** sets out under what circumstances each section of the FMP applies. **Section 1.06** limits surplus distributions or contribution decreases to those permitted by law. **Section 1.07** makes temporary improvements conditional on not having a restoration basis deficit.
Definitions (Article II):	**Section 2.01** Defines key terms, including: ▪ Basic contributions (contributions as per Sch.1 on January 1, 2012), which is used throughout the FMP as the target contribution rate (10.4% on earnings up to the YMPE/12% above the YMPE). ▪ Run-rate benefits (benefits as per Sch.1 on January 1, 2009), which include 100% inflation protection and assume basic contributions. ▪ Reference Rate (rate chosen by the Board representing Government of Canada nominal and real return bonds, which may be based on market or smoothed data; has recently been 36 month smoothed nominal and real return bonds). ▪ Remaining amortization value (difference between the temporary improvement value and the commitment value). ▪ Temporary improvement value (present value of a temporary improvement amortized over 3-10 years; if amortized over fewer than 10 years, improvement for a year is limited to the amount of basic contributions paid during a year).
Restore basic contributions and benefits (Article III):	**Section 3.01** ▪ Restoration basis is used (*reference rate* + 1.55%). ▪ Defines assets (refers to PBA Regulations) and current and revised liabilities. **Section 3.02** ▪ Sets out that current and revised liabilities are calculated using the restoration basis, plus an adjustment. The phrase "plus an adjustment" is used throughout the FMP and reflects the fact that the Board often files using a basis that is higher than required under the FMP. **Section 3.03** ▪ Outlines how indexing is accounted for in the valuation (that is, level of indexing provided in current filing zone continues).
Restoration Basis: ***Surplus***	*Sections 3.04 to 3.08 apply when surplus exists using the restoration basis and current contributions are higher than target, partial indexing (for previous years or go forward) exists or other benefits have been reduced.* **Section 3.04** Sets conditions under which sections 3.05-3.08 apply: ▪ If Assets > Liabilities (surplus reported); and ▪ Current contributions > Basic contributions (i.e., contributions are above long-term target level); or ▪ Current Benefits < Run-Rate Benefits (i.e. contributions are above long-term target level or benefits are below the long-term target level). **Section 3.06** Sets out the order of how to restore past benefit reductions or contribution increases: ▪ Actions can consist of increasing benefits to run-rate (long-term target) including prospective restoration or lowering contributions to basic (target) or a combination. ▪ First, increase go-forward indexing to 50% for post-2013 service period, then to 100% on all post-2009 service periods. Second, restore current pension amounts to run rate level, as much as possible, starting with the years where indexing was less than 50% until all years of partial indexation are restored to the same level and then restore to 100% for all service periods. ▪ Partners reserve the right to reconsider order in the future.
(Article III continued)	**Section 3.07** A number of conditions apply after a decision: ▪ Assets equal to or greater than revised liabilities (i.e. no deficit created); ▪ Inflation indexing restored to no more than if 100% of inflation was provided;

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	▪ Inflation indexing restored to no less than current level (i.e. can't lower prior inflation indexing given); ▪ The value of revised benefits needs to be between current and run-rate benefits (similarly, contributions must be between current and target). **Section 3.08** (Expires December 30, 2017) Sets out the limits from the 2013 Term Sheet (commonly known as the JSPP Agreement) with respect to escalated adjustments and benefit improvements: ▪ Escalated adjustments if assets are greater than 100% of the current liabilities (and not below 100% after). ▪ Benefit improvement or restoration if net assets available for benefits are greater than 105% of the current (unsmoothed) liabilities (and not below 105% after).
Restoration Basis: *Deficit*	*Sections 3.09 to 3.14 apply when the liabilities are greater than the assets using the restoration basis; thus the Partners must raise contribution rates, lower the amount of indexing and/or decrease other benefits.* **Section 3.09** Sets conditions under which Sections 3.10 to 3.14 apply: ▪ If Current liabilities > Assets (i.e., deficit reported). **Section 3.11** Sets out that deficit can be eliminated by changing contributions or benefits provided that: ▪ Assets are equal to or greater than revised liabilities; and ▪ Revised member contributions are no more than 15% (above YMPE).
(Article III continued)	**Section 3.12** The Partners can agree to change benefits or contribution level as long as: ▪ Partners have entered into a written agreement governing the manner in which contributions by the Minister and the Employers will be adjusted to offset any reduction in benefits; and ▪ No indexing granted gets taken away. **Section 3.13** Outlines the current intention that member contributions will be increased up to 15% (above YMPE) before benefits are reduced or less than full indexing is provided. **Section 3.14** Sets out the limits with respect to the 2013 Term Sheet regarding employer contribution increases.
Funding Zone: Temporary (Article IV):	**Section 4.01** ▪ Temporary basis is used (*reference rate* + 1.25%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent). - Current liabilities (liabilities including the greater of current and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Revised liabilities (liabilities including the greater of revised and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus). **Section 4.02** Sets out that the liabilities are calculated using the temporary basis, plus an adjustment. *Sections 4.03 to 4.06 apply when the plan has a surplus using the temporary basis; that is, there is surplus available for improving benefits, decreasing contributions or distributing surplus, all on a temporary basis. The surplus spend is amortized over a period of three to ten years, at the partners' choice. If amortization period is less than ten years, the annual spend limit is the amount of basic contributions for a year.* **Section 4.03** Sets out conditions under which Sections 4.04 and 4.05 apply: - If assets > liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided. **Section 4.04**

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	The Board reports the commitment value (the amount of surplus that can be used to provide a temporary improvement). **Section 4.05** The Partners can agree to temporary improvements so long as after the change, assets over revised liabilities are equal to or greater than zero. **Section 4.06** provides a requirement for a side agreement setting out how Minister contributions may be adjusted if there is a surplus distribution or temporary improvement of benefits.
"Do Nothing" Zone (Article IV continued):	*Sections 4.07 to 4.09 apply if assets are equal to or less than current liabilities using the temporary basis; that is, if there is a deficit using the temporary basis.* **Section 4.09** States that the Partners will not provide new improvements if there is a temporary basis deficit. That is, the Partners will do nothing, and Article III (restoration basis) will apply. However, no actions result from move to restoration because contributions and indexing are already at run-rate in order to be in temporary zone. The Partners could, however, have to file a valuation (using the restoration basis) if the filing schedule required a filing.
Funding Zone: Distributions (Article V):	**Section 5.01** ▪ Distribution basis is used (*reference rate* + 0.5%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent) - Liabilities (includes remaining amortization value) - Current targeted funding amount - Revised targeted funding amount - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus) **Section 5.02** Sets out that the liabilities are calculated using the distribution basis, plus an adjustment. *Sections 5.03 to 5.05 apply when the plan has a surplus using the distribution basis; that is, there is usable surplus for improving benefits above run-rate permanently or decreasing contributions below target level permanently.* **Section 5.03** Sets out conditions under which Sections 5.04 and 5.05 apply: - If Assets **>** 110% of Liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.05** The Partners can agree to change benefits or contributions so long as after the change assets remain greater than 110% of the liabilities and a side agreement has been entered into to set out how Minister contributions may be adjusted if there is a surplus distribution or temporary improvement of benefits. *Sections 5.06 to 5.08 apply when the plan has a funding ratio that is at least 100% but less than 110% and valued using contribution rates at the basic or target level, full indexing provided prospectively and benefits fully restored.* **Section 5.06** Sets out the conditions under which Sections 5.07 and 5.08 apply: ▪ If Assets ≤ 110% of Liabilities; and ▪ Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and ▪ Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and ▪ Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.08** If the conditions in Section 5.06 are satisfied, there is not sufficient surplus to provide a permanent improvement; therefore, Article IV will apply to determine whether there is surplus using the temporary basis.

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
Post-December 30, 2017 Valuations (Article VI):	*This section articulates at a high level the use of the surplus credits (earned pre-January 1, 2018) after December 30, 2017. OTF earns surplus credit for any unmatched forgone inflation (i.e., inflation indexing less than 50%) prior to January 1, 2018 or via other benefit reductions made before January 1, 2018. See the JSPP Agreement for more detail.* **Section 6.01** ▪ Restoration basis is used (*reference rate* + 1.55%). ▪ Defines: - Assets (PBA regulations) - Current Liabilities - Revised Liabilities **Section 6.02** Provides overriding provision for post-December 30, 2017: for valuations where assets are greater than current liabilities, Section 6.03 applies (with reference to the 2013 Term Sheet). **Section 6.03** Sets out the use of surplus credits: ▪ OTF has first call on surplus up to a limit; ▪ Surplus credits include foregone pension payment amounts.
Valuation frequency and filing (Article VII):	*This section reinforces an earlier section of the Partners' Agreement that specifies that it is the Partners' joint decision whether to file (other than in a required filing year).* ▪ Partners' decision when to file. ▪ Partners will notify the Board within 7 months of valuation date.
Arbitration (Article VIII):	Refers to Arbitration already in prior section of the Partners' Agreement.
Limitations (Article IX):	FMP does not apply for changes required by law or for changes that increase the liabilities by less than 0.5% or for changes that use the $76m in section 60 *(Note $76m was utilized with January 1, 2008 filing).*

OTPP JSPP Afreement final March 2013.pdf

OTPP Term Sheet – March 13, 2013

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

March 13, 2013
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	6,309
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	467
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	4,094
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	7,386
			$ 20,107

Report on Funding.pdf

Teachers' Pension Plan Board

Ontario

REPORT ON FUNDING

April 2002

This is a report on the financial health of the Teachers' pension plan and on the progress of the development of a funding management policy.

The responsibility to ensure a defined benefit pension plan is fully funded lies with the sponsor of the plan, usually the employer. In the case of the Teachers' pension plan, however, there are two sponsors: the Ontario government and the Ontario Teachers' Federation, representing the plan members.

The co-sponsors negotiate the use of surplus and, when there is a deficiency, they both make additional contributions to ensure the plan is fully funded within a specified time period.

To assess the financial health of the plan, we hire an independent actuary to conduct a valuation at least once every three years. This valuation determines if the plan has a funding surplus or deficit.

Funding Valuation Results

On January 1, 2002, the Teachers' pension plan had a funding surplus of $1.9 billion, including a $3-billion smoothing adjustment. Without smoothing, the plan had a $1.1-billion deficit.

($ billions) (at January 1)	**02**	01	00	99	98	96	93**
Net assets	**$ 69.5**	73.1	68.3	59.1	54.5	40.1	29.4
Smoothing	**3.0**	(4.3)	(7.3)	(5.1)	(6.0)	(1.8)	---
Value of assets	**72.5**	68.8	61.0	54.0	48.5	38.3	29.4
Future contributions	**13.7**	14.4	13.4	12.0	12.6	14.5	14.3
Special payments*	---	---	---	3.7	8.5	8.4	8.4
Actuarial assets	**86.2**	83.2	74.4	69.7	69.6	61.2	52.1
Future accrued benefits	**84.3**	76.4	69.8	66.2	62.8	60.5	50.6
Surplus (deficit)	**$ 1.9**	6.8	4.6	3.5	6.8	0.7	1.5

* Payments committed by the government toward the pre-1990 unfunded liability

** Valuation dates determined by co-sponsors

Assumptions

Valuations use many estimates, or assumptions. Among them are: how long will a teacher teach? What will inflation be in the future? What salary increases are teachers likely to receive? How long will the average teacher live?

These assumptions are used to estimate the value of the future benefits owed to teachers. In addition, an assumption of the long-term rate of return is used to determine if today's assets plus future contributions will be sufficient to pay promised pensions.

Valuation Assumptions

(percent)	2002	2001
Discount rate	6.30	6.25
Salary escalation rate	2.90	3.20
Inflation rate	1.90	2.20

The discount rate is the long-term market rate of return used to determine the present value of all future pension benefits and assets.

The assumptions are intended to be accurate over a long horizon. While actual experience mirrors some assumptions closely, annual equity returns fluctuate greatly compared to our assumption (6% plus inflation).

It would be impractical to adjust contribution rates frequently because of investment swings. So, to reduce short-term fluctuations in the funding surplus, equity returns compared to our long-term assumptions are 'smoothed.'

WHAT'S INSIDE...

- Understanding Smoothing pg 2
- Funding Management Policy pg 2
- Use of Surplus pg 4

Questions? www.otpp.com or 1-800-668-0105

Understanding Smoothing

Gains and losses from equities are smoothed over five years, a practice accepted by the actuarial profession and pension regulators.

Smoothing defers gains when actual equity returns exceed the 6% plus inflation assumption. On the other hand, when returns are below the assumption, smoothing defers losses (as is the case this year). This practice is simply used to soften the impact of annual volatility in equity markets.

How Smoothing is Calculated

($ billions)

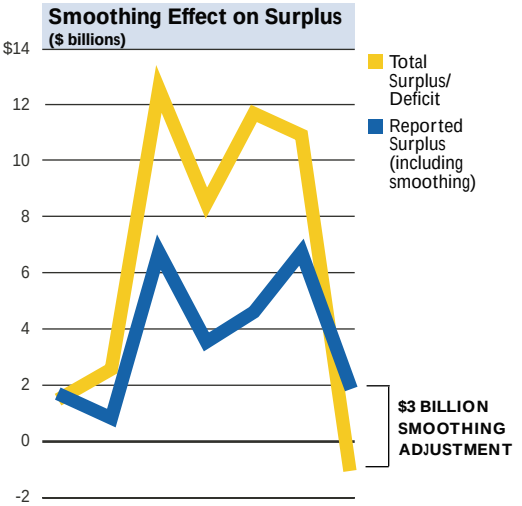
Year	Gain/ (loss)	to be recognized in 2006	2005	2004	2003	Held back in 2002
1997	$3.5					
1998	$1.3				0.3	**0.3**
1999	$6.7			1.34	1.34	**2.7**
2000	($1.2)		(0.24)	(0.24)	(0.24)	**(0.7)**
2001	($6.6)	(1.32)	(1.32)	(1.32)	(1.32)	**(5.3)**
Smoothing						**(3.0)**

Each year, we recognize 20% of equity gains or losses. Smoothing consists of the remaining portions that will be recognized in the future. For the last two years, equity returns have fallen short of our assumption, causing losses held back by smoothing.

At its peak, smoothing held $7.3 billion in reserve. In 2002, smoothing increased actuarial assets by $3 billion to show a $1.9 billion surplus, instead of a $1.1 billion deficit.

However, smoothing is only capable of absorbing short-term fluctuations in returns and will not sustain a funding surplus in a long period of poor market performance.

The funding surplus is the more important number for plan members. It is used to determine benefit improvements or changes to the contribution rate.



Without the $3-billion smoothing adjustment, the plan would have had a funding deficiency of $1.1-billion this year. We are concerned about the downward trend.

Comparing Valuations

We also report a financial valuation in our annual report. The two surpluses are different because the funding surplus includes two projections: future contributions and future benefits for all current teachers.

Comparing the valuations shows a $5.1-billion difference. In other words, there is a $5.1-billion cost to provide future benefits for plan members that are not funded by the current contribution rate. We expect this gap to grow as new teachers enter the plan.

($ billions)	**Financial** (at Dec. 31/01)	**Funding** (at Jan. 1/02)
Net assets	$ 69.5	$ 69.5
Smoothing adjustment	3.0	3.0
Future contributions	---	13.7
Actuarial assets	72.5	86.2
Accrued benefits	65.5	65.5
Future benefits	---	18.8
Surplus	**$ 7.0**	**$ 1.9**

The Role of a Funding Management Policy

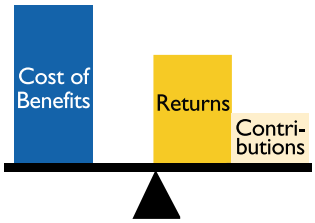
Within certain legislated limits, the co-sponsors negotiate benefit and contribution levels. For 2002, the co-sponsors have decided not to make any changes to contributions or benefits and to concentrate on developing the funding management policy. The pension board fully supports their decision and efforts.

In light of our outlook for equity markets, new benefit costs present a challenge to us and a cautionary note to plan members and the co-sponsors. Over the next decade, we expect modest real rates of return from stock and bond markets compared with the past 10 years.

Despite what the 1990s suggested, 2000 and 2001 have proven that markets are not one-way streets. In fact, historically they have only produced returns equal to the plan's 4.5% long-term funding requirement about 60% of the time.

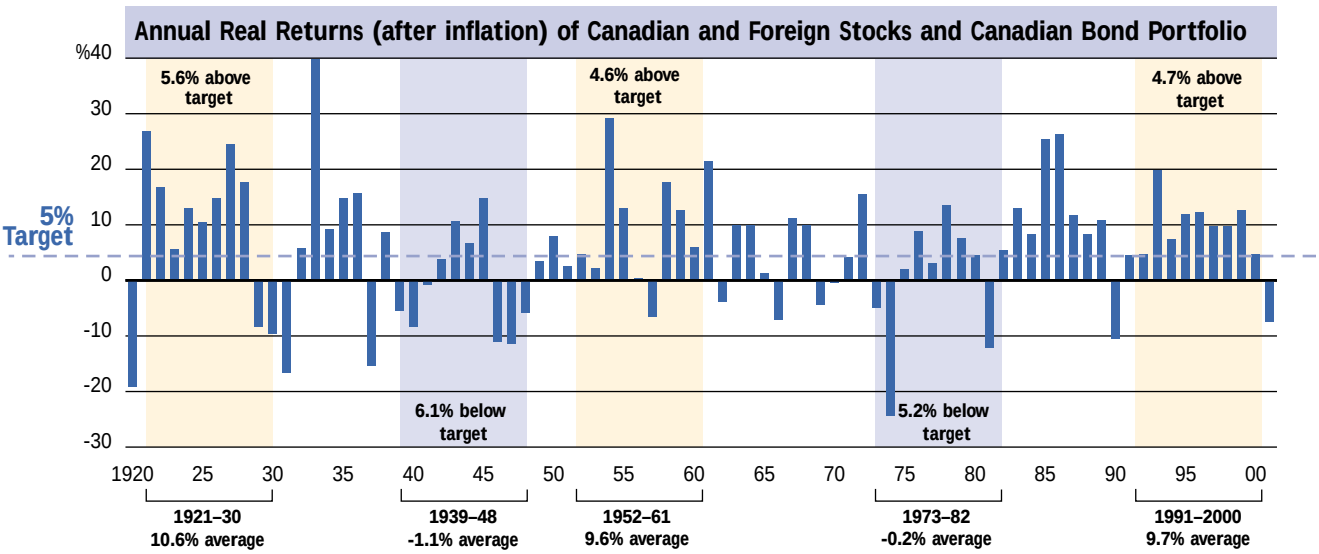
To sustain improved benefit levels for young and future teachers, without the need for contribution increases, we will need to generate a minimum real rate of return of 5% over the long term. That may be very difficult over the next decade.

Over the long term, benefits must balance with contributions plus investment returns or there will be a deficit. If the fund has a deficit when the funding valuation is filed, the law will automatically trigger a contribution rate increase. The only alternative for the co-sponsors would be to reduce future benefits.



The objective of a funding management policy is to provide a framework for improved long-term governance of the fund by determining when it is prudent to increase benefits, change contributions, or conserve assets. This policy will guide the co-sponsors in making these complex decisions, and help address the risks of poor market performance borne by both working teachers and the government. It is also important from an investment perspective, as it will change the risk profile of the fund and affect the pension board's investment policies.

Teachers have told us in focus groups that they would prefer contribution rates to remain stable. A funding management policy will help to ensure this occurs. Development of a workable policy will put the plan's co-sponsors at the forefront of exercising solid pension plan governance that balances the interests of all plan members – working or retired teachers – and the government.



This graph shows how a hypothetical portfolio, based on a similar asset mix as our own, would have performed over the last 80 years. One of the best decades in history was the 1990s. The portfolio includes two-thirds stocks (28% Canadian, 17% U.S., 22% foreign), and one-third Canadian bonds. The plan will need to earn a minimum of 5% over the long term to fund benefits at current levels.

Use of Surplus

In 1990, the plan had a $7.8 billion unfunded liability. The Ontario government agreed to pay the initial unfunded liability through a series of special payments over 40 years.

The pension plan has enjoyed a series of funding surpluses, primarily due to above-average investment growth brought on by strong equity markets throughout the 1990s and lower than expected increases in wages and inflation.

Since 1993, $18.6 billion in surplus was used by co-sponsors to improve benefits and eliminate special payments.

Valuation date	Surplus/ (Deficit)	OTF	Ontario government	Surplus remaining
1990	($7.8) 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	$325 million to offset social contract days	Eliminated special payments for $1.2 billion saving	$0
1996	$0.7	$0.6 for benefit improvements and RCA contributions[2]		$0.1
1998[3]	$6.8	$2.2 for benefit improvements[4]	$4.6 to reduce the value of remaining special payments	$0
1999	$3.5		$3.5 to reduce the value of remaining special payments[5]	$0
2001	$6.8	$6.2 for benefit improvements[6]		$0.6
2002	$1.9	Co-sponsors agreed not to make any changes to benefits or contributions		$1.9
Total		$9.3 billion	$9.3 billion	

[1] Savings offset cuts that would have been made in the education sector as part of the government's overall cost-cutting program.

[2] Benefit improvements: reduced early retirement penalty to 2.5% from 5% for each point short of 90 factor, making it easier to retire early; lower CPP reduction after age 65 (to 6.8% from 0.7%).

[3] In 1998, the co-sponsors agreed future surplus would first be used to eliminate the remaining special payments, and the next $6.2 billion would be available exclusively to the OTF.

[4] Benefit improvements: 85-factor window from 1998 to 2002; lower CPP reduction after age 65 (to 0.6%)

[5] The government paid off its remaining special payments by the end of 1999.

[6] Benefit improvements: permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average YMPE to calculate CPP reduction; pension recalculation based on approximate best-5 salary for older pensioners; and top-up waived for LTIP contributions.

FW_ OTPP documents.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: FW: OTPP documents
Date: Friday, September 16, 2016 19:35:43
Attachment 1: Schedule 1 - 20140721.pdf
Attachment 2: 20150928 amendment.pdf
Attachment 3: 20150922 amendment.pdf
Attachment 4: 20151128 amendment.pdf
Attachment 5: Current - Partners' Agreement - 03-06-15.pdf
Attachment 6: 20150521 amendment.pdf

Lucy,

These docs should all be in the materials provided earlier, but I'm just going through a duplicate binder and I fear that the Partnership Agreement may have been accidentally excluded. It is the 5th attachment. My apologies for any inconvenience.

Nadine

Schedule 1 - 20140721.pdf

ONTARIO TEACHERS' PENSION PLAN

SCHEDULE 1 to the *TEACHERS' PENSION ACT*

PART I
INTERPRETATION

Definitions

1. (1) In this Schedule,

“active member” means a person employed in education who is making contributions under the plan and includes a person receiving payments under a long term income protection agreement and by whom or on whose behalf contributions are being made in accordance with subsection 21 (1); (Last amended August 4, 2011 – Effective September 1, 2011)

"active member on LTIP" means an active member as described in section 6;

"administrator" means the Ontario Teachers' Pension Plan Board; (Last amended June 28, 1990 - Effective June 28, 1990)

"average salary", of a member, means the average salary determined in accordance with section 15;

“benefit” means an amount payable under the pension plan, including a pension, a commuted value or a lump-sum payment; (Last amended May 5, 2010 – Effective September 1, 2002)

"board of education" has the same meaning as "board" in subsection 1 (1) of the *Education Act*;

"child" has the same meaning as in subsection 1 (1) of the *Family Law Act*;

"date of disability", of an active member on LTIP, means the date on which the member ceases to be employed in education as a result of the disability;

"dependent child" means a child of a deceased member who was dependent on the member for support at the time of the member’s death, and who,

(a) is less than eighteen years of age, or

(b) is eighteen or more years of age but less than twenty-five years of age and is in full-time attendance at a school or university, having been in such attendance substantially without interruption since the child reached eighteen years of age or since the member died, whichever occurred later, or

(c) is disabled, having been disabled without interruption since the member died;

(Last amended May 5, 2010 – Effective January 1, 1992)

"designated organization" means an organization designated under subsection 119 (2);

"designated private school" means a school designated under subsection 119 (1);

"employed in education" means employed as described in section 2, 6, 7, 8 or 9; (Last amended October 10, 1995 - Effective January 1, 1990)

“employer-approved leave” means a leave of absence, with or without pay, to which the member’s employer consents; (Last amended July 21, 2014 – Effective September 1, 2014)

“long term income protection agreement” means an agreement to provide long term income protection in the event of a member’s long term disability that is entered into by an insurer within the meaning of section 1 of the *Insurance Act* and,

(a) the Minister of Education;

(b) a board of education;

(c) the Ontario Teachers’ Federation established under the *Teaching Profession Act*;

(d) an affiliated body described in the *Teaching Profession Act*; or

(e) an authority approved by the administrator.

(Last amended August 4, 2011 – Effective September 1, 2011)

"member" means a person who, as a result of his or her employment in education, is entitled to benefits or to a refund of contributions under the pension plan;

"re-employed pensioner" means a member who, after

(a) ceasing to be employed in education before, on or after September 1, 2012, and

(b) the beginning of the month in which the member’s retirement pension under the plan begins,

is employed by or otherwise engaged, directly or indirectly, to provide services for compensation for an employer who participates in the pension plan; (Last amended June 20, 2012 – Effective September 1, 2012)

“school day” has the same meaning as “school day” in subsection 1 (1) of the *Education Act* as amended from time to time; (Last amended July 21, 2014 – Effective September 1, 2014)

"school year" means the twelve-month period that normally begins on the 1st day of September, however, for a member whose school year commences prior to September 1st, the administrator may determine the days that the member is required to work prior to September 1st to be in the subsequent school year; (Last amended September 8, 2006 – Effective September 1, 2006)

“short absence” means an employer-approved leave of five or fewer consecutive school days; (Last amended July 21, 2014 – Effective September 1, 2014)

"spouse" means either of two persons who,

(a) are married to each other, or

(b) are not married to each other and are living together in a conjugal relationship,

(i) continuously for a period of not less than three years, or

(ii) in a relationship of some permanence, if they are the natural or adoptive parents of a child, both as defined in the *Family Law Act;*

(Last amended September 8, 2006 – Effective June 10, 2003)

"standard interest rate" means the interest rate determined under section 89;

"statutory leave" means any leave of absence within the meaning of the *Employment Standards Act, 2000* as amended from time to time; (Last amended September 8, 2006 – Effective September 4, 2001)

"Year's Maximum Pensionable Earnings", in relation to a year, means the Year's Maximum Pensionable Earnings prescribed under the *Canada Pension Plan.*

Qualification as a teacher

(2) A person is considered to be qualified as a teacher for the purposes of membership in the pension plan,

(a) if the person has obtained teacher certification from one of the Ministry of Education or the Ontario College of Teachers; or

(b) if a board of education holds a letter of permission granted by the Minister of Education in respect of the person.

(Last amended November 27, 2000 – Effective May 20, 1997)

Employment

(3) A person is considered to be employed,

(a) full-time, if the person is required to work throughout each work day of a year or of a session; and

(b) part-time, if the person is required to work on a regular but not full-time basis.

Idem

(4) A person is considered to be employed on an occasional basis as a teacher and not part-time if the person is an occasional teacher within the meaning of section 1 of the *Education Act*.

PART II
PARTICIPATION

A. Membership in the Plan

Eligibility for membership

2. (1) Every person is eligible to be an active member of the pension plan who is qualified as a teacher and is employed,

(a) as a teacher, as determined by the administrator, in a school within the meaning of subsection 1 (1) of the *Education Act*;

(b) as a teacher in a school outside Ontario under an approved teacher exchange system;

(c) as a teacher by the minister of a ministry of the Government of Ontario;

(d) as a teacher in a school or a class operated by the Toronto and Region Conservation Authority; or

(e) by a board of education.

(Last amended June 20, 2012 – Effective January 1, 2012)

Idem

(2) Every person is eligible to be an active member of the pension plan who is qualified as a teacher and is employed in a designated private school or a designated organization. (Last amended December 21, 2007 – Effective September 1, 2008)

Idem

(2a) Every person is eligible to be an active member of the pension plan who is qualified as a teacher and has taken a statutory leave from employment in education which leave began prior to the 1st day of September, 2010. (Last amended December 30, 2009 - Effective September 1, 2010)

Idem

(2b) Every person is eligible to be an active member of the pension plan who is qualified as a teacher and is receiving payments for loss of earnings in respect of employment in education under the *Workplace Safety and Insurance Act*. (Last amended September 8, 2006 – Effective September 1, 2006)

Exception

(3) No person is eligible to be an active member of the pension plan,

(a) if the person is regularly employed outside Ontario and is performing services in Ontario under an approved teacher exchange system; or

(b) beyond November 30th of the calendar year in which the person attains seventy-one years of age, or beyond such other time as is permitted under the *Income Tax Act* (Canada).

(Last amended June 20, 2012 – Effective January 1, 2012)

Commencement of membership

3. (1) Every person employed as described in subsection 2 (1) full-time or part-time becomes an active member of the plan on the later of,

(a) the 1st day of January, 1990;

(b) the date the employment contract begins; or

(c) the date on which the person becomes qualified as a teacher.

(Last amended June 20, 2012 – Effective January 1, 2012)

Idem

(2) Subject to subsection 5 (1), every person employed as described in subsection 2 (2) full-time or part-time becomes an active member of the plan on the day that is the latest of,

(a) the 1st day of January, 1990;

(b) the date the employment contract begins; or

(c) the date the designation of the private school or the organization is effective.

Idem

(3) Every person employed in education on an occasional basis becomes an active member of the plan on the person's first day of employment in a school year. (Last amended February 20, 1997 - Effective January 1, 1997)

(3a) Revoked. (Last amended February 20, 1997 - Effective January 1, 1997)

Commencement of membership, re-employed pensioner

(4) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Idem

(4a) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Idem

(5) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Idem

(6) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Election re occasional employee

4. (1) Revoked. (Last amended February 20, 1997 - Effective January 1, 1997)

Obligations

(2) Revoked. (Last amended October 10, 1995 - Effective September 1, 1996)

Election re designated private schools, etc.

5. (1) A person employed at a designated private school or a designated organization on the date the designation becomes effective may elect not to become an active member of the plan.

Time for election

(2) An election under this section is not effective unless delivered in writing to the governing body of the designated private school or designated organization and to the administrator,

(a) not later than three months after the effective date of designation for the private school or organization, if the person is qualified as a teacher when the designation takes effect; or

(b) not later than three months after the date the person becomes qualified as a teacher, if the person is not so qualified on the effective date of designation for the private school or organization.

Not applicable

(3) This section does not apply to a person who is an active member of the plan or to a person who is receiving a pension under the plan on the date the designation becomes effective. (Last amended September 8, 2006 – Effective September 1, 2002)

Further election

(4) This section applies with necessary modifications to a person employed at a designated private school or a designated organization on September 1, 2008, who becomes eligible for active plan membership on that date in accordance with subsection 2 (2). The required election must be delivered by December 1, 2008. (Last amended December 21, 2007 – Effective September 1, 2008)

Active member on LTIP

6. (1) An active member who begins to receive payments under a long term income protection agreement continues as an active member of the plan until the earlier of:

(a) the date the member ceases to receive payments under the long term income protection agreement;

(b) the date the member begins receiving a benefit under the pension plan; or

(c) the end of the calendar year in which the member attains seventy-one years of age, or such other time as is permitted under the *Income Tax Act* (Canada).

(Last amended August 4, 2011 – Effective September 1, 2011)

Idem

(1a) For the purposes of subsection (1), an active member who has been approved for payments under a long term income protection agreement but is not receiving payments by reason of the application of offset or all-source maximum provisions of the long term income protection agreement shall be deemed to receive payments under a long term income protection agreement. (Last amended August 4, 2011 – Effective September 1, 2001)

Idem

(1b) For the purposes of subsection (1) and subject to the limits set forth therein, an active member who receives payment in the form of a lump sum under a long term income protection agreement shall be deemed to receive payments under a long term income protection agreement for the period determined by the administrator. (Last amended August 4, 2011 – Effective September 1, 2011)

Evidence of medical condition

(1c) The administrator may at any time require a member described in subsection (1b) to furnish evidence, in such form as the administrator directs, that the member is disabled as defined under Regulation 8500 (1) of the *Income Tax Act* (Canada) throughout the period of active membership on LTIP. The period of active membership on LTIP of a member described in subsection (1b) shall terminate at the end of the month in which the administrator notifies the member that the administrator is not satisfied that the member is disabled. (Last amended August 4, 2011 – Effective September 1, 2011)

Return to employment

(1d) If a member described in subsection (1b) becomes employed in education, other than as an active member on LTIP, and the percentage of full-time basis of that employment is equal to or greater than the percentage of full-time basis upon which the member was employed immediately prior to becoming disabled, the member shall be deemed to have ceased to receive payments under a long term income protection agreement on the date that the member commences that period of employment in education. (Last amended August 4, 2011 – Effective September 1, 2011)

Eligibility

(2) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(3) Revoked. (Last amended April 2, 2001- Effective September 1, 2001)

Definition

(4) Revoked. (Last amended August 4, 2011 – Effective September 1, 2011)

Active membership, university faculty

7. (1) A member who, during an employer-approved leave, becomes employed on the staff of a faculty of education of an Ontario university on or after the 1st day of January, 1990 is an active member of the plan. (Last amended July 21, 2014 – Effective September 1, 2014)

Limitation

(2) A person is eligible for active membership under this section for a maximum of five school years.

Not applicable

(3) This section does not apply to a person who is employed on the staff of a faculty of education of an Ontario university that is designated under section 119. (Last amended September 8, 2006 – Effective September 1, 2002)

Transitional re universities

8. (1) A person who, on the 1st day of January, 1990, is qualified as a teacher and is employed full-time on the staff of a faculty of education of an Ontario university is an active member of the plan as long as the person continues in full-time or part-time employment at such a faculty.

Idem, part-time employee

(2) A person who, on the 1st day of January, 1990, is qualified as a teacher and is employed part-time on the staff of a faculty of education of an Ontario university is an active member of the plan as long as the person continues either part-time or full-time employment at such a faculty.

Not applicable

(3) This section does not apply to a person who is employed on the staff of a faculty of education of an Ontario university that is designated under section 119. (Last amended September 8, 2006 – Effective September 1, 2002)

Transitional re Ryerson, CAATs

9. (1) This section applies with respect to a person who,

(a) is qualified as a teacher and is employed by Ryerson University; or

(b) was deemed, under a predecessor of this Act, to be employed in education by a college of applied arts and technology. (Last amended May 5, 2010 – Effective July 1, 2002)

Idem, full-time employee

(2) A person who, on the 1st day of January, 1990, has been employed full-time by Ryerson University or a college of applied arts and technology continuously since the 1st day of September, 1984 is an active member of the pension plan as long as the person continues in full-time employment either at Ryerson or at such a college. (Last amended May 5, 2010 – Effective July 1, 2002)

Idem, part-time employee

(3) A person who, on the 1st day of January, 1990, has been employed part-time by Ryerson University or a college of applied arts and technology continuously since the 1st day of September, 1984 is an active member of the pension plan as long as the person continues in part-time or full-time employment either at Ryerson or at such a college. (Last amended May 5, 2010 – Effective July 1, 2002)

B. Credit for Service

Credited service

10. (1) An active member receives one year of credited service for working a full-time school year. (Last amended June 28, 1990 - Effective June 28, 1990)

(1a) For the purpose of determining credited service of an active member under this section, for the period to August 31, 2001, the administrator may use one or more standard calendars. (Last amended April 15, 1998 - Effective January 1, 1990)

Idem, partial year

(2) An active member receives credited service for part of a year in the proportion that the number of hours or days worked by the member during the school year bears to the number of hours or days in a full-time school year. (Last amended June 28, 1990 - Effective June 28, 1990)

Credited service during statutory leave

(2a) Despite subsections (1) and (2) an active member who makes contributions during a statutory leave which began prior to the 1st day of September, 2010 receives credited service for the number of days which the member would have worked during that leave to earn the amount of pensionable salary attributed to the member in calculating the member's contributions during the leave. (Last amended December 30, 2009 - Effective September 1, 2010)

Credited service during LTIP

(2b) (a) Despite subsections (1) and (2), an active member who is receiving payments under a long term income protection agreement and in respect of whom required contributions are being made in accordance with subsection 21 (1) shall receive credited service for the period that the member's employer reports the member would have worked if the member had worked throughout the school year. (Last amended August 4, 2011 – Effective September 1, 2011)

(b) Despite subsections (1) and (2), an active member who receives payment in the form of a lump sum under a long term income protection agreement and in respect of whom required contributions are being made in accordance with subsection 21 (1) shall receive credited service for the period to which the lump sum payment relates, as determined by the administrator in accordance with subsection 6 (1b). (Last amended August 4, 2011 – Effective September 1, 2011)

Credited service during WSIB

(2c) Despite subsections (1) and (2), an active member who is receiving payments for loss of earnings under the *Workplace Safety and Insurance Act* and in respect of whom required contributions are being made, shall receive credited service for the period that the member's employer reports the member would have worked if the member had worked throughout the school year. (Last amended September 8, 2006 – Effective September 1, 2006)

Idem

(2d) Despite subsection (2b), for the period of September 1, 2001 to August 31, 2006, where the credited service of an active member as described in subsection 6 (1a) is subject to the certification of a Past Service Pension Adjustment under the *Income Tax Act* (Canada), an active member shall receive credited service only once the administrator has obtained a certificate from the Minister of National Revenue. (Last amended August 4, 2011 – Effective September 1, 2011)

Credited service during sick leave

(2e) Despite subsections (1) and (2), an active member who is receiving sick leave payments, and in respect of whom required contributions are being made, shall receive credited service for the period that the member's employer reports the member would have worked if not for the sick leave. (Last amended December 19, 2012 – Effective September 1, 2012)

Credited service during unpaid professional activity days

(2f) Despite subsections (1) and (2), an active member who is subject to unpaid professional activity days, and in respect of whom required contributions are being made, shall receive credited service for the period that the member's employer reports the member would have worked if not for the unpaid professional activity days. (Last amended April 2, 2013 – Effective September 1, 2012)

Credited service during a short absence

(2g) Despite subsections (1) and (2), an active member who is on a short absence, and in respect of whom required contributions are being made, shall receive credited service for the period that the member's employer reports the member would have worked if not for the short absence. (Last amended July 21, 2014 – Effective September 1, 2014)

Idem, more than full-time school year

(3) Where an active member works more than a full-time school year he or she is not entitled to credited service for hours or days worked which are in excess of a full-time school year if he or she is entitled to a refund of contributions under s. 28, whether or not the refund is paid. (Last amended June 28, 1990 - Effective June 28, 1990)

Limitation

(4) Except for periods of lockout or legal strike a person shall not receive credited service for employment unless contributions in respect of the employment are made by or on behalf of that person. (Last amended June 29, 1994 - Effective January 1, 1990)

Idem

(5) No person is entitled to receive more than one year of credited service in respect of the person's employment during one school year.

Idem

(6) Subject to subsection (7), no person is entitled to accumulate more than thirty-five years of credited service under the plan in respect of a period prior to the 1st day of January, 1992. (Last amended February 28, 1992 - Effective January 1, 1992)

Exception

(7) A member who accumulates thirty-five years of credited service may continue to accumulate credited service until the month in which he or she reaches the age which, when added to the member's credited service equals ninety. (Last amended February 28, 1992 - Effective January 1, 1992)

Idem

(8) Despite subsection (7) a member may accumulate credited service greater than the limit set out therein with respect to a period after the 31st day of December, 1991. (Last amended June 1, 1995 - Effective June 1, 1995)

Partial year

11. (1) The length of a member's qualifying service determined under this section applies for the purpose of determining the member's entitlement to a benefit but does not apply for the purpose of calculating the amount of the benefit. (Last amended October 10, 1995 - Effective September 1, 1995)

Idem

(2) If a member accumulates more than ten days but less than or equal to one year of credited service as determined under sections 10, 96, 97 or 97a during one school year, the member's qualifying service shall be considered to equal one year. (Last amended May 5, 2010 - Effective September 1, 2001)

Idem

(2a) If the administrator is unable to determine in which of two successive school years the credited service of a member described in subsection (2) took place, it shall be deemed to have taken place in the earlier year. (Last amended October 10, 1995 - Effective September 1, 1995)

Idem

(3) If a member described in subsection (2), or a survivor of a member, receives a pension during the school year, the member shall receive qualifying service only for those months which the member, or survivor of the member, as the case may be, does not receive a pension. (Last amended October 10, 1995 - Effective September 1, 1995)

Idem

(4) If a member described in subsection (2) becomes employed in education for the first time on or after the 1st day of January, 1990, the member shall receive qualifying service only for that portion of the school year during which the member is an active member. (Last amended October 10, 1995 - Effective September 1, 1995)

Idem

(5) Revoked. (Last amended October 10, 1995 - Effective September 1, 1995)

Purchases of credit

(6) Subsection (2) shall include credited service accumulated by a member for a school year under section 94 or 95 in respect of periods on or after the 1st day of September, 2010, provided that the member has completed a purchase of the entire eligible absence period in respect of that school year. (Last amended August 4, 2011 – Effective September 1, 2010)

Partial purchases of credit

(7) If a member referred to in subsection (6) does not complete a purchase of the entire eligible absence period for a school year, the member shall only receive qualifying service in respect of the purchase equal to the member's credited service in respect of the absence. (Last amended December 30, 2009 - Effective September 1, 2010)

Limitation

(8) A member is not entitled to accumulate more than one year of qualifying service under this section in respect of a school year. (Last amended December 30, 2009 - Effective September 1, 2010)

Idem

(9) If a member accumulates ten days or less of credited service in respect of a school year, the member shall receive qualifying service for that school year equal to the member's credited service for that school year. (Last amended December 30, 2009 - Effective September 1, 2010)

C. Calculation of Pensionable Salary

Pensionable salary

12. (1) A member's pensionable salary for a school year is the remuneration paid to the member respecting employment in education and excludes,

(a) remuneration for services other than for employment in education;

(b) perquisites related to employment;

(c) payments related to accumulated sick leave or other employment benefit credits;

(d) payments related to retirement or termination of employment;

(e) payments to reimburse the member for expenses incurred during the course of employment;

(f) payments related to employment or for loss of earnings under the *Workplace Safety and Insurance Act* during a period in which the member is already an active member under section 6; (Last amended May 5, 2010 – Effective September 1, 2006)

(g) payments related to employment during a period in which the member is already an active member by virtue of receiving payments for loss of earnings under the *Workplace Safety and Insurance Act*; and (Last amended September 8, 2006 – Effective September 1, 2006)

(h) any remuneration paid to the member respecting employment in education that exceeds an annual rate of pay of six times the Year's Maximum Pensionable Earnings in effect each year. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(2) Pensionable salary excludes the amounts described in clauses (1) (a) to (h) whether paid under a contract or gratuitously by an employer. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(3) The pensionable salary of a member who receives board or lodging related to employment in education shall be deemed to be such amount, having regard for the value of the board or lodging, as is determined by the administrator.

Idem

(4) The pensionable salary of a member who is entitled to a refund under s. 28 (overpayment) shall be reduced by the amount of remuneration for which the contributions could have been refunded, whether or not the refund is paid. (Last amended June 28, 1990 - Effective June 28, 1990)

Pensionable salary during statutory leave

(5) The pensionable salary of an active member who makes contributions for a statutory leave which began prior to the 1st day of September, 2010 is the remuneration that the member's employer reports that the member would have earned if the member had not taken a statutory leave. (Last amended December 30, 2009 - Effective September 1, 2010)

Pensionable salary during WSIB

(5a) The pensionable salary of an active member who is receiving payments for loss of earnings under the *Workplace Safety and Insurance Act* is the remuneration that the member's employer reports that the member would have earned if the member had not been receiving such payments under the *Workplace Safety and Insurance Act*. (Last amended September 8, 2006 – Effective September 1, 2006)

Pensionable salary during sick leave

(5b) For the purposes of subsection 10 (2e), the pensionable salary of an active member who is receiving sick leave payments is the remuneration that the member's employer reports that the member would have earned if not for the sick leave. (Last amended December 19, 2012 – Effective September 1, 2012)

Pensionable salary during unpaid professional activity days

(5c) For the purposes of subsection 10 (2f), the pensionable salary of an active member who is subject to unpaid professional activity days is the remuneration that the member's employer reports that the member would have earned if not for the unpaid professional activity days. (Last amended April 2, 2013 – Effective September 1, 2012)

Pensionable salary during a short absence

(5d) For the purposes of subsection 10 (2g), the pensionable salary of an active member who is on a short absence is the remuneration that the member's employer reports that the member would have earned if not for the short absence. (Last amended July 21, 2014 – Effective September 1, 2014)

Pensionable salary

(6) Revoked. (Last amended June 29, 1994 - Effective January 1, 1992)

Deferred salary leave plans

12a. (1) This section applies to a member who participates in a deferred salary leave plan entered into in writing between the member and his or her employer. (Last amended April 2, 2001- Effective September 1, 2001)

Deemed pensionable salary

(2) Despite subsection 12 (1) the pensionable salary of a member referred to in subsection (1) is the amount that the member's employer advises the administrator would have been paid to the member but for the member's participation in a deferred salary leave plan. (Last amended June 29, 1994 - Effective January 1, 1992)

Coming into force

(3) Revoked. (Last amended April 2, 2001- Effective September 1, 2001)

Pensionable salary re active member on LTIP

13. (1) The pensionable salary of an active member on LTIP is the remuneration that the member's employer reports the member would have earned if the member had worked throughout the school year in which the member began receiving LTIP benefits. (Last amended April 2, 2001- Effective September 1, 2001)

Idem

(2) Revoked. (Last amended April 2, 2001- Effective September 1, 2001)

Idem

(3) Despite subsection (1), for the period of September 1, 2001 to August 31, 2011, the pensionable salary of an active member as described in subsection 6 (1a) shall be the greater of:

(a) the pensionable salary determined in accordance with subsection (1) and increased in accordance with subsections 15 (4) to (4c); and

(b) the pensionable salary determined in accordance with subsection 12 (5a).

(Last amended August 4, 2011 – Effective September 1, 2011)

Pensionable salary re purchases of credit prior to September 1, 2010

14. (1) The pensionable salary of a member who purchases credited service under section 94, 95 or 96 for an absence is the amount of remuneration that, in the opinion of the member's employer, the member would have earned had he or she not taken the absence. (Last amended April 2, 2001 - Effective September 1, 2001)

Idem re pensionable salary for purchases on or after September 1, 2010

(1a) Despite subsection (1), the pensionable salary for a purchase of credited service under section 94, 95 or 96, where the member has not completed payment prior to the 1st day of September, 2010 for the entire eligible absence period, is an amount based upon the annual pensionable salary that, in the opinion of the administrator, the member earned prior to the start of the absence as adjusted in accordance with this section. (Last amended October 19, 2012 – Effective September 1, 2010)

Adjusted pensionable salary

(1b) For the purposes of subsection (1a), a member’s pensionable salary for an absence is adjusted after the school year in which the member began the absence by multiplying the pensionable salary for that year by the accumulated adjustment ratio determined in the manner set out in subsection (1d). (Last amended June 20, 2012 – Effective September 1, 2010)

Exception

(1c) Despite subsection (1b), where an absence begins on the first day of the member’s school year, the pensionable salary is adjusted in the manner set out in subsection (1b) beginning with the school year in which the member began the absence. (Last amended December 30, 2009 - Effective September 1, 2010)

Accumulated adjustment ratio

(1d) A member's accumulated adjustment ratio for purposes of subsection (1b) is the product of the basic ratio for each school year beginning with the school year following the school year in which the member began the absence and ending with the school year for which the accumulated adjustment ratio is being determined. (Last amended December 30, 2009 - Effective September 1, 2010)

Exception

(1e) Despite subsection (1d), where an absence begins on the first day of the member’s school year, the member's accumulated adjustment ratio for purposes of subsection (1b) is the product of the basic ratio for each school year beginning with the school year in which the member began the absence and ending with the school year for which the accumulated adjustment ratio is being determined. (Last amended December 30, 2009 - Effective September 1, 2010)

Basic ratio

(1f) The basic ratio for a school year referred to in subsections (1d) and (1e) is a factor provided by the Minister. (Last amended December 30, 2009 - Effective September 1, 2010)

Alternative basic ratio

(1g) In the event that the basic ratio described in subsection (1f) is not provided by the Minister before the date that the cost for the purchase of credited service is calculated, the basic ratio for a school year referred to in subsections (1d) and (1e) is the ratio expressed to three decimal places that the average for the consumer price index over the last twelve months of the twenty-four month period ending with the 31st day of July in the preceding school year bears to the average for the consumer price index over the first twelve months of that period. (Last amended December 30, 2009 - Effective September 1, 2010)

Idem

(1h) For the purposes of subsection (1g), "consumer price index" means the Consumer Price Index for Canada as published by Statistics Canada under the authority of the *Statistics Act* (Canada). (Last amended December 30, 2009 - Effective September 1, 2010)

Transition

(1i) Revoked. (Last amended October 19, 2012 - Effective September 1, 2010)

Grandfathering the portion of an absence previously considered complete

(1j) Despite subsection (1a), where, in the opinion of the administrator, payment was considered to be complete as of the 1st day of September, 2010 for a portion of the entire eligible absence period, the pensionable salary for that portion of the absence is determined in accordance with subsection 14(1). (Last amended October 19, 2012 - Effective September 1, 2010)

Idem re pensionable salary for the remaining portion of an employer approved leave

(1k) Despite subsection (1a), where, in the opinion of the administrator, payment was considered to be complete as of the 1st day of September, 2010 for a portion of the entire eligible absence period, the pensionable salary for any remaining subsequent portion of the entire eligible absence period that is an employer-approved leave is determined in accordance with subsection (1j), and adjusted, with necessary modifications, in accordance with subsections (1b) to (1h). (Last amended October 19, 2012 - Effective September 1, 2010)

Idem

(2) The pensionable salary of a member who purchases credited service under section 103 is the amount of the member's remuneration for employment during the applicable period.

(3) The pensionable salary described in subsection 14(2) shall not be used in the calculation of the average salary of the member. (Last amended June 29, 1994-Effective January 1, 1992)

Average salary

15. (1) The average salary of a member,

(a) with more than five years' qualifying service is the average of the member's annual pensionable salary for the five school years during which it was highest; and

(b) with five years' or less qualifying service is the average of the member's annual pensionable salary. (Last amended October 10, 1995 - Effective September 1, 1995)

Part-time or occasional employee

(2) For the purpose of determining the average salary of a member employed more than ten days but less than a full-time school year or an active member on LTIP whose LTIP payments are based upon a less than full-time salary, the annual pensionable salary of the member is calculated using the formula,

$$(A/B) \times C$$

in which,

"A" is the amount of the member's pensionable salary for the school year,

"B" is the lesser of,

(a) the number of days of credited service accumulated by the member during the school year, and

(b) the number of days in a full-time school year, and

"C" is the number of days in a full-time school year except,

(a) in the first year of the member's employment in education when it is the number of days between the first day worked by the member and the end of the school year, or

(b) in the final year of active membership when it is the number of days in a full-time school year between the beginning of the school year and the date the member's pension or the pension of a survivor of the member begins. (Last amended February 20, 1997 - Effective January 1, 1997)

Employee working less than full final year

(2a) For the purpose of determining the average salary of a member employed more than ten days but less than a full-time school year during his or her final year of active membership, the pensionable salary of the member as determined under subsection (2) for that final year shall be increased by an amount calculated using the formula,

$$A \times B/C$$

in which,

"A" is the member's pensionable salary for the school year in which it was sixth highest,

"B" is the number of days in a full-time school year between the date the member's pension or the pension of a survivor of the member begins and the end of the school year, and

"C" is the number of days in a full-time school year. (Last amended February 20, 1997 - Effective January 1, 1997)

Purchases of credit

(2b) Subsections (2) and (2a) shall apply, with necessary modifications, to credited service accumulated by a member for a school year under section 94 or 95 in respect of periods on or after the 1st day of September, 2010, provided that the member has completed a purchase of the entire eligible absence period in respect of that school year. (Last amended August 4, 2011 – Effective September 1, 2010)

Restriction

(3) Revoked.

(a) Revoked.

(b) Revoked. (Last amended October 10, 1995 - Effective September 1, 1995)

Inflation adjusted pensionable salary

(4) For the purposes of this section, the pensionable salary for an active member on LTIP is increased after the school year in which the member began receiving LTIP benefits by multiplying the pensionable salary for that year, as determined under section 13, by the accumulated adjustment ratio determined in the manner set out in subsection (4a). (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(4a) A member's accumulated adjustment ratio for purposes of subsection (4) is the product by multiplication of the basic ratio for each school year beginning with the school year following the school year in which the member began receiving LTIP benefits and ending with the school year for which the accumulated adjustment ratio is being determined. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(4b) The basic ratio for a school year referred to in subsection (4a) is the ratio expressed to three decimal places that the average for the consumer price index over the last twelve months of the twenty-four month period ending with the 30th day of September in that school year bears to the average for the consumer price index over the first twelve months of that period. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(4c) For the purposes of subsection (4b), "consumer price index" means the Consumer Price Index for Canada as published by Statistics Canada under the authority of the *Statistics Act* (Canada). (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(4d) Subsections (4) to (4c) do not apply for the period of September 1, 2001 to August 31, 2011 in respect of a member who is an active member as described in subsection 6 (1a) and whose pensionable salary is determined in accordance with subsection 12 (5a). (Last amended August 4, 2011 – Effective September 1, 2011)

D. Transitional

Transitional re membership

16. (1) Every person who has credit in the Teachers' Superannuation Fund on the 31st day of December, 1989 and who is not entitled to an allowance under a predecessor of this Act becomes an active member of the pension plan upon completing one day of employment in education on or after the 1st day of January, 1990.

Idem, active member on LTIP

(2) Every person who was making contributions or on whose behalf contributions were being made on the 31st day of December, 1989 under an agreement referred to in section 4 of the *Teachers' Superannuation Act, 1983* or under a predecessor of that section is considered to be an active member on LTIP.

Transitional re credited service

17. Every active member shall be considered to have accumulated credited or qualifying service under the pension plan in an amount equal to the credited or qualifying service that he or she had accumulated under a predecessor of this Act. (Last amended October 10, 1995 - Effective September 1, 1995)

Re-employed pensioners

18. A re-employed pensioner making contributions under the pension plan or a predecessor of this Act on or after the 1st day of September, 1989 up to the 1st day of January, 1990 is entitled to a refund of contributions, if any, made in respect of the first ninety-five days or less of employment during that period.

PART III
CONTRIBUTIONS

A. Member Contributions

Amount of member's contributions

19. (1) Every active member who is required to contribute to the *Canada Pension Plan* or to the *Quebec Pension Plan* shall contribute for a year, for salary paid after 2011,

(a) 10.4 per cent of that portion of the member's pensionable salary up to and including the amount of the Year's Maximum Pensionable Earnings as prescribed under the *Canada Pension Plan*; and

(b) 12 per cent of that portion of the member's pensionable salary that exceeds the amount of the Year's Maximum Pensionable Earnings. (Last amended August 4, 2011 – Effective January 1, 2012)

Idem

(2) Every active member who is not required to contribute to the *Canada Pension Plan* or to the *Quebec Pension Plan* shall contribute 12 per cent of the member's pensionable salary for the year, for salary paid after 2011. (Last amended August 4, 2011 – Effective January 1, 2012)

Maximum amount of contributions, R.S.C. 1952, C. 148

(2a) If a member's contributions calculated under this section for a period after the 31st day of December, 1991 exceeds the lesser of the maximum contribution permitted under the *Income Tax Act* (Canada) and the maximum contribution determined by the actuary, it shall be reduced to an amount equal to the lesser maximum. (Last amended December 21, 2006 – Effective January 1, 2007)

Deemed required to contribute to CPP

(2b) An active member who at any time after the end of the month in which he or she attains the age of 65 years and before the end of the month in which he or she attains the age of 70 years receives a Canada Pension Plan retirement pension shall contribute for salary paid after 2011 the contributions set out in paragraphs (1) (a) and (b) if an election under paragraph 12 (1) (c) of the *Canada Pension Plan* is not in effect at the time of the salary payment. (Last amended June 20, 2012 – Effective January 1, 2012)

Pensionable salary

(3) Revoked. (Last amended October 23, 1991 - Effective October 23, 1991)

Additional contributions

(4) In addition to the contributions required under subsection (1) or (2), every active member shall contribute 2.0 per cent of the member’s pensionable salary for the year, for salary paid during the year 2007. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(5) In addition to the contributions required under subsection (1) or (2), every active member shall contribute 2.3 per cent of the member's pensionable salary for the year, for salary paid during the year 2008. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(6) In addition to the contributions required under subsection (1) or (2), every active member shall contribute 2.1 per cent of the member's pensionable salary for the year, for salary paid after 2008 but before 2012. (Last amended August 4, 2011 – Effective January 1, 2012)

Idem

(7) In addition to the contributions required under subsection (1), (2) or (2b), every active member shall contribute 0.4 per cent of the member's pensionable salary for the year, for salary paid during the year 2012. (Last amended June 20, 2012 – Effective January 1, 2012)

Idem

(8) In addition to the contributions required under subsection (1), (2) or (2b), every active member shall contribute 0.75 per cent of the member's pensionable salary for the year, for salary paid during the year 2013. (Last amended June 20, 2012 – Effective January 1, 2012)

Idem

(9) In addition to the contributions required under subsection (1), (2) or (2b), every active member shall contribute 1.1 per cent of the member's pensionable salary for the year, for salary paid after 2013 but before 2027. (Last amended June 20, 2012 – Effective January 1, 2012)

Contributions by members working more than full-time

19a. An active member who is employed on a full-time basis to work a full-time school year is not required to make a contribution for any employment during that school year in excess of a full-time school year. (Last amended June 28, 1990 - Effective June 28, 1990)

Member contributions during statutory leaves

19b. An active member shall, during a statutory leave which began prior to the 1st day of September, 2010, contribute the applicable amount set out in section 19 unless the member has notified the employer in writing that she or he elects not to participate in the pension plan during the statutory leave. (Last amended December 30, 2009 - Effective September 1, 2010)

Member contributions during statutory leaves on or after September 1, 2010

19c. A member shall, during a statutory leave which begins on or after the 1st day of September, 2010, contribute the applicable amount set out in section 94 unless the member has notified the employer in writing that she or he elects not to participate in the pension plan during the statutory leave. (Last amended December 30, 2009 - Effective September 1, 2010)

Collection of member contributions

20. (1) The employer of an active member shall deduct the amount the member is required to contribute under section 19 from the salary paid to the member.

Transfer of amount deducted

(2) An employer shall deliver to the administrator or deposit to the account of the pension fund on or before the last day of each month in which a member's salary is paid the amount deducted for the member's contribution.

Interest payable

(3) An employer shall pay interest on amounts in arrears from the date the payment is due to the day before it is made, calculated at the standard interest rate. (Last amended September 8, 2006 - Effective January 1, 2003)

Idem

(3a) An employer shall pay additional interest at the rate of 4 per cent compounded annually on amounts in arrears after the last day of the month following the month in which the employer billing occurs. (Last amended September 8, 2006 – Effective January 1, 2003)

Report to administrator

(4) An employer shall make such reports to the administrator as the administrator requires in respect of member contributions.

Member contributions not to be collected

(5) An employer shall not deduct from the salary paid to an active member employed on a full-time basis for a full-time school year an amount greater than the contributions payable under section 19 by an employee who works a full-time school year unless the member directs the employer to do so. (Last amended June 28, 1990 - Effective June 28, 1990)

Idem

(6) An employer who is provided with evidence that an active member is employed on a full-time basis for a full-time school year by another employer shall not make any deduction from the salary paid to that member for contributions under section 19 unless the member directs the employer to do so. (Last amended June 28, 1990 - Effective June 28, 1990)

Status of contributions

(7) A contribution which an active member directs his or her employer to deduct under subsection (5) or (6) is considered to be a required contribution for the purpose of sections 25 and 26. (Last amended June 28, 1990 - Effective June 28, 1990)

Underpayment of contributions

20a. (1) A member who has for any year contributed an amount less than that calculated under section 19 shall, upon being notified of the amount of the undercontribution, pay as a lump sum an amount equal to the undercontribution. (Last amended February 28, 1992 - Effective January 1, 1992)

Interest

(2) A member referred to in subsection (1) shall pay interest calculated at the standard rate on the amount of the undercontribution from the day the member is notified to the day before the undercontribution is paid. (Last amended February 28, 1992 - Effective January 1, 1992)

Contributions re active members on LTIP

21. (1) The amount of the required contribution for an active member on LTIP is,

(a) 6.9 per cent of the pensionable salary of a member who becomes disabled before the 1st day of January, 1991, and

(b) 8.9 per cent of the pensionable salary of a member who becomes disabled after the 31st day of December, 1990,

except that payment of the required contribution is waived for a member who becomes disabled after the 31st day of August, 2001. (Last amended April 2, 2001 – Effective September 1, 2001)

Inflation adjusted pensionable salary

(2) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(2a) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(2b) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem S.C. 1970 - 1971 - 1972 c. 15

(2c) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

(2d) If a member's contribution calculated under subsection (1) for a period after the 31st day of December, 1991 exceeds the lesser of the maximum contribution to a registered pension plan permitted under the *Income Tax Act* (Canada) and the maximum contribution determined by the actuary, it shall be reduced to an amount equal to the lesser maximum. (Last amended June 1, 1995 - Effective June 1, 1995)

Restriction re election

(3) Revoked. (Last amended October 23, 1991 - Effective October 23, 1991)

Notice of status

(4) An active member on LTIP shall give notice on the first day of each school year to his or her employer or former employer that the member continues to be an active member on LTIP.

Minister's payments re active member on LTIP

22. The contributions required under subsection 21 (1) from an active member on LTIP who is receiving benefits under a long term income protection plan established under the *Public Service Act* shall be paid on behalf of the member by the Minister.

Collection re active member on LTIP

23. (1) The required contribution for an active member on LTIP shall be paid to the person who was his or her employer on the date of disability.

Idem

(2) Payments under subsection (1) must be made on or before the fifteenth day of the month following the month in which each payment under the long term income protection agreement is made to the member.

Increased contributions

(3) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Transfer of contribution

(4) An employer to whom a payment in respect of an active member on LTIP is to be made under this section shall, whether or not the payment is made, deliver to the administrator on or before the last day of each month in which the member's LTIP payment is required the amount of the member's required contribution. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(5) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Interest payable

(6) Interest is payable on payments in arrears made to the employer or by the employer from the date the payment is due to the day before it is made, calculated at the standard interest rate plus 4 per cent. (Last amended February 28, 1992 - Effective January 1, 1992)

Cause of action

(7) An employer may maintain an action for the recovery of an amount paid to the administrator under subsection (4) if the employer has not received the corresponding payment of required contributions for an active member on LTIP.

Collection re member on statutory leave

23a. (1) An active member who has taken a statutory leave which began prior to the 1st day of September, 2010 and has not notified his or her employer in writing that she or he elects not to participate in the pension plan during the leave, shall pay the member's contribution to the member's employer on or before the normal pay day of the employer. (Last amended December 30, 2009 - Effective September 1, 2010)

(2) An employer to whom a payment in respect of an active member referred to in subsection (1) is to be made shall, whether or not the payment is made, deliver to the administrator on or before the last day of each month of the member's statutory leave the amount of the member's required contribution. (Last amended October 23, 1991 - Effective October 23, 1991)

(3) Interest is payable on payments due from the employer which are in arrears from the date the payment is due to the day before it is made, calculated at the standard interest rate. (Last amended May 5, 2010 – Effective January 1, 2003)

(3a) An employer shall pay additional interest at the rate of 4 per cent compounded annually on amounts in arrears after the last day of the month following the month in which the employer billing occurs. (Last amended May 5, 2010 – Effective January 1, 2003)

(4) An employer may maintain an action for the recovery of an amount paid to the administrator together with interest thereon at the standard interest rate under this section if the employer has not received the corresponding payment of required contributions from the active member who has taken a statutory leave. (Last amended October 23, 1991 - Effective October 23, 1991)

B. Employer Contributions

Liability for contributions

24. (1) Employer contributions in respect of an active member employed as described in subsection 2 (1) shall be paid by the Minister.

Idem

(2) Subsection (1) does not apply with respect to any contribution in relation to which the member is required under this pension plan to make the contribution that would otherwise be made by the Minister.

Idem

(3) Employer contributions in respect of an active member employed as described in subsection 2 (2) or section 7, 8 or 9 shall be paid by the employer of the member.

Idem

(4) Employer contributions in respect of an active member on LTIP shall be paid by the person making the employer contributions in respect of the member immediately before the date of disability.

(5) No employer contribution, other than an eligible contribution under the *Income Tax Act* (Canada), shall be made to the plan. (Last amended June 29, 1994 - Effective January 1, 1992)

Contributions by the Minister

25. (1) The Minister shall contribute in each year an amount equal to the required contributions made during the year before the preceding year by or on behalf of those members for whom the Minister is required to make employer contributions.

Idem, active members on LTIP

(2) In addition to the amount required under subsection (1), the Minister shall contribute in each year, in respect of the year before the preceding year, 4 per cent of the pensionable salaries of active members on LTIP who become disabled before the 1st day of January, 1991. (Last amended June 3, 2009 – Effective January 1, 2010)

Idem

(2a) In addition to the amounts required under subsections (1) and (2), the Minister shall contribute in each year, in respect of the year before the preceding year:

(a) an amount equal to the required contributions that would have been made by or on behalf of active members on LTIP who became disabled after the 31st day of August, 2001, but for the waiver in subsection 21(1); and

(b) an amount equal to the required contributions that would have been made by or on behalf of active members on LTIP to increase the member's pensionable salary under section 15, if contributions were required on such increase in pensionable salary. (Last amended June 3, 2009 – Effective January 1, 2010)

Additional contributions

(2b) In respect of the year 2008, the Minister shall contribute, in addition to the amounts required under this section, an amount equal to 0.8 per cent of the pensionable salaries of active members in respect of whom required contributions were made during that year in accordance with section 19 and for whom the Minister is required to make employer contributions. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(2c) In respect of the year 2008, the Minister shall contribute, in addition to the amounts required under this section, an amount equal to 0.8 per cent of the pensionable salaries of members who purchase credit under the pension plan in respect of that year and for whom the Minister is required to make employer contributions. (Last amended December 21, 2007 – Effective January 1, 2007)

Idem

(2d) In addition to the amounts required under this section, the Minister shall contribute in each year a proportional amount of the difference, as calculated by the administrator, between the inflation adjustments that were included in pensions, commuted values and lump sum payments (other than reciprocal transfers) that were paid in the year before the preceding year and the inflation adjustments that would have been included in such benefits but for the combined application of subsections 80(3a) and (3b). The Minister's proportional amount shall be based on the pensionable salaries of active members for whom the Minister is required to make employer contributions, in respect of the year before the preceding year, as a percentage of the pensionable salaries of all active members for that year. (Last amended September 17, 2013 - Effective January 1, 2014)

Idem

(2e) For greater certainty, if inflation adjustments have ever been made in accordance with subsection 80(3d), the Minister's contributions pursuant to subsection 25(2d) shall be determined as if inflation adjustments had never been made in accordance with subsection 80(3d). (Last amended September 17, 2013 - Effective January 1, 2014)

Due date

(3) The Minister's contribution is due on the first business day following the 1st day of January in each year and not as required under the *Pension Benefits Act*. (Last amended June 28, 1990 - Effective June 28, 1990)

Interest payable

(4) Interest on the Minister's contribution is payable for the period beginning on the 1st day of June of the year that was two years before the date on which a payment is due and ending on the day before the payment is made, calculated at the standard interest rate in effect on that 1st day of June.

(4a) Despite subsections (3) and (4), $500,000,000 of the Minister's contribution due on January 4, 1993 shall be made on April 1, 1993 with interest at the rate of 11.25% per annum applied from January 4, 1993 to March 31, 1993. (Last amended May 29, 1992 - Effective May 29, 1992)

Idem, transitional

(5) Interest payable in respect of a period before the 1st day of January, 1990 shall be calculated,

(a) up to that date, in accordance with the *Teachers' Superannuation Act, 1983;*

(b) on and after that date, at the standard interest rate in effect on the 1st day of January, 1990.

Delivery

(6) The Minister shall deliver contributions to the administrator or deposit them to the account of the pension fund.

Order of Lieutenant Governor in Council

(7) To reduce the time between the date of payment mentioned in subsection (3) and the payment of contributions by or on behalf of those members for whom the Minister is required to make employer contributions, the Lieutenant Governor in Council may, despite subsections (1) and (4), by order require the Minister to make payments for such number of months in the preceding year as are specified in the order in respect of contributions in those months by or on behalf of those members for whom the Minister is required to make employer contributions.

Idem

(8) An order made under subsection (7) shall revise the period of time mentioned in subsection (1) in respect of which contributions by the Minister are computed so that it reflects the additional contributions required to be made by the Minister.

Idem

(9) An order under subsection (7) shall adjust the date from which interest is to be calculated under subsection (4) to reflect the reduced time between the last month in which contributions are made by or on behalf of those members for whom the Minister is required to make employer contributions and the month when the Minister pays an amount equal to those contributions.

Contributions by employers

26. (1) An employer shall contribute in each month an amount equal to the required contributions made during the month by or on behalf of those members for whom the employer is required to make employer contributions.

Idem, active members on LTIP

(1a) In addition to the amount required under subsection (1), an employer shall contribute:

(a) an amount equal to the required contributions that would have been made by or on behalf of active members on LTIP who became disabled after the 31st day of August, 2001, but for the waiver in subsection 21(1); and

(b) an amount equal to the required contributions that would have been made by or on behalf of active members on LTIP to increase the member's pensionable salary under section 15, if contributions were required on such increase in pensionable salary. (Last amended April 2, 2001 – Effective September 1, 2001)

Additional contributions

(1b) In respect of the year 2008, an employer shall contribute, in addition to the amounts required under this section, an amount equal to 0.8 per cent of the pensionable salaries of active members in respect of whom required contributions are made during that year in accordance with section 19 and for whom the employer is required to make employer contributions. (Last amended December 21, 2006 – Effective January 1, 2007)

Idem

(1c) In respect of the year 2008, an employer shall contribute, in addition to the amounts required under this section, an amount equal to 0.8 per cent of the pensionable salaries of members who purchase credit under the pension plan in respect of that year and for whom the employer is required to make employer contributions. (Last amended December 21, 2007 – Effective January 1, 2007)

Idem

(1d) In addition to the amounts required under this section, an employer shall contribute in each year a proportional amount of the difference, as calculated by the administrator, between the inflation adjustments that were included in pensions, commuted values and lump sum payments (other than reciprocal transfers) that were paid in the year before the preceding year and the inflation adjustments that would have been included in such benefits but for the combined application of subsections 80(3a) and (3b). The employer's proportional amount shall be based on the pensionable salaries of active members for whom the employer was required to make employer contributions, in respect of the year before the preceding year, as a percentage of the pensionable salaries of all active members for that year. (Last amended September 17, 2013 – Effective January 1, 2014)

Idem

(1e) For greater certainty, if inflation adjustments have ever been made in accordance with subsection 80(3d), an employer's contributions pursuant to subsection 26(1d) shall be determined as if inflation adjustments had never been made in accordance with subsection 80(3d). (Last amended September 17, 2013 - Effective January 1, 2014)

Due date

(2) An employer's contribution is due on the last day of the month.

Idem

(2a) Notwithstanding subsection (2), an employer's contribution under subsection (1d) is due on the first business day following the 1st day of January in each year. (Last amended June 3, 2009 – Effective January 1, 2010)

Interest payable

(3) Interest on an employer's contribution is payable from the date the payment is due to the day before it is made, calculated at the standard interest rate. (Last amended September 8, 2006 - Effective January 1, 2003)

Idem

(3a) An employer shall pay additional interest at the rate of 4 per cent compounded annually on amounts in arrears after the last day of the month following the month in which the employer billing occurs. (Last amended September 8, 2006 – Effective January 1, 2003)

Idem

(3b) Notwithstanding subsection (3), interest on an employer's contribution under subsection (1d) is payable from June 1st of the year before the preceding year to the day before the payment is made, calculated at the standard interest rate in effect on that June 1st. (Last amended June 3, 2009 - Effective January 1, 2010)

Delivery

(4) An employer shall deliver contributions to the administrator or deposit them to the account of the pension fund.

C. Refund of Overpayments

Refund error

27. The administrator shall refund contributions or other payments made in error or not permitted under the pension plan, together with interest, if the administrator received the contributions or other payments.

Overpayment of contributions

28. (1) This section applies to an active member who,

(a) (i) works more than a full-time school year during the school year, or

(ii) was employed on an occasional basis in addition to an absence purchased on a contributions plus interest basis in accordance with section 94; and (Last amended April 2, 2001 – Effective September 1, 2001)

(b) has made contributions greater than those required under s. 19 of a member working a full-time school year. (Last amended June 28, 1990 - Effective June 28, 1990)

Idem

(2) An active member described in subsection (1) is entitled to a refund of contributions calculated in accordance with subsection (4). (Last amended June 28, 1990 - Effective June 28, 1990)

Refund to employer

(3) Despite section 78 of the *Pension Benefits Act*, a person who has made employer contributions in respect of a member described in subsection (1) is entitled to a refund of employer contributions equal to the amount of the refund to which the member is entitled. (Last amended June 28, 1990 - Effective June 28, 1990)

Amount of refund

(4) The refund of contributions is calculated using the formula,

$$\mathbf{(A + B + C \ldots) \times N}$$

in which, "A", "B", "C" … is the series in which each variable is the amount of salary paid to the member at each different rate of salary earned by the member during the school year and/or the amount of salary attributable to the credit purchase in accordance with section 94, beginning with the lowest rate of salary and ending with the highest provided that the number of days for which salary is accumulated by the addition of variables does not exceed the number of days in excess of a full-time school year for which the member makes contributions, and

"N" is the per cent referred to in clause 19 (1) (b), plus any additional per cent of salary that was paid by the member in accordance with section 19 in respect of the salary being refunded, expressed as a decimal fraction. (Last amended December 21, 2006 – Effective January 1, 2007)

(4a) For the purposes of subsection (4), credit purchased on an actuarial cost basis, or transferred into the plan in accordance with section 104, will be deemed to be the highest rate of salary. (Last amended December 20, 1999 - Effective September 1, 1998)

Interest payable

(5) Interest is payable on a refund of contributions from the last day of the school year until the day before it is paid. (Last amended February 28, 1992 - Effective January 1, 1992)

Lump sum

(6) A refund of contributions shall be paid as a lump sum. (Last amended June 28, 1990 - Effective June 28, 1990)

Refund, re-employed pensioners

29. Despite subsection 63 (4) of the *Pension Benefits Act*, a person described in subsection 46 (3) of the *Teachers' Superannuation Act, 1983* who became re-employed in education for less than twenty days between the 1st day of September, 1986 and the 31st day of August, 1989 is entitled to the refund described in that section.

PART IV
PAYMENTS UPON TERMINATION OF MEMBERSHIP

A. Vesting

Vesting of benefits

30. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Idem

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Payment of deferred pension

(3) A member who terminates membership in the pension plan on or after July 1, 2012 is entitled to a deferred pension calculated and paid in accordance with Part V. (Last amended June 19, 2012 – Effective July 1, 2012)

Payment of benefits upon death of member

(3a) Benefits payable in respect of a member who terminates membership in the pension plan as a result of the member's death on or after July 1, 2012, and before the commencement of payment of the deferred pension to which the member was entitled on the date of death, shall be calculated and paid in accordance with Part VII. (Last amended December 13, 2012 – Effective July 1, 2012)

Limit

(4) No person is entitled to more than one deferred pension in respect of the same period of employment.

Entitlement on termination of membership

31. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Idem

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Limitation

(3) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Idem, transitional

(4) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Rights of former members

32. Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

B. Refunds and Transfers

Refund re post-1986 contributions

33. Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund re pre-1987 contributions

34. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund at or after sixty-five years of age

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund re pre-1987 deferred pension

35. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Before reaching forty-five years of age

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

On or after forty-five years of age

(3) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Reduction in deferred pension

(4) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

50 per cent rule

36. (1) A member entitled to a deferred pension relating to employment after the 31st day of December, 1986 is entitled to a refund, paid in a lump sum, upon ceasing to be employed in education, of the amount by which the member's required contributions plus interest for the period after that date exceeds one half of the commuted value of the deferred pension for that period. (Last amended June 19, 2012 – Effective July 1, 2012)

Exclusion

(2) Subsection (1) does not apply with respect to a member's contributions and credited service for which no corresponding employer contribution is required under section 25 or 26. (Last amended June 1, 1995 - Effective June 1, 1995)

(3) A member who receives a refund under subsection (1), who elects to receive a deferred pension and who subsequently becomes re-employed in education or completes a purchase of credited service, must repay the refund together with interest thereon before the pension commences. (Last amended September 8, 2006 - Effective September 1, 2001)

(4) Revoked. (Last amended September 8, 2006 - Effective September 1, 2002)

(5) Revoked. (Last amended September 8, 2006 - Effective September 1, 2002)

(6) Revoked. (Last amended September 8, 2006 - Effective September 1, 2002)

(7) The member or survivor benefit, as the case may be, shall be actuarially reduced to reflect the unpaid portion of the repayment not completed under subsection (3) with interest thereon to the commencement date of the benefit. The actuarial reduction will be offset by any lump sum payment that would otherwise be payable to the member. (Last amended September 8, 2006 – Effective September 1, 2002)

Transfer re deferred pension

37. (1) A member entitled to a deferred pension who ceases to be employed in education is entitled to a transfer of the commuted value of the deferred pension, paid in a lump sum, to another retirement savings arrangement in accordance with section 42 of the *Pension Benefits Act* and to a refund or transfer of excess contributions, calculated under section 36, subject to the limitations of the *Income Tax Act* (Canada). (Last amended June 19, 2012 – Effective July 1, 2012)

(2) A member who is entitled to an immediate payment of a pension benefit is not entitled to a refund or transfer under this section. (Last amended September 8, 2006 – Effective June 1, 1995)

(3) A member who is entitled to a transfer under this section shall deliver a completed termination options application, including all supporting documentation, to the administrator within six months of the member’s termination of membership in the plan. (Last amended September 8, 2006 – Effective January 1, 1995)

(4) A termination options application completed after the deadline specified in subsection (3) shall be considered a new notification of intention to terminate membership in the plan and the member's entitlement to a transfer under this section shall be determined as of the new termination of membership date. (Last amended September 8, 2006 – Effective January 1, 1995)

Application for refund, etc.

38. (1) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Payment of refund

(2) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

PART V
RETIREMENT PENSIONS

A. Entitlement to Pension

One pension only

39. (1) No member is entitled to more than one retirement pension under the pension plan in respect of the same period of credited service.

Idem

(2) A member receiving a disability pension under the pension plan is not eligible to receive a retirement pension.

Retirement

(3) No member is entitled to begin to receive a retirement pension or a disability pension while the member is employed in education until the end of the calendar year in which the member attains seventy-one years of age, or until such other time as is required under the *Income Tax Act* (Canada). (Last amended June 20, 2012 – Effective January 1, 2012)

Normal retirement date

40. The normal retirement date of a member is the first day of the month following the date on which the member reaches sixty-five years of age.

Entitlement to pension (2 year rule)

41. (1) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Commencement

(2) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Amount of pension (2 year rule)

(3) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Maximum pension payable, R.S.C. 1952, c. 148

(3a) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Payment, pre-1987 service

(4) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Limitation on pensions less than $2,400

(5) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Entitlement to pension (10 year rule), transitional

42. (1) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Commencement

(2) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Amount of pension (10 year rule)

(3) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Maximum pension payable, R.S.C. 1952, c. 148

(3a) Revoked. (Last amended June 19, 2012 – Effective July 1, 2012)

Entitlement to pension (immediate vesting)

42a. (1) A member who terminates membership in the pension plan on or after July 1, 2012 is entitled to receive a retirement pension for the member's lifetime calculated under subsection (3). (Last amended June 19, 2012 – Effective July 1, 2012)

Commencement

(2) A retirement pension under this section begins as of the member's normal retirement date. (Last amended June 19, 2012 – Effective July 1, 2012)

Amount of pension

(3) Subject to subsection (4), the amount of the retirement pension, before adjustment for inflation, is calculated using the formula,

$$\mathbf{(A \times B) - C}$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service, and

"C" is the amount, if any, calculated under section 81 (CPP reduction). (Last amended June 19, 2012 – Effective July 1, 2012)

Payment of pensions, predecessor Acts

(4) The retirement pension of a member who ceased to be employed in education prior to January 1, 1990 shall be calculated, with necessary modifications, in accordance with the terms of the *Teachers' Superannuation Act, 1983*, or a predecessor Act, and shall be paid out of the pension fund in accordance with the Act under which the member ceased to be employed in education. (Last amended June 19, 2012 – Effective July 1, 2012)

Maximum pension payable, R.S.C. 1952, c. 148

(5) If the amount of the retirement pension calculated under subsection (3) in respect of a period after the 31st day of December, 1991 is greater than the maximum pension payable by a registered pension plan under the *Income Tax Act* (Canada), it shall be reduced to an amount equal to the maximum. (Last amended June 19, 2012 – Effective July 1, 2012)

Limitation on pensions less than $2,400

(6) Subject to section 84, where the annual amount of the retirement pension calculated under subsection (3) or (4) is less than $2,400 the member is entitled to a pension in that lesser amount and not to a pension in the amount of $2,400 as provided for by Order in Council 1453/74. (Last amended June 19, 2012 – Effective July 1, 2012)

Exception

(7) Subsection (6) shall not apply to a member who has at least ten years of credited service in whole or in part before the 1st day of January, 1987 on the date he or she ceased to be employed in education. (Last amended June 19, 2012 – Effective July 1, 2012)

Limitation

(8) For greater certainty, subsection 76 (2) of the *Teachers' Superannuation Act, 1983* shall not apply to the retirement pension of a member who did not have at least ten years of credited service on the date he or she ceased to be employed in education. (Last amended June 19, 2012 – Effective July 1, 2012)

Entitlement to pension (special early retirement)

43. (1) A member who has accumulated at least that number of years of qualifying service that, when added to the member's age upon termination of employment in education, totals ninety years is entitled to a retirement pension for the member's lifetime calculated under subsection (4). (Last amended October 10, 1995 - Effective September 1, 1995)

(1a) A member who ceases to be employed in education on or after June 1, 1998, and who has accumulated at least that number of years of qualifying service that, when added to the member's age upon termination of employment in education, totals eighty-five years is entitled to a retirement pension for the member's lifetime calculated under subsection (4). (Last amended April 2, 2001 – Effective April 1, 2001)

Idem (35 year rule)

(2) A member who ceases to be employed in education after the 31st day of May, 1987 and before the 1st day of September, 1990 and who has thirty-five years of qualifying service is entitled to a retirement pension for the member's lifetime calculated under subsection (4). (Last amended October 10, 1995 - Effective September 1, 1995)

(2a) A member who has accumulated thirty-five or more years of credited service is entitled to a retirement pension for the member's lifetime calculated under subsection (4). (Last amended February 20, 1997 - Effective January 1, 1997)

Commencement

(3) A retirement pension under this section begins as of the beginning of the month following the date the member ceases to be employed in education or, at the election of the member, of any month thereafter that is not later than:

(a) the end of the calendar year in which the member attains seventy-one years of age, or

(b) such other time as is required under the *Income Tax Act* (Canada).

(Last amended June 20, 2012 – Effective January 1, 2012)

Amount of pension

(4) The amount of the retirement pension, before adjustment for inflation, is calculated using the formula,

$$(A \times B) - C$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service, and

"C" is the amount, if any, calculated under section 81 (CPP reduction).

Maximum pension payable, R.S.C. 1952, c. 148

(4a) If the amount of the retirement pension calculated under subsection (4) in respect of a period after the 31st day of December, 1991 is greater than the maximum pension payable by a registered pension plan under the *Income Tax Act* (Canada), it shall be reduced to an amount equal to the maximum. (Last amended February 28, 1992 - Effective January 1, 1992)

Early retirement option

44. (1) A member entitled to a deferred pension under section 42a may elect to begin to receive a retirement pension on the first day of any month that is ten years before the member's normal retirement date. (Last amended June 19, 2012 – Effective July 1, 2012)

Idem

(1a) A member who ceases to be employed in education on or after June 30, 2001 and who is entitled to a deferred pension under section 42a may elect to begin to receive a retirement pension on the first day of any month that is within fifteen years of the member's normal retirement date. (Last amended June 19, 2012 – Effective July 1, 2012)

Amount of early retirement pension

(2) The amount of the annual retirement pension, before adjustment for inflation, of a member who elects early retirement under subsection (1) and who elects to begin to receive the pension on the first day of the month following the later of: the cessation of employment in education; or the last day of credited service in the plan, shall be calculated using the formula,

$$[A \times B \times (1 - C)] - D$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service,

"C" is an amount equal to the lesser of,

(a) 0.05 times the number of years by which the member's age is less than sixty-five on the date the pension is to begin, and

(b) 0.025 times the difference between ninety and the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension is to begin, and

"D" is the amount, if any, calculated under section 81 (CPP reduction).

"C" in the above formula shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended June 19, 2012 – Effective July 1, 2012)

Maximum pension payable, R.S.C. 1952, c. 148

(2a) Revoked. (Last amended February 20, 1997 - Effective January 1, 1997)

(2b) The amount of the annual retirement pension, before adjustment for inflation, for a member who ceases to be employed in education on or after June 1, 1998, where the member elects early retirement under subsection (1) or (1a) and elects to begin to receive the pension on the first day of the month following the later of: the cessation of employment in education; or the last day of credited service in the plan, shall be calculated using the formula set out in subsection (2) except that:

"C" is an amount equal to the lesser of,

(a) 0.05 times the number of years by which the member's age is less than sixty-five on the date the pension is to begin, and

(b) 0.025 times the difference between eighty-five and the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension is to begin,

however, "C" shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended April 2, 2001 – Effective April 1, 2001)

(3) The amount of the annual retirement pension, before adjustment for inflation, of a member who elects early retirement under subsection (1) on a deferred pension shall be calculated using the formula,

$$[A \times B \times (1 - C)] - D$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service,

"C" is an amount equal to the lesser of,

(a) 0.05 times the number of years by which the member's age is less than sixty-five on the date the pension is to begin, and

(b) 0.05 times the difference between ninety and the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension is to begin, and

"D" is the amount, if any, calculated under section 81 (CPP reduction).

"C" in the above formula shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended June 19, 2012 – Effective July 1, 2012)

(3a) The amount of the annual retirement pension, before adjustment for inflation, for a member who ceases to be employed in education on or after June 1, 1998, where the member elects early retirement under subsection (1) or (1a) on a deferred pension shall be calculated using the formula set out in subsection (3) except that:

"C" is an amount equal to the lesser of,

(a) 0.05 times the number of years by which the member's age is less than sixty-five on the date the pension is to begin, and

(b) 0.05 times the difference between eighty-five and the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension is to begin,

however, "C" shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended April 2, 2001 – Effective April 1, 2001)

Maximum pension payable, R.S.C. 1952, c. 148

(4) If the amount of the retirement pension determined under subsection (2), (2b), (3), (3a) or (5), in respect of a period after the 31st day of December, 1991 is greater than the maximum pension payable by a registered pension plan under the *Income Tax Act* (Canada) after taking into account the reduction (if any) on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada) it shall be reduced to an amount equal to such maximum. (Last amended May 27, 1998 - Effective June 1, 1998)

Commuted value

(5) Despite subsections (3) and (3a), the commuted value of the retirement pension received on early retirement shall be not less than the commuted value of the retirement pension to which the member would be entitled on the normal retirement date based upon the member's credited service up to the early retirement date. (Last amended May 27, 1998 - Effective June 1, 1998)

Postponed pension option

45. (1) A member may elect to begin to receive his or her retirement pension in any month after the member's normal retirement date, but not later than:

(a) the end of the calendar year in which the member attains seventy-one years of age, or

(b) such other time as is required under the *Income Tax Act* (Canada).

(Last amended June 20, 2012 – Effective January 1, 2012)

Amount of late retirement pension

(2) The amount of the annual retirement pension, before adjustment for inflation, of a member who elects late retirement as described in subsection (1) is calculated using the formula,

$$\mathbf{(A \times B) - C}$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service, and

"C" is the amount, if any, calculated under section 81 (CPP reduction).

(2a) If the amount of the retirement pension calculated under subsection (2) in respect of a period after the 31st day of December, 1991 is greater than the maximum pension payable by a registered pension plan under the *Income Tax Act* (Canada), it shall be reduced to an amount equal to the maximum. (Last amended June 29, 1994 - Effective January 1, 1992)

Re-employed pensioner election

46. (1) Prior to commencing re-employment for the first time after commencement of pension, a pensioner may elect to become an active member for the purpose of a pension recalculation in accordance with subsection (2), in which case the pension is suspended immediately upon the re-employment. (Last amended October 23, 2008 – Effective January 1, 2009)

Recalculation of pension

(2) If a re-employed pensioner accumulates one year or more of credited service after becoming an active member, other than by means of a purchase of credited service or by the annualization of a partial year of credited service under section 11, and, if the re-employed pensioner makes an application to the administrator, the amount of the pensioner's retirement pension shall be recalculated in accordance with the terms of the pension plan in force on the date of the application.

(2a) A re-employed pensioner making application under subsection (2) shall repay any refund previously made under section 36 together with interest thereon before the pension commences. (Last amended April 15, 1998 - Effective June 1, 1995)

(2b) Revoked. (Last amended September 8, 2006 – Effective September 1, 2002)

(2c) Revoked. (Last amended September 8, 2006 – Effective September 1, 2002)

(2d) Revoked. (Last amended September 8, 2006 – Effective September 1, 2002)

(2e) The member or survivor benefit, as the case may be, shall be actuarially reduced to reflect the unpaid portion of the repayment not completed under subsection (2a) with interest thereon to the commencement date of the benefit. The actuarial reduction will be offset by any lump sum payment that would otherwise be payable to the member. (Last amended September 8, 2006 – Effective September 1, 2002)

Exception

(3) A re-employed pensioner who does not accumulate one year of credited service after becoming an active member is entitled when the re-employment ceases,

(a) to the resumption of the retirement pension to which the pensioner was entitled immediately before becoming re-employed; and

(b) to the refund of the member's required contributions, together with interest thereon, made during the re-employment.

Pension suspension

(3a) Except for a pensioner whose pension is suspended immediately under subsection (1), no retirement pension is payable to a re-employed pensioner as of the month following the member's fifty-first day of re-employment in a school year. (Last amended May 6, 2010 – Effective September 1, 2012)

Pension resumption

(3b) A re-employed pensioner whose pension is suspended in accordance with subsection (3a) is entitled, when the re-employment ceases, to the resumption of the retirement pension to which the pensioner was entitled immediately before becoming re-employed. (Last amended October 23, 2008 – Effective January 1, 2009)

Notice of re-employment

(3c) A re-employed pensioner shall notify the administrator promptly upon exceeding the limits under subsection (3a). (Last amended October 23, 2008 – Effective January 1, 2009)

Reporting of re-employment

(3d) An employer shall report to the administrator any service provided to the employer by a re-employed pensioner. (Last amended May 6, 2010 – Effective September 1, 2012)

Idem

(3e) At the request of the administrator, a re-employed pensioner shall report to the administrator the number of days, if any, that the member provides services to an employer as a re-employed pensioner. If the member does not report within a reasonable time after the request, the administrator shall cease to pay the pension until the report is given. (Last amended May 6, 2010 – Effective September 1, 2012)

Repayment

(4) A re-employed pensioner who receives pension payments to which the pensioner is not entitled shall repay the amount so received, together with interest thereon, before becoming entitled to further payments under the pension plan.

"Re-employed pensioner" not applicable

(5) The term "re-employed pensioner" shall not include a member who provides services, other than as a teacher, to a ministry of the Government of Ontario other than the Ministry of Education. (Last amended May 6, 2010 – Effective September 1, 2010)

Idem

(6) The term "re-employed pensioner" shall not include a member who has been providing services, other than as a teacher, under contract to the Ministry of Education since before September 1, 2010, until the earlier of:

(a) the renewal of such contract, if applicable, or

(b) September 1, 2015.

(Last amended May 6, 2010 – Effective September 1, 2010)

B. Payment of Retirement Pensions

Application for retirement pension

47. (1) A member who wishes to begin receiving a retirement pension shall apply to the administrator.

Deemed application

(2) A member who does not apply to begin receiving a retirement pension shall be deemed to do so on November 30th of the calendar year in which the member attains seventy-one years of age, or at such other time as is required under the *Income Tax Act* (Canada). (Last amended June 20, 2012 – Effective January 1, 2012)

Payment of pension

48. (1) The administrator shall begin payment of a member's retirement pension not later than the later of,

(a) the month following the month in which the member ceases to be employed in education; or

(b) the month following the month in which application for the pension is complete.

Monthly instalments

(2) The administrator shall pay a retirement pension in monthly instalments on the last day of the month.

Interest payable

(3) The administrator shall pay interest on late payments, from the first day of the month following the month in which the member's pension begins. (Last amended June 20, 2012 – Effective January 1, 2012)

Notice of re-employment

49. (1) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Failure to give notice

(2) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

Repayment of pension

(3) Revoked. (Last amended October 23, 2008 – Effective January 1, 2009)

PART VI
DISABILITY PENSIONS

A. Entitlement to Disability Pension

Entitlement to disability pension

50. (1) This section applies to a member with at least ten years of qualifying service who becomes disabled while employed in education and who, as a result of the disability, ceases before the normal retirement date to be employed in education. (Last amended October 10, 1995 - Effective September 1, 1995)

Full disability pension

(2) If the administrator finds that a member described in subsection (1) is incapable of further employment, the member is entitled to a full disability pension for the member's lifetime.

Partial disability pension

(3) If the administrator finds that a member described in subsection (1) is incapable of further employment in education, the member is entitled to a partial disability pension for the member's lifetime.

Eligibility

(4) A member who has previously terminated his or her membership and who returns to membership and purchases credited service for previous employment in education is not eligible to receive a disability pension until the member accumulates two additional years of credited service.

Idem

(5) Subsection 11 (2) (partial year) does not apply for the purpose of determining a member's accumulation of the two additional years of credited service under subsection (4).

Effect of re-employment

51. (1) A member receiving a full disability pension who becomes employed ceases to be entitled to a full disability pension.

Idem

(2) A member receiving a disability pension who becomes employed in education ceases to be entitled to a disability pension. (Last amended June 1, 1995 - Effective June 1, 1995)

Reduced partial disability pension

(3) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Application

(4) This section applies with respect to a member who is receiving a disability pension on or after the 1st day of January, 1990.

Amount of full disability pension

52. (1) The amount of the annual full disability pension, before adjustment for inflation, for a member is calculated using the formula,

$$\mathbf{(A \times B) - C}$$

in which,

"A" is 2 per cent of the member's average salary,

"B" is the number of years of the member's credited service under the plan, and

"C" is the amount, if any, calculated under section 81 (CPP reduction).

Amount of partial disability pension

(2) The amount of a partial disability pension, before adjustment for inflation, for a member is calculated using the formula,

$$\mathbf{[(A \times B)\ (1 - C)] - D}$$

in which,

"A" and "B" have the same meaning as in the formula for calculating the amount of a full disability pension,

"C" is an amount equal to 0.025 times the lesser of,

(a) the number of years by which the member's age on the date the pension begins is less than 65, and

(b) ninety minus the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension begins, and

"D" is the amount, if any, calculated under section 81 (CPP reduction).

"C" in the above formula shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended April 15, 1998 - Effective January 1, 1992)

(2a) The amount of a partial disability pension, before adjustment for inflation, for a member who ceases to be employed in education on or after June 1, 1998, is calculated using the formula set out in subsection (2), except that:

"C" is an amount equal to 0.025 times the lesser of,

(a) the number of years by which the member's age on the date the pension begins is less than sixty-five, and

(b) eighty-five minus the sum of,

(i) the number of years of the member's qualifying service determined under section 11, and

(ii) the member's age on the date the pension begins,

however, "C" shall not be less than the minimum reduction on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada). (Last amended April 2, 2001 – Effective April 1, 2001)

Maximum pension payable, R.S.C. 1952, c. 148

(2b) If the amount of the full or partial disability pension determined under either subsection (1), (2), or (2a), as applicable, in respect of a period after the 31st day of December, 1991 is greater than the maximum pension payable by a registered pension plan under the *Income Tax Act* (Canada) after taking into account the reduction (if any) on early retirement applicable to registered pension plans under the *Income Tax Act* (Canada), it shall be reduced to an amount equal to such maximum. (Last amended May 27, 1998 - Effective June 1, 1998)

Limitation

(3) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Amount of reduced partial disability pension

(4) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Resumption of disability pension

53. (1) Subject to subsection (2), if a member becomes re-employed in education and ceases to receive a disability pension under the pension plan or a predecessor Act, the member is entitled upon ceasing the re-employment to the resumption of the original disability pension without adjustment of the amount of the pension and to a refund of the member's contributions made during the period of re-employment, together with interest thereon. (Last amended June 1, 1995 - Effective June 1, 1995)

Idem

(2) A member described in subsection (1) who completes the equivalent of two years of full-time employment in education after becoming re-employed and then ceases to be so employed shall make a fresh application for a pension, and the terms of the pension plan on the date the application is made shall apply with respect to the member's entitlement to a pension.

(3) A member making application under subsection (2) shall repay any refund previously made under section 36 together with interest thereon before the pension commences. (Last amended September 8, 2006 – Effective September 1, 2006)

(4) The member or survivor benefit, as the case may be, shall be actuarially reduced to reflect the unpaid portion of the repayment not completed under subsection (3) with interest thereon to the commencement date of the benefit. The actuarial reduction will be offset by any lump sum payment that would otherwise be payable to the member. (Last amended September 8, 2006 – Effective September 1, 2006)

Change of disability status re survivor pension

54. (1) This section applies if a member receiving a partial disability pension dies while the administrator is considering whether the member is entitled to a full disability pension based upon fresh medical evidence concerning the member's disability. (Last amended February 28, 1992 - Effective January 1, 1992)

Determination by the administrator

(2) Having regard to the facts established at the date of the member's death, the administrator shall determine whether the member would have been entitled, immediately before the date of death, to a full disability pension.

Deemed receipt

(3) For the purpose of calculating the amount of a survivor pension, child's pension or beneficiary's pension, if the administrator determines that the member would have been entitled to a full disability pension, the member shall be deemed to have been receiving it on the date of death.

(4) Despite subsection 3, where the benefit otherwise payable to a survivor exceeds the maximum payable under the regulations of the *Income Tax Act* (Canada), the amount in excess shall not be paid. (Last amended June 29, 1994 - Effective January 1, 1992)

B. Payment of Disability Pension

Application for disability pension

55. (1) A member shall apply for a disability pension within two years after the date when the member ceases, as a result of the disability, to be employed in education.

Idem

(2) The administrator shall accept an application for a disability pension that is made after the time described in subsection (1) if the administrator is satisfied,

(a) that the delay in making the application resulted from a delay in diagnosing the disability; or

(b) that the member was unable, because of the effects of the disability, to make the application within the time described in subsection (1).

Proof of disability

(3) No application for a disability pension shall be considered by the administrator until the administrator has received,

(a) the certificate of a medical doctor licensed in Ontario designated by the administrator, certifying that the applicant became mentally or physically disabled while employed in education and indicating the nature and degree of the disability; and

(b) a report of the medical referee of the administrator containing such recommendations as the medical referee considers proper with regard to the granting of a disability pension to the applicant. (Last amended April 15, 1998 - Effective January 1, 1992)

Disability pension, predecessor Acts

56. (1) This section applies with respect to a person who ceased to be employed in education before the 1st day of January, 1990 as a result of a mental or physical incapacity and who did not apply for a disability allowance under a predecessor of this Act.

Application

(2) Section 55 applies with necessary modifications to an application by a person described in subsection (1).

Entitlement

(3) The person is entitled to a disability allowance determined in accordance with the *Teachers' Superannuation Act, 1983.*

Idem

(4) Clause 17 (1) (d) or 18 (1) (d) of the *Teachers' Superannuation Act, 1983* does not apply if the administrator accepts an application under subsection 55 (2).

Commencement of disability pension

57. (1) Subject to subsection (2), a member's disability pension shall begin as of the first day of the month following the month in which the member ceases to be employed in education.

Idem

(2) No disability pension shall begin as of a date earlier than one year before the date the administrator receives the completed application for the pension.

Reduced partial disability pension

(3) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Monthly instalments

(4) The administrator shall pay a disability pension in monthly instalments.

Due date

(5) Disability pension payments are due on the last day of the month.

Interest payable

(6) Interest shall be paid on overdue pension payments if the administrator does not begin paying a pension by the end of the month in which the member becomes entitled to receive it.

Interest payable

(7) Interest on each overdue monthly pension payment, calculated at the standard rate, shall be paid from the date the payment was due to the day before it was made. (Last amended February 28, 1992 - Effective January 1, 1992)

Evidence of medical condition

58. (1) The administrator may at any time require a member who is receiving a disability pension to furnish evidence, in such form as the administrator directs, of the member's mental or physical condition.

Failure to furnish evidence

(2) If the member fails to furnish evidence within a reasonable time that his or her condition continues to be of a nature that entitles the member to receive the disability pension, the administrator shall terminate payment of the pension.

Review by administrator

(3) If the administrator terminates payment of a full disability pension, the member may request the administrator to review the decision to terminate payment.

Idem

(4) If the administrator is satisfied upon reviewing a decision to terminate payment that the member is entitled to a disability pension under section 50 or 51, the administrator shall pay the disability pension.

Application

(5) This section does not apply with respect to a member who has reached normal retirement age.

Notice of re-employment

59. (1) A member receiving a disability pension shall notify the administrator in writing promptly upon becoming employed or changing employment.

Failure to give notice

(2) A member who fails to comply with subsection (1) is not entitled to receive a disability pension payment during a period when notice should have been given under that subsection.

Repayment of pension

(3) A member who receives pension payments to which the member is not entitled shall repay the amount so received, together with interest thereon, before becoming entitled to further payments under the pension plan.

PART VII
BENEFITS UPON DEATH

A. Upon the Death of a Member not Entitled to a Pension

Refund of contributions

60. Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund of post-1986 contributions

60a. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Application

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund of pre-1987 contributions

60b. (1) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Application

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

B. Upon the Death of a Member Entitled to a Deferred Pension

Pre-retirement (spousal) death benefit

61. (1) If a member who is entitled to a deferred pension dies before commencement of payment of the deferred pension, the person who is the spouse of the member on the date of death is entitled to receive,

(a) the benefit described in section 62, in respect of the member's employment, if any, before the 1st day of January, 1987; and

(b) the benefit described in section 63, in respect of the member's employment, if any, on or after the 1st day of January, 1987.

(Last amended May 5, 2010 – Effective June 1, 1995)

Application

(2) Subsection (1) does not apply if the member and the spouse are living separate and apart on the date of death of the member.

Further application

(3) Revoked. (Last amended August 4, 2011 – Effective March 1, 2007)

Idem

(4) Revoked. (Last amended August 4, 2011 – Effective March 1, 2007)

Idem

(5) Revoked. (Last amended August 4, 2011 – Effective March 1, 2007)

Idem

(6) Revoked. (Last amended August 4, 2011 – Effective March 1, 2007)

Pre-1987 (spousal) death benefit

62. (1) This section applies with respect to that portion of the death benefit that relates to a member's employment before the 1st day of January, 1987.

Survivor pension

(2) The spouse of a member with ten years or more qualifying service is entitled to the survivor pension described in subsection (3) for the lifetime of the spouse. (Last amended October 10, 1995 - Effective September 1, 1995)

Pre-1987 survivor pension

(3) The amount of the survivor pension, before adjustment for inflation, shall be based upon the member's credited service for employment before the 1st day of January, 1987 and shall be one half of the amount of the pension, before adjustment for inflation,

(a) that would have been paid to the member at the date of death, if the member was at least sixty-five years of age on the date of death; or

(b) that would have been paid to the member as of the first day of the month following the month in which he or she would have reached sixty-five years of age, if the member was less than sixty-five years of age on the date of death.

Commutation of pension

(3a) If the spouse of a member elects to receive payment of the benefit described under clause 63 (4) (a), then the spouse of the member shall receive a lump sum payment equal to the commuted value of the survivor pension calculated in accordance with subsection (3), and not the survivor pension calculated in accordance with subsection (3). (Last amended December 13, 2012 - Effective July 1, 2012)

Refund of contributions (10 year rule)

(3b) If the commuted value of the survivor pension calculated in accordance with subsection (3) is less than the amount of the member's contributions for employment before the 1st day of January, 1987 together with interest thereon, then the spouse of the member is entitled to a refund, paid in a lump sum, of the member's contributions for employment before the 1st day of January, 1987 together with interest thereon, and not to the benefit described in either subsection (3) or (3a). (Last amended December 13, 2012 - Effective July 1, 2012)

Refund of contributions

(4) The spouse of a member who dies with less than ten years of qualifying service is entitled to a refund of the member's contributions for employment before the 1st day of January, 1987 together with interest thereon. (Last amended June 19, 2012 - Effective July 1, 2012)

Post-1986 (spousal) death benefit

63. (1) This section applies with respect to that portion of the death benefit that relates to a member's employment on or after the 1st day of January, 1987.

Benefit

(2) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Refund of contributions

(3) Revoked. (Last amended September 8, 2006 - Effective September 1, 1995)

Idem

(4) The spouse of a member is entitled to receive,

(a) a lump sum payment equal to the commuted value of the deferred pension to which the member was entitled for credited service for employment on or after the 1st day of January, 1987; or

(b) a survivor pension for the lifetime of the spouse, the commuted value of which is at least equal to the commuted value of a pension for credited service for the member's employment on or after the 1st day of January, 1987, calculated as if the member had become entitled to a retirement pension on the date of death.

(Last amended June 19, 2012 - Effective July 1, 2012)

Election

(5) The spouse may elect the form of benefit to be paid under subsection (4) and a spouse who does not do so within twelve months after the death of the member shall be deemed to have elected to receive a survivor pension. (Last amended May 5, 2010 – Effective January 1, 2008)

Deemed election

(5a) The spouse of a member who dies within twelve months after the death of the member without electing the form of benefit to be paid under subsection (4) shall be deemed to have elected to receive payment of the benefit described under clause (4) (a). (Last amended December 13, 2012 - Effective July 1, 2012)

Survivor pension

(6) A spouse who elects to receive a survivor pension may elect to begin to receive the pension at any time up to the end of the calendar year in which the spouse attains seventy-one years of age, or up to such other time as is required under the *Income Tax Act* (Canada), provided that the pension shall not begin before the month following the month in which the administrator has received all supporting documentation required to pay the pension. (Last amended June 20, 2012 – Effective January 1, 2012)

Pre-retirement child's pension

64. (1) This section applies with respect to the dependent children of a member entitled to a deferred pension who died before commencement of payment of the deferred pension and,

(a) who had a spouse who became entitled to a survivor pension who subsequently died; or

(b) who did not have a spouse entitled to a survivor pension.

(Last amended May 5, 2010 – Effective June 1, 1995)

Entitlement to child's pension

(2) Subject to subsections (3), (3a) and (3b), each dependent child of a member is entitled upon the death of the spouse or the member, as the case may be, to receive a child's pension calculated under subsections (4a) and (4b) while the child remains a dependent child. (Last amended December 13, 2012 - Effective July 1, 2012)

Exception re: post-1986 spousal death benefit

(3) No child's pension is payable in respect of the credited service of a deceased member for which the spouse of the member received the lump sum payment described in clause 63 (4) (a).

Exception re: post-1986 benefit to spouse's estate

(3a) No child's pension is payable in respect of the credited service of a deceased member for which the spouse's estate is entitled to payment of the benefit described under clause 63 (4) (a). (Last amended December 13, 2012 - Effective July 1, 2012)

Exception re: pre-1987 spousal death benefit

(3b) No child's pension is payable in respect of the credited service of a deceased member for which the spouse of the member is entitled to payment of the benefit described under either subsection 62 (3), 62 (3a) or 62 (3b). (Last amended December 13, 2012 - Effective July 1, 2012)

Amount of child's pension

(4) Revoked. (Last amended June 19, 2012 - Effective July 1, 2012)

Pre-1987 (child) death benefit

(4a) (a) This subsection applies with respect to that portion of the death benefit that relates to a member's employment before the 1st day of January, 1987. (Last amended June 19, 2012 - Effective July 1, 2012)

Survivor pension

(b) The dependent child of a member with ten years or more qualifying service is entitled to the child's pension described in subsection (4a) (c) while the child remains a dependent child. (Last amended June 19, 2012 – Effective July 1, 2012)

Pre-1987 child's pension

(c) The amount of the child's pension, before adjustment for inflation, shall be based upon the member's credited service for employment before the 1st day of January, 1987 and shall be one half of the amount of the pension, before adjustment for inflation,

(i) that would have been paid to the member at the date of death, if the member was at least sixty-five years of age on that date; or

(ii) that would have been paid to the member as of the first day of the month following the month in which he or she would have reached sixty-five years of age, if the member was less than sixty-five years of age on the date of death.

(Last amended June 19, 2012 - Effective July 1, 2012)

Post-1986 (child) death benefit

(4b) (a) This subsection applies with respect to that portion of the death benefit that relates to a member's employment on or after the 1st day of January, 1987. (Last amended June 19, 2012 - Effective July 1, 2012)

Benefit

(b) The amount of the child's pension, before adjustment for inflation, shall be based upon the member's credited service for employment on or after the 1st day of January, 1987 and shall be one half of the amount of the pension, before adjustment for inflation,

(i) that would have been paid to the member at the date of death, if the member was at least sixty-five years of age on that date; or

(ii) that would have been paid to the member as of the first day of the month following the month in which he or she would have reached sixty-five years of age, if the member was less than sixty-five years of age on the date of death.

(Last amended June 19, 2012 - Effective July 1, 2012)

Idem

(5) The child's pension shall be shared equally among the member's dependent children.

Share accrues to others

(6) The share of the child's pension of each of the children who ceases to be a dependent child accrues to the remaining dependent children, if any.

Benefit to beneficiary

65. (1) A beneficiary designated by a member entitled to a deferred pension is entitled to the benefit described in subsection (2),

(a) if the member dies before commencement of payment of the deferred pension; and

(b) if, on the date of death, the member does not have a spouse entitled to a benefit payable on his or her death.

(Last amended December 13, 2012 - Effective July 1, 2012)

Amount of benefit

(2) Subject to subsection (3), a beneficiary designated by a member is entitled to receive,

(a) a refund of the member's contributions for employment before the 1st day of January, 1987 together with interest thereon; and

(b) a lump sum payment equal to the commuted value of the deferred pension to which the member was entitled for credited service for employment on or after the 1st day of January, 1987.

(Last amended December 13, 2012 - Effective July 1, 2012)

Residual entitlement

(3) If a person is entitled to a child's pension under section 64 on the death of the member, the beneficiary is entitled to a refund of the amount by which the amount calculated under clause (2) (a) exceeds the commuted value of the amount payable under subsection 64 (4a), together with interest thereon, and a refund of the amount by which the amount calculated under clause (2) (b) exceeds the commuted value of the amount payable under subsection 64 (4b), together with interest thereon. (Last amended December 13, 2012 - Effective July 1, 2012)

Benefit to member's estate

66. (1) The estate of a member entitled to a deferred pension who dies before commencement of payment of the deferred pension is entitled to the payments described in this section. (Last amended May 5, 2010 – Effective June 1, 1995)

Idem, no others entitled

(2) Subject to subsection (3), if no spouse or designated beneficiary is entitled to a benefit on the death of the member, the estate is entitled to,

(a) a refund of the member's contributions for employment before the 1st day of January, 1987 together with interest thereon; and

(b) a lump sum payment equal to the commuted value of the deferred pension to which the member was entitled for credited service for employment on or after the 1st day of January, 1987.

(Last amended December 13, 2012 - Effective July 1, 2012)

Residual entitlement

(3) If a person is entitled to a child's pension under section 64 on the death of the member, the estate is entitled to a refund of the amount by which the amount calculated under clause (2) (a) exceeds the commuted value of the amount payable under subsection 64 (4a), together with interest thereon, and a refund of the amount by which the amount calculated under clause (2) (b) exceeds the commuted value of the amount payable under subsection 64 (4b), together with interest thereon. (Last amended December 13, 2012 - Effective July 1, 2012)

(4) Revoked. (Last amended December 13, 2012 - Effective July 1, 2012)

(5) Revoked. (Last amended December 13, 2012 - Effective July 1, 2012)

Benefit to spouse's estate

66a. (1) Where the member had a spouse who elected to receive the benefit described under clause 63 (4) (b), and who subsequently dies after the payments described under clause 63 (4) (b) have commenced, the spouse's estate is entitled to a refund of the amount by which the member's contributions made in respect of credited service on or after January 1, 1987, together with interest thereon, minus any payments made under section 36, together with interest thereon, and minus the commuted value of the amount payable under subsection 64 (4b), together with interest thereon, exceed the amount paid to the spouse under clause 63 (4) (b), together with interest thereon. (Last amended December 13, 2012 - Effective July 1, 2012)

(2) Where the member had a spouse who elected to receive the benefit described under clause 63 (4) (b), and who subsequently dies before the payments described under clause 63 (4) (b) have commenced, the spouse's estate is entitled to the amount determined under clause 63 (4) (a), together with interest thereon. (Last amended December 13, 2012 - Effective July 1, 2012)

(3) Where the member had a spouse who died after becoming entitled to a survivor pension under subsection 62 (3), the spouse's estate is entitled to a refund of the amount by which the member's contributions for employment before the 1st day of January, 1987, together with interest thereon, exceed the amount paid to the spouse under subsection 62 (3), together with interest thereon. (Last amended December 13, 2012 - Effective July 1, 2012)

Payment of benefits, predecessor Acts

66b. (1) Benefits paid upon the death of a member who ceased to be employed in education prior to January 1, 1990 and who is entitled to a deferred pension on the date of death shall be calculated, with necessary modifications, in accordance with the terms of the *Teachers' Superannuation Act, 1983*, or a predecessor Act, and shall be paid out of the pension fund in accordance with the Act under which the member ceased to be employed in education. (Last amended December 13, 2012 - Effective July 1, 2012)

Limitation on survivor pensions less than $1,200

(2) Subject to section 84, where the annual amount of the survivor pension calculated under sections 62 and 63 is less than $1,200 the spouse of a member is entitled to a pension in that lesser amount and not to a pension in the amount of $1,200 as provided for by Order in Council 1453/74. (Last amended December 13, 2012 - Effective July 1, 2012)

Exception

(3) Subsection (2) shall not apply to the spouse of a member who has at least ten years of credited service in whole or in part before the 1st day of January, 1987 on the date he or she ceased to be employed in education. (Last amended December 13, 2012 - Effective July 1, 2012)

Limitation

(4) For greater certainty, subsection 76 (2) of the *Teachers' Superannuation Act, 1983* shall not apply to any survivor pension payable in respect of a member who did not have at least ten years of credited service on the date he or she ceased to be employed in education. (Last amended December 13, 2012 - Effective July 1, 2012)

C. Upon the Death of a Pensioner

Survivor pension, spouse

67. (1) If a member dies on or after commencement of payment of a pension, the person who was the spouse on the date that the payment of the first instalment of the pension was due is entitled to the survivor pension described in subsection (3) for the spouse's lifetime. (Last amended May 5, 2010 – Effective June 1, 1995)

Application

(2) Subsection (1) does not apply if the member and the spouse were living separate and apart on the date that the payment of the first instalment of the member's pension was due. (Last amended May 5, 2010 – Effective June 1, 1995)

Amount of survivor pension

(3) Subject to sections 68, 69, and 84a, the amount of the annual survivor pension, before adjustment for inflation, payable to the surviving spouse shall be not less than 50 per cent of the pension, before adjustment for inflation,

(a) that was being paid to the member at the date of death, if the member was at least sixty-five years of age on that date; or

(b) that would have been paid to the member as of the first day of the month next following the month in which he or she would have reached sixty-five years of age, if the member was less than sixty-five years of age on the date of death.

(Last amended June 20, 2012 – Effective March 3, 2000)

Exception for low pensions

(4) Despite subsection (3) the survivor of a person who died while receiving an annual pension that had been adjusted under Order in Council 1453/74, is entitled to a pension that is 50 per cent of the pension being paid to the person at the date of death, or such greater percentage as the deceased person had elected prior to death. (Last amended October 23, 1991 - Effective October 23, 1991)

Spousal election re survivor pension

68. (1) In the absence of a joint waiver by a member and the member's spouse of the spouse's entitlement under subsection 44 (3) of the *Pension Benefits Act* (amount of survivor benefit), the amount of the survivor pension payable on the death of the member shall be 60 per cent of the amount of the member's pension that would be payable if the amount of the pension were calculated without regard to this section. (Last amended October 23, 1991 - Effective October 23, 1991)

Waiver void

(2) A waiver referred to in subsection (1) is void if it is dated, signed, or delivered to the administrator more than twelve months before the commencement of payment of the member’s pension or after the commencement of payment of the member’s pension. (Last amended August 4, 2011 – Effective May 18, 2010)

Adjustment of member's pension

(3) In the absence of a waiver referred to in subsection (1), the amount of the pension payable to the member shall be actuarially reduced before limits imposed by the *Income Tax Act* (Canada) to allow for payment of the increased survivor pension in accordance with subsection (1). (Last amended October 10, 1995 - Effective January 1, 1992)

(3a) Prior to calculating the payment described in subsection (1), the pension the member was receiving shall be reduced immediately upon the member’s death to reflect any reduction described in section 81 that was not applicable immediately prior to the member’s death. (Last amended June 20, 2012 – Effective January 1, 1990)

Application

(4) This section does not apply with respect to a member who, before the 1st day of January, 1988, began to receive a pension under a predecessor Act.

Idem

(5) This section does not apply with respect to a member who dies before commencement of payment of the member’s pension. (Last amended May 5, 2010 – Effective June 1, 1995)

Increase of survivor pension

69. (1) A member may direct the administrator to increase the amount of a survivor pension that may become payable under section 67 in respect of the member to an amount equal to 55, 65, 70 or 75 per cent of the member's pension that would be payable if the amount of the pension were calculated without regard to this section.

Time limit

(2) A direction must be given in writing and must be delivered to the administrator at least two years before the earlier of,

(a) the member's normal retirement date; or

(b) the beginning of the month in which the member's pension begins.

Idem

(3) The administrator shall act on a direction delivered after the deadline specified in subsection (2) and before the member applies for a retirement pension if the administrator is satisfied that the member is in good health having regard to the member's age.

Adjustment of member's pension

(4) The amount of the pension payable to the member shall be actuarially reduced before limits imposed by the *Income Tax Act* (Canada) to allow for payment of the increased survivor pension in accordance with the direction. (Last amended October 10, 1995 - Effective January 1, 1992)

(4a) Prior to calculating the payment described in subsection (1), the pension the member was receiving shall be reduced immediately upon the member's death to reflect any reduction described in section 81 that was not applicable immediately prior to the member's death. (Last amended June 20, 2012 – Effective January 1, 1990)

Commuted value

(5) The commuted value of pension paid to the member including the commuted value of the increased survivor benefit shall not be less than the commuted value of the pension, including survivor benefit, that would otherwise be payable.

Revocation of direction

(6) A member may revoke a direction given under this section by a written revocation delivered to the administrator before the member begins receiving a pension.

Direction void

(7) A direction given under this section by a member is void if the member dies before beginning to receive a pension.

Restriction

(8) A person whose pension would be reduced from an amount greater than $2,400 to an amount less than $2,400 upon making an election under this section is not entitled to an increase in his or her pension under Order in Council 1453/74. (Last amended October 23, 1991 - Effective October 23, 1991)

Survivor pension, new spouse

70. (1) In this section and section 84a, "new spouse", in relation to a member, means a person who becomes the spouse of the member after the commencement of payment of the member's retirement or disability pension. (Last amended June 20, 2012 – Effective March 3, 2000)

Idem

(2) A member who does not have a spouse eligible to receive a survivor pension under section 67 may, after the commencement of payment of the member's retirement or disability pension, direct the administrator to provide a survivor pension to a new spouse. (Last amended May 5, 2010 – Effective June 1, 1995)

Time limit

(3) A direction must be given in writing and must be delivered to the administrator on or before the later of,

(a) ninety days after the date on which the member becomes the spouse of the new spouse; or

(b) if immediately before the member becomes the spouse of the new spouse there is a child who would be entitled upon the death of the member to receive a child's pension under section 73, ninety days after the date on which the child ceases to be eligible to receive the child's pension.

Idem

(4) The administrator shall act on a direction delivered after the deadline specified in subsection (3) if the administrator is satisfied that the member is in good health having regard to the member's age.

(4a) A direction given under this section is not effective until six months following the date of delivery of the direction to the administrator. (Last amended June 1, 1995 - Effective June 1, 1995)

(4b) A direction made under this section is null and void if the death of the member occurs before the effective date of the direction. (Last amended June 1, 1995 - Effective June 1, 1995)

(4c) A member may revoke a direction given under this section by a written revocation delivered to the administrator before the direction becomes effective in accordance with subsection (4a). (Last amended September 8, 2006 – Effective June 1, 1995)

Amount of survivor pension

(5) Subject to section 84a, a member described in subsection (2) shall direct the administrator to pay a survivor pension in the amount of 50, 55, 60, 65, 70 or 75 per cent of the pension that would otherwise be payable on the first day of the month next following the month in which the member becomes the spouse of the new spouse. (Last amended June 20, 2012 – Effective March 3, 2000)

Adjustment of member's pension

(6) The amount of a retirement or disability pension payable to the member shall be actuarially reduced before limits imposed by the *Income Tax Act* (Canada) to allow for payment of the survivor pension in accordance with the direction. (Last amended October 10, 1995 - Effective January 1, 1992)

Idem

(7) The actuarial reduction required by subsection (6) shall be based upon the ages of the member and of the spouse on the last day of the month in which the direction is delivered to the administrator.

(7a) Prior to calculating the payment described in subsection (5), the pension the member was receiving shall be reduced immediately upon the member’s death to reflect any reduction described in section 81 that was not applicable immediately prior to the member’s death. (Last amended June 20, 2012 – Effective January 1, 1990)

Payment of survivor pension

(8) The administrator shall pay the survivor pension in accordance with the direction but not while there is a person who is eligible to receive a child's pension in respect of the member.

Eligibility

70a. (1) This section applies to a member or former member who, as of April 23, 1998, was:

(a) receiving a pension in respect of which there was no person eligible, as of April 22, 1998, to receive a survivor pension, and

(b) living with a person who would have qualified under the relevant provisions of the pension plan as the member's same-sex partner for purposes of eligibility for a survivor pension, other than a survivor pension provided by sections 70, 71, 72, or any predecessor thereof, if the definition of "same-sex partner" as set out in the pension plan had been in effect prior to April 23, 1998. (Last amended July 10, 2000 – Effective April 23, 1998)

Direction

(2) Subject to subsections (3) and (4), a member described in subsection (1) may direct the administrator to pay a survivor pension to the person described in subsection (1) for the person's lifetime commencing the month following the member's date of death. (Last amended July 10, 2000 – Effective April 23, 1998)

Idem

(3) Where the member dies prior to providing the direction referred to in subsection (2), such direction may be provided by the person described in subsection (1). (Last amended July 10, 2000 – Effective April 23, 1998)

Deadline

(4) The direction provided in accordance with subsection (2) or (3) shall be provided to the administrator. (Last amended September 8, 2006 - Effective April 23, 1998)

Entitlement

(5) Subject to subsection (6), the amount of the annual survivor pension, before adjustment for inflation, payable under this section shall be 50 per cent of the pension, before adjustment for inflation,

(a) that was being paid to the member at the date of death, if the member was at least sixty-five years of age on that date, or

(b) that would have been paid to the member as of the first day of the month next following the month in which he or she would have reached sixty-five years of age, if the member was less than sixty-five years of age on the date of death. (Last amended July 10, 2000 - Effective April 23, 1998)

Offset

(6) The survivor pension described in subsection (5) shall be actuarially reduced by any amounts paid to any person, including the member's estate, as a result of the member's death. (Last amended July 10, 2000 - Effective April 23, 1998)

(7) No survivor pension is payable under this section if the person described in subsection (1) dies prior to providing the direction in accordance with subsections (3) and (4). (Last amended July 19, 2007 – Effective April 23, 1998)

(8) Revoked. (Last amended August 4, 2011 – Effective March 1, 2007).

Survivor pension, predecessor Acts

71. (1) This section applies with respect to a member who, before the 1st day of September, 1984, ceased to be employed in education within the meaning of a predecessor of this Act and who became the spouse of a person after ceasing that employment.

Direction re survivor pension

(2) A member described in subsection (1) may direct the administrator to provide a survivor benefit for the member's spouse and section 70 applies with respect to the direction with necessary modifications.

Time limit

(3) A direction under this section shall be delivered to the administrator on or before the latest of,

(a) the 31st day of March, 1990;

(b) ninety days after the date on which the member becomes a spouse; or

(c) if on the 1st day of January, 1990 there is a child who would be entitled upon the death of the member to receive a survivor allowance under a predecessor of this Act, ninety days after the date on which the child ceases to be eligible to receive the survivor allowance.

Idem

(4) The administrator shall act on a direction delivered after the deadline specified in subsection (3) if the administrator is satisfied that the member is in good health having regard to the member's age.

Deemed direction

(5) A member described in subsection (1) who dies on or before the 31st day of March, 1990 without having given a direction under this section shall be deemed to have given it on that date and shall be deemed to have directed the administrator to pay a 50 per cent survivor pension.

Survivor pension (prior inquiry)

72. (1) This section applies with respect to a person who became the spouse of a member described in subsection 71 (1) after the member ceased to be employed in education within the meaning of a predecessor of this Act.

Idem

(2) This section does not apply unless the member has ceased to be a member before the 1st day of January, 1990 because he or she has died.

Survivor pension

(3) A spouse described in subsection (1) is entitled to a survivor pension calculated from the date of a written inquiry respecting a survivor pension,

(a) made to the Teachers' Superannuation Commission before the 1st day of January, 1990; or

(b) made to the administrator on or after the 1st day of January, 1990.

Amount of pension

(4) The amount of the survivor pension is 50 per cent of the amount of the member's retirement pension on the date of the member's death adjusted for inflation as if it were a pension for the period from the date of the member's death to the date the spouse becomes entitled to the survivor pension.

(5) Prior to calculating the payment described in subsection (4), the pension the member was receiving shall be reduced immediately upon the member’s death to reflect any reduction described in section 81 that was not applicable immediately prior to the member’s death. (Last amended June 20, 2012 – Effective January 1, 1990)

Child's pension

73. (1) This section applies with respect to the dependent children of a member who died while receiving a retirement or disability pension and,

(a) who had a spouse who died after becoming entitled to a survivor pension; or

(b) who did not have a spouse entitled to a survivor pension.

Entitlement to child's pension

(2) Each dependent child of a member, upon the death of the spouse or the member, as the case may be, is entitled to a child's pension while remaining a dependent child.

Amount of child's pension

(3) The amount of the annual child's pension is the amount of the survivor pension to which a spouse of the member was or would have been entitled after the death of the member, shared equally among the dependent children.

Share accrues to others

(4) The share of the child's pension of each of the children who ceases to be a dependent child accrues to the remaining dependent children, if any.

Beneficiary's pension, R.S.C. 1952, c. 148

74. (1) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Time limit

(2) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Idem

(3) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Amount of beneficiary's pension

(4) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Adjustment of member's pension

(5) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Revocation of direction

(6) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Direction void

(7) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Benefit to estate

75. The estate of a member who was receiving a pension on the date of death is entitled to a refund of the amount by which the member's contributions together with interest thereon exceeds the sum of the amount paid to the member and the amount, if any, paid to every other person who was entitled to a benefit on the member's death, together with interest thereon.

10 year guarantee

75a. (1) Notwithstanding any other provision of the plan, but subject to this section, where a member dies while receiving a retirement pension or a disability pension, but prior to receiving the equivalent of 120 monthly pension payments, the remaining balance of such pension payments shall be paid:

(a) as a pension to the person who remains otherwise eligible for benefits under the plan as a result of the member’s death, or

(b) to the member’s estate, if there is no person eligible as described in (a), in a lump sum equal to the present value of the remaining payments. (Last amended April 2, 2001 – Effective April 1, 2001)

Direction

(2) If a member has a spouse eligible for a survivor pension at the commencement of payment of the member’s pension, subsection (1) shall only apply if the member has delivered a written direction to the administrator prior to the commencement of payment of the member’s pension. (Last amended April 2, 2001 – Effective April 1, 2001)

Idem

(3) A direction provided in accordance with subsection (2) may be revoked by the member provided that a written revocation is delivered to the administrator prior to the commencement of payment of the member’s pension. (Last amended April 2, 2001 – Effective April 1, 2001)

Idem

(4) A direction provided in accordance with subsection (2) is void if the member dies prior to the commencement of payment of the member’s pension. (Last amended April 2, 2001 – Effective April 1, 2001)

Adjustment of member's pension

(5) The pension of a member who provides a direction in accordance with subsection (2) shall be reduced to allow for payment of the benefits in accordance with subsection (1). (Last amended April 2, 2001 – Effective April 1, 2001)

Offset

(6) Subject to subsection (11), the payments made in accordance with subsection (1) shall be paid in lieu of any other amounts otherwise payable under the plan as a result of the member's death. (Last amended April 2, 2001 – Effective April 1, 2001)

CPP Reduction

(7) The payments made in accordance with subsection (1) shall be reduced immediately upon the member's death to reflect any reduction described in section 81 that was not applicable immediately prior to the member's death. (Last amended April 2, 2001 – Effective April 1, 2001)

More than one beneficiary

(8) Where there is more than one person eligible as described in clause (1)(a), then the pension payable in accordance with that provision shall be shared equally among such persons. (Last amended April 2, 2001 – Effective April 1, 2001)

Upon death of beneficiary

(9) Where any person eligible as described in clause (1)(a) dies prior to completion of the pension payments under that provision, the remaining payments shall be shared equally among any remaining eligible persons or, if none, shall be paid to the person's estate in a lump sum equal to the present value of the remaining payments. (Last amended April 2, 2001 – Effective April 1, 2001)

Upon ineligibility of beneficiary

(10) Where any person eligible as described in clause (1)(a) ceases to be a person eligible as described in clause (1)(a) prior to completion of the pension payments under that provision, the remaining payments shall be shared equally among any remaining eligible persons or, if none, shall be paid to the member's estate in a lump sum equal to the present value of the remaining payments. (Last amended April 2, 2001 – Effective April 1, 2001)

Completion of 10 year guarantee

(11) Upon completion of the pension payments in accordance with clause (1)(a), the person or persons described in that provision shall be entitled to receive, on a prospective basis only, the pension that they would otherwise be receiving as a result of the member's death but for this section, except that any reduction that was applied pursuant to subsection (5) shall continue to apply. (Last amended April 2, 2001 – Effective April 1, 2001)

Application to existing pensions

(12) This section shall apply, with necessary modifications, to a member who is receiving a pension as of April 1, 2001 except that, for the purposes of subsection (2) only, spousal eligibility for a survivor pension shall be determined as of April 1, 2001 and the direction required in accordance with (2) must be delivered to the administrator by May 1, 2001. (Last amended April 2, 2001 – Effective April 1, 2001)

Application to deferred pensions

(12a) This section shall apply, with necessary modifications, to a member who ceased employment in education on or after January 1, 1990 but prior to April 1, 2001 and who is entitled to a deferred pension. (Last amended June 19, 2012 – Effective April 1, 2001)

Application to suspended pensions

(13) For the purposes of this section, references to a member who is receiving a pension shall include a member whose pension is suspended. (Last amended April 2, 2001 – Effective April 1, 2001)

Application to TSA pensions

(14) This section shall apply, with necessary modifications, to a member who ceased employment in education prior to January 1, 1990 and who is either entitled to a deferred pension or receiving a pension as of April 1, 2001. (Last amended May 5, 2010 – Effective April 1, 2001)

Application to deferred pensions post-June 30, 2012

(15) This section shall apply, with necessary modifications, to a member who ceased employment in education prior to July 1, 2012 and who was not entitled to a deferred pension under section 30 as it read on June 30, 2012. (Last amended June 19, 2012 – Effective July 1, 2012)

D. Payment of Death Benefits

Commencement of pension

76. (1) A pension that is payable immediately on the death of a member who was not receiving a retirement or disability pension on the date of death shall begin as of the day after the day the member dies.

Idem

(2) A pension that is payable on the death of a member who was receiving a retirement or disability pension on the date of death shall begin as of the first day of the month after the month in which the member dies.

Interest payable

(3) Interest shall be paid on pension payments due under a pension mentioned in this section if the administrator does not begin paying the pension by the end of the month in which the beneficiary becomes entitled to receive it. (Last amended June 28, 1990 - Effective June 28, 1990)

Interest Payable

(4) Interest on each overdue monthly pension payment, calculated at the standard rate, shall be paid from the date the payment was due to the day before it was made. (Last amended February 28, 1992 - Effective January 1, 1992)

Payments to estate

77. (1) If the administrator is unable to locate a personal representative of the estate of a deceased member, the administrator may pay into court any payments that under the pension plan are required to be made to the estate.

Missing beneficiary

(2) If the administrator is unable, after making reasonable inquiries, to locate an individual who is entitled to a death benefit under the pension plan or a beneficiary designated by the deceased member under the *Pension Benefits Act*, the administrator shall pay to the estate of the deceased member one year after the date of death the amount to which the estate is otherwise entitled when no other person is entitled to a benefit on the death of the member.

Missing beneficiary found

(3) If an individual entitled to a death benefit under the pension plan or a beneficiary designated by the deceased member under the *Pension Benefits Act* applies for the benefit after the administrator makes a payment under subsection (2), the administrator shall pay the individual the amount of the benefit to which the individual is entitled less the amount paid to the estate by the administrator.

Transitional

(4) This section applies with respect to a person with credited service under a predecessor of this Act who dies before the 1st day of January, 1990, as if that person were a deceased member of the pension plan.

Discharge

(5) The administrator is discharged on making a payment in accordance with this section.

Interpleader, more than one applicant

78. (1) Revoked. (Last amended September 8, 2006 – Effective September 1, 2006)

Court may order

(2) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Application to court

(3) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

Application of R.S.O. 1980, c. 488, s. 62

(4) Revoked. (Last amended September 8, 2006 - Effective September 1, 2006)

PART VIII
BENEFITS AND PAYMENTS - GENERAL

A. Adjustments for Inflation

Inflation adjustment, pensions

79. (1) Every retirement pension, disability pension, survivor pension, child's pension and beneficiary's pension shall be adjusted for inflation in accordance with section 80.

Idem, deferred pensions

(2) Every deferred pension payable under the pension plan shall be adjusted for inflation in accordance with section 80 for the period beginning at the end of the last month for which the member has credit under the plan and ending when the pension begins.

Limitation

(3) No pension or deferred pension shall be adjusted under this section for inflation in respect of a period before the 1st day of January, 1990.

Adjustment of pensions for cessations prior to May 31, 1982

79a. (1) For pension instalments payable for periods on or after June 1, 2001, the annual pension of a member, or of the survivor of a member, who ceased to be employed for purposes of the plan prior to May 31, 1982, shall be adjusted in accordance with salary adjustments determined by the actuary with reference to the year in which the member ceased to be employed for purposes of the plan. (Last amended April 2, 2001 – Effective April 1, 2001)

Idem

(2) Subsection (1) shall also apply to the pension payable to the survivor of a member where the member:

(a) ceased to be employed for purposes of the plan on or after May 31, 1982 but prior to September 1, 1984, and

(b) died prior to receiving a pension calculated on the basis of the average of the member's annual pensionable salary for the five school years during which it was highest,

but only to the extent that the survivor is not already receiving a survivor pension equivalent to that calculated on the basis described in (b). (Last amended April 2, 2001 – Effective April 1, 2001)

Applicability

(3) This section shall not apply to the retirement pension or benefits upon death of a member who did not have at least ten years of credited service on the date he or she ceased to be employed in education. (Last amended December 13, 2012 – Effective July 1, 2012)

Calculation of inflation adjustments

80. (1) In the formulas in this section,

"A" is the carry forward determined for the immediately preceding year,

"B" is the basic ratio for the year,

"C" is the adjustment ratio for the year,

"D" is the basic ratio for the year after the last year for which the member has credit in the pension plan, and shall be calculated to a maximum of 1.080 or to a minimum of 1.000, and (Last amended October 9, 2008 – Effective January 1, 2009)

"E" is the number of full months in the year that are after the month in the last year for which the member has credit in the pension plan. (Last amended October 9, 2008 – Effective January 1, 2009)

Definitions

(2) In this section,

"accumulated adjustment ratio", for a person's pension, means the product of the multiplication of all adjustment ratios for the years in the period commencing with the last year for which the member has credit in the pension plan and ending with the year for which the accumulated adjustment ratio is being determined; (Last amended October 9, 2008 – Effective January 1, 2009)

"adjustment ratio", for a person's pension, means,

(a) for any year before the year 1976 and for the last year for which the member has credit in the pension plan, 1.000,

(b) if the member for whose credit in the plan the pension is payable ceased to be employed in education in or after the year 1975, for the year after the last year for which the member has credit in the pension plan, the ratio determined by the formula "[(D - 1.000) × E / 12] + 1.000", and

(c) for the later of the year 1976 and the second year after the last year for which the member has credit in the pension plan and for any subsequent year, the ratio determined by the formula "A + B" calculated to a maximum of 1.080 or to a minimum of 1.000; (Last amended October 9, 2008 – Effective January 1, 2009)

"basic ratio", for a year, means the ratio expressed to three decimal places that the average for the Consumer Price Index over the last twelve months of the twenty-four-month period ending with the 30th day of September in the immediately preceding year bears to the average for the Consumer Price Index over the first twelve months of that period;

"carry forward", with respect to the pension of a person, means,

(a) for any year before the year 1976, for the last year for which the member has credit in the pension plan and for the year after that year, nil, and

(b) for the later of the year 1976 and the second year following the last year for which the member has credit in the pension plan and for any subsequent year, the positive or negative number determined by the formula "A + B - C"; (Last amended October 9, 2008 – Effective January 1, 2009)

"Consumer Price Index" means the Consumer Price Index for Canada as published by Statistics Canada under the authority of the *Statistics Act* (Canada);

"member" means the person in respect of whose credit in the pension plan the pension, to which the formula is applied under this section, is payable, and includes a contributor within the meaning of the *Teachers' Superannuation Act*, *1983* or a predecessor Act; (Last amended October 9, 2008 – Effective January 1, 2009)

"pension" means a pension to which a person is entitled from the plan other than the adjustment for inflation provided by this section, and an allowance, annuity, deferred annuity or other periodic payments to which a person has become entitled under the *Teachers' Superannuation Act*, *1983* or a predecessor Act;

"plan" includes the pension plan established under the *Teachers' Superannuation Act*, *1983* and any predecessor Act.

Payment of inflation adjustment

(3) The annual amount of pension payable to a person from the pension fund shall, commencing with the year when payment of the pension is to commence and in each subsequent year that the pension continues to be payable, be adjusted for inflation by multiplying the annual amount of the pension by the accumulated adjustment ratio for the pension of the person for that year, and the amount by which the pension thus adjusted exceeds the annual amount of pension before the adjustment in each year shall be paid to the person entitled to receive the pension for which it is calculated at the same times, in the same manner and subject to the same terms and conditions as apply to the pension in respect of which it is paid.

Conditional inflation adjustment for post-2009 credit

(3a) Notwithstanding subsections (1), (2) and (3), but subject to subsection (3b), benefits payable in respect of credit accrued under the pension plan for periods after 2009 shall only be adjusted for inflation under this section to the extent that sufficient funds are available to provide for such adjustments without creating a going concern unfunded liability. (Last amended October 9, 2008 – Effective January 1, 2009)

50% guaranteed inflation adjustment for post-2009 credit

(3b) Benefits payable in respect of credit accrued under the pension plan for periods after 2009 shall be adjusted for inflation under this section such that the adjustment made each year is not less than one half of the adjustment that would have been made for the year in accordance with this section as it read on December 31, 2008. (Last amended October 9, 2008 – Effective January 1, 2009)

Inflation adjustment for benefits payable after 2011

(3c) Revoked. (Last amended September 17, 2013 – Effective January 1, 2014)

0% guaranteed inflation adjustment for post-2013 credit

(3d) Notwithstanding subsection (3b), benefits payable in respect of credit accrued under the pension plan for periods after 2013 may be further adjusted for inflation under this section such that the total adjustment made each year is less than one half of the adjustment that would have been made for the year in accordance with this section as it read on December 31, 2008. (Last amended September 17, 2013 – Effective January 1, 2014)

Determination of inflation adjustment for post-2009 and post-2013 credit

(3e) For purposes of subsections (3a), (3b) and (3d), the inflation adjustments for benefits payable each year, in respect of credit accrued under the pension plan for periods after 2009 and after 2013 respectively, shall be determined by the co-sponsors of the pension plan, the Executive of the Ontario Teachers' Federation and the Minister of Education. (Last amended September 17, 2013 – Effective January 1, 2014)

Ratio not to apply

(4) The ratio determined for the year 1990 under the *Superannuation Adjustment Benefits Act* does not apply to a pension to which this section applies.

Effect of re-employment

(5) For the purpose of determining an accumulated adjustment ratio for benefits that commence to be paid on or after May 10, 2007, for members who cease to be employed in education on or after September 1, 1995:

(a) the last school year in which the member accumulated more than ten days of credited service during the period from January 1, 1997 onward, or, if the member did not accumulate more than ten days of credited service in a school year during this period, then

(b) the last school year in which the member accumulated more than twenty days of credited service during the period from September 1, 1990 to December 31, 1996,

is deemed to be the last year for which the member has credit in the pension plan. (Last amended December 21, 2007 – Effective May 10, 2007)

(6) Revoked. (Last amended July 19, 2007 – Effective May 10, 2007)

B. CPP Reduction

CPP reduction for pensions

81. (1) If a member has contributed to the *Canada Pension Plan* or the *Quebec Pension Plan*, the amount of the member's retirement pension, full disability pension or partial disability pension shall be reduced by the amount calculated under subsection (3).

Commencement, retirement pension

(2) A reduction of a member's pension shall apply with respect to pension payments due the month after the earlier of,

(a) the month in which the member reaches sixty-five years of age; or

(b) the month in which the first instalment of the member's disability pension, if any, under the *Canada Pension Plan* or the *Quebec Pension Plan* is due.

Amount of reduction

(3) The amount of the reduction in an annual pension payable for periods on or after January 1, 1997 and prior to January 1, 1999 is calculated using the formula,

0.0068 x A x B,

and the amount of the reduction in an annual pension payable for periods on or after January 1, 1999 and prior to January 1, 2002 is calculated using the formula,

0.0060 x A x B,

and the amount of the reduction in an annual pension payable for periods on or after January 1, 2002 is calculated using the formula,

0.0045 x A x B

in which,

"A" is the lesser of,

(a) the member's average salary, and

(b) the amount determined under subsection (4), and

"B" is the number of years of the member's credited service for employment on or after the 1st day of January, 1966 in respect of which the member made contributions under the *Canada Pension Plan* or the *Quebec Pension Plan*. (Last amended April 2, 2001 – Effective April 1, 2001)

(3a) For pension instalments due on or after January 1, 1997, the amount of the reduction in annual pension, for participation in the *Canada Pension Plan* or the *Quebec Pension Plan*, of a member, or a survivor of a member, calculated under Schedule 1 of the *Teachers' Pension Act* or a predecessor act, is recalculated substituting 0.0068 for 0.007 in the formula used to calculate the reduction, but the amount of the reduction to provide for a higher survivor pension will not be recalculated. (Last amended February 20, 1997 - Effective January 1, 1997)

(3b) For pension instalments payable for periods on or after January 1, 1999, the amount of the reduction in annual pension, for participation in the *Canada Pension Plan* or the *Quebec Pension Plan*, of a member, or a survivor of a member, calculated under Schedule "1" of the *Teachers' Pension Act* or a predecessor act, is recalculated substituting 0.0060 for 0.0068 in the formula used to calculate the reduction, but the amount of the reduction to provide for a higher survivor pension will not be recalculated. (Last amended May 27, 1998 - Effective June 1, 1998)

(3c) For pension instalments payable for periods on or after January 1, 2002, the amount of the reduction in annual pension, for participation in the *Canada Pension Plan* or the *Quebec Pension Plan*, of a member, or a survivor of a member, calculated under Schedule 1 of the *Teachers' Pension Act* or a predecessor act, is recalculated substituting 0.0045 for 0.0060 in the formula used to calculate the reduction, but the amount of the reduction to provide for a higher survivor pension or a 10 year guaranteed pension will not be recalculated. (Last amended September 8, 2006 – Effective April 1, 2001)

Average YMPE

(4) The amount is the average of the Year's Maximum Pensionable Earnings for the year in which the member ceases to be employed in education and for each of the two preceding years, except that for an annual pension payable for periods on or after January 1, 2002 the amount is the average of the Year's Maximum Pensionable Earnings for the year in which the member ceases to be employed in education and for each of the four preceding years. (Last amended April 2, 2001 – Effective April 1, 2001)

Idem

(4a) For pension instalments payable for periods on or after January 1, 2002, the amount of the reduction in annual pension, for participation in the *Canada Pension Plan* or the *Quebec Pension Plan*, of a member, or a survivor of a member, calculated under Schedule 1 of the *Teachers' Pension Act* or a predecessor act, is recalculated using the five year average of the Year's Maximum Pensionable Earnings, as described in subsection (4), in the formula used to calculate the reduction, but the amount of the reduction to provide for a higher survivor pension or a 10 year guaranteed pension will not be recalculated. (Last amended September 8, 2006 – Effective April 1, 2001)

(5) Where a reduction is applied as provided in subsection 81(2)(b) and the member's *Canada Pension Plan* or *Quebec Pension Plan* disability pension is terminated before the member reaches sixty-five years of age, the reduction will be suspended, effective the month following the month of the termination, until the payment of pensions due the month after the earlier of,

(a) the month in which the member reaches sixty-five years of age; or

(b) the month in which the first instalment of the member's disability pension, if any, under the *Canada Pension Plan* or the *Quebec Pension Plan* is due.

(Last amended April 15, 1998 - Effective January 1, 1997)

C. Payment of Benefits

Application for benefit

82. (1) No benefit under the plan shall be paid before the administrator receives an application for it in the form provided by the administrator.

Election or direction

(2) An election available under the plan or a direction that may be given to the administrator shall be made or given in the form provided by the administrator.

Repayment

82a. A person who receives payments to which the person is not entitled shall repay the amounts so received, together with interest thereon calculated at the standard interest rate. (Last amended May 5, 2010 – Effective January 1, 2002)

Multiple pensions

83. No member is entitled to payment of more than one pension under the plan during the same month or other payment period in respect of the member's credited service.

Commutation of pensions

84. The administrator shall pay the commuted value of a pension, other than a disability pension or dependent child pension, in accordance with subsections 44 (7) and (7.1), or clause 50 (1) (a), of the *Pension Benefits Act.* (Last amended January 15, 2014 – Effective January 1, 2014)

Shortened life expectancy

84a. (1) Upon application by a member, the administrator shall pay the commuted value of a pension or deferred pension in such circumstances of shortened life expectancy as may be prescribed under subsection 49(2) of the *Pension Benefits Act*, provided the prescribed conditions under that Act are satisfied. (Last amended June 17, 2003 – Effective March 3, 2000)

Amount

(2) Subject to subsections (3) and (4), the amount payable under subsection (1) shall be determined in accordance with the *Pension Benefits Act* and accepted actuarial practice. (Last amended September 8, 2006 – Effective March 3, 2000)

Idem

(3) The commuted value of a deferred pension shall be determined as if the member had a normal life expectancy. (Last amended June 17, 2003 – Effective March 3, 2000)

Idem

(4) The commuted value of a pension shall be determined based on the member having a shortened life expectancy. (Last amended June 17, 2003 – Effective March 3, 2000)

Application void

(5) An application made under this section is void if the member dies before the benefit under subsection (1) is paid. (Last amended June 17, 2003 – Effective March 3, 2000)

Deemed cessation

(6) A member who makes an application under this section and who satisfies the evidentiary requirements of the *Pension Benefits Act* is deemed to have ceased employment in education for the purposes of membership in the pension plan, on the date the member's physician signs the statement required under the *Pension Benefits Act*. (Last amended June 20, 2012 – Effective January 1, 2007)

(7) If a direction under section 70 regarding a "new spouse" has been delivered to the administrator, the benefit under subsection 84a (1) shall not be paid unless the "new spouse" provides to the administrator a signed statement waiving any entitlement under section 70. (Last amended June 20, 2012 – Effective March 3, 2000)

Deductions from pensions

85. (1) Despite section 65 of the *Pension Benefits Act*, a person receiving a pension under the pension plan or an allowance under a predecessor Act may direct the administrator to deduct and remit from the pension or allowance on behalf of the person,

(a) premiums payable under the Ontario Health Insurance Plan by the person;

(b) premiums for life, medical, dental or health-related insurance payable by the person under a contract of group insurance approved by the administrator for the purpose of this section; and

(c) membership fees payable to The Retired Teachers of Ontario (RTO)/Les enseignantes et enseignants retraités de l'Ontario (ERO). (Last amended September 8, 2006 – Effective January 1, 1999)

Conditions

(2) The administrator may impose and require compliance with such conditions as the administrator considers appropriate before acting upon a direction.

Revocation of direction

(3) A person making a direction may revoke it by written notice to the administrator.

Termination of pension

86. Every pension terminates as of the end of the month in which the event that terminates the pension occurs.

No assignment etc.

86a. No pension or benefit shall be capable of being assigned, charged, anticipated, given as security or surrendered except as provided for in the *Pension Benefits Act*. (Last amended September 8, 2006 - Effective January 1, 1992)

D. Administration

Appeal of decision

87. (1) A person who is aggrieved by a decision of an employee of the administrator respecting the person's entitlement to, or the amount of, a pension benefit may appeal the decision to a committee of the administrator designated for the purpose of this section and the committee of the administrator shall determine the appeal. (Last amended April 15, 1998 - Effective October 1, 1997)

Idem

(2) An appeal shall be made in accordance with the procedures established by the administrator.

Determination of commuted value

88. The commuted value of a benefit shall not be less than the amount calculated in accordance with the *Recommendations for Minimum Transfer Values of Pensions* published from time to time by the Canadian Institute of Actuaries and shall be calculated using the rate of interest specified by, and such actuarial tables as may be adopted by, the administrator.

Calculation of interest

89. (1) Unless otherwise indicated, interest shall be calculated at the standard interest rate. For a given year, the standard interest rate attributable to a transaction is a rate equal to the average yield for the 12 month period, ending on the 31st day of October in the preceding calendar year, of five-year personal fixed term chartered bank deposit rates as determined from the Canadian Socio-Economic Information Management (CANSIM) Series V 122515 published monthly in the Bank of Canada Review and interest is compounded annually each December 31st. (Last amended September 8, 2006 - Effective September 1, 2006)

Idem, transitional

(2) For 1990 the standard interest rate attributable to a transaction is the weighted average effective annual yield of the debentures held by the Teachers' Superannuation Fund under the *Teachers' Superannuation Act, 1983* as at the 31st day of December, 1989.

Idem, transitional

(3) Interest payable in respect of a period before the 31st day of December, 1989 shall be calculated up to that date at the applicable rate in effect under the *Teachers' Superannuation Act, 1983* and at the applicable standard rate in effect thereafter. (Last amended June 1, 1995 - Effective June 1, 1995)

Interest on contributions

(4) Interest credited under the pension plan on contributions shall be calculated in accordance with the *Pension Benefits Act* and credited to the member as at the 31st day of December in each year.

Interest on lump sums

(5) Interest is payable in accordance with the *Pension Benefits Act* on a lump sum payment of the commuted value of a benefit from the effective date of the determination of the commuted value to the day before the lump sum is paid. (Last amended February 28, 1992 - Effective January 1, 1992)

Report re employment in education

90. (1) Revoked. (Last amended May 6, 2010 – Effective September 1, 2012)

Failure to report

(2) Revoked. (Last amended May 6, 2010 – Effective September 1, 2012)

Prior refund re multiple pensions

91. Revoked. (Last amended April 15, 1998 - Effective January 1, 1992)

PART IX
PURCHASE OF CREDIT FOR SERVICE

A. General

Purchases, general

92. (1) A member may purchase or receive a maximum of five years of credited service,

(a) under sections 10 (2a), 10 (2f), 10 (4), 12a, 94 and 96, and

(b) for any unpaid portion of a period under subsections 10 (2e) and 10 (2g) in respect of which compensation is prescribed in accordance with Regulation 8507 (1) (a) of the *Income Tax Act* (Canada),

for absences after the 31st day of December, 1990.

(Last amended July 21, 2014 – Effective September 1, 2014)

Idem

(2) Subject to section 28, a member may not purchase credited service for a period of time for which the member has credited service under the plan. (Last amended December 20, 1999 - Effective September 1, 1998)

Past service pension adjustment

92a. (1) The purchase of credited service by a member who requires certification of a Past Service Pension Adjustment under the *Income Tax Act* (Canada) is not complete until the administrator has obtained a certificate from the Minister of National Revenue. (Last amended February 28, 1992 - Effective January 1, 1992)

Idem

(2) Credited service in respect of which certification has been obtained from the Minister of National Revenue shall not be included in the credited service maximums in subsections 92 (1) and 94 (15). (Last amended February 28, 1992 - Effective January 1, 1992)

Purchases, transitional

93. (1) The purchase of credited service by a member who delivers a completed application to the administrator before the 1st day of January, 1992 shall be made in accordance with sections 9, 10, 36, 45 and 48 of the *Teachers' Superannuation Act, 1983* and with sections 7 to 14 of Ontario Regulation 423/84 as those sections read on the 31st day of December, 1989.

Idem

(2) The *Teachers' Superannuation Act, 1983* as it reads on the 31st day of December, 1989 continues to apply for the purpose of determining a purchase of credited service under subsection (1).

Idem

(2a) Despite subsections (1) and (2) a member who has delivered a completed application to the administrator before the 1st day of January 1992 who fails to pay all of the contributions required to complete the purchase of credited service applied for before the 31st day of December, 1994 shall receive credited service in an amount based upon the contributions plus interest which he or she has actually made. (Last amended June 28, 1990 - Effective June 28, 1990)

Transitional

(3) Sections 95, 96 and 99 apply with respect to a member's application before the 1st day of January, 1992 in the circumstances described in those sections.

End of transitional period

(4) A person is not eligible after the 31st day of December, 1994 to make or complete a purchase of credited service to which a predecessor Act applies.

Interest rate

(5) For the purpose of a purchase of credited service described in subsection (1) for a period on or after the 1st day of January, 1990, references to the applicable rate of interest in Ontario Regulation 423/84 shall be read as if they were references to the standard interest rate.

Idem

(6) Subsection 89 (3) (calculation of interest, transitional) does not apply with respect to a purchase of credited service described in subsection (1) for a period before the 1st day of January, 1990.

B. For Employment in Education

Absences

94. (1) In this section,

"absence" means either an employer-approved leave of greater than five consecutive school days or a break in service;

"break in service" means a period when a member is not employed in education or is absent from employment without the employer's consent.

(Last amended July 21, 2014 – Effective September 1, 2014)

Purchase re break in service

(2) A member may purchase credited service for a break in service approved by the administrator for a period of disability immediately following a period of employment in education, where the member ceases to be employed in education as a result of the disability and meets the definition of "disabled" as defined under Regulation 8500 (1) of the *Income Tax Act* (Canada). (Last amended August 4, 2011 – Effective December 2, 2010)

Application for purchase re break in service

(2a) A member shall apply to purchase credited service for a break in service within two years after the date when the member ceases, as a result of the disability, to be employed in education. (Last amended August 4, 2011 – Effective December 2, 2010)

Idem

(2b) The administrator shall accept an application to purchase credited service for a break in service that is made after the time described in subsection (2a) if the administrator is satisfied,

(a) that the delay in making the application resulted from a delay in diagnosing the disability; or

(b) that the member was unable, because of the effects of the disability, to make the application within the time described in subsection (2a).

(Last amended August 4, 2011 – Effective December 2, 2010)

Proof of disability

(2c) No application to purchase credited service for a break in service shall be considered by the administrator until the administrator has received the certificate of a medical doctor licensed in Ontario certifying that the applicant became mentally or physically disabled while employed in education and indicating the nature and degree of the disability. (Last amended August 4, 2011 – Effective December 2, 2010)

Ongoing proof of disability

(2d) The administrator may at any time require a member who has applied to purchase credited service for a break in service to furnish evidence, in such form as the administrator directs, that the member was disabled, as defined under Regulation 8500 (1) of the *Income Tax Act* (Canada), throughout the break in service. A member's entitlement to purchase credited service for a break in service shall terminate if the administrator is not satisfied that the member is disabled. (Last amended August 4, 2011 – Effective December 2, 2010)

Limit

(2e) Despite subsections 92 (1) and 92a (2), no member may purchase credited service for a break in service in respect of a period that is after the fifth anniversary of the start of the break in service. (Last amended August 4, 2011 – Effective December 2, 2010)

Application

(3) A member may apply to purchase credited service for an absence by notifying the administrator of the member's intent to purchase. (Last amended December 30, 2009 - Effective September 1, 2010)

(3a) A member may only purchase credit for an absence for service outside of Canada, where that service was arranged by the member's employer, if the purchase is made on an ongoing basis during the period of the leave. (Last amended April 2, 2001 – Effective September 1, 2001)

Purchase re absence

(4) A member may purchase credited service for all or part of an absence. (Last amended April 2, 2001 – Effective September 1, 2001)

(4a) Despite subsection (4) a member on an absence from other than a full-time position is entitled to purchase credit under this section only for the time that, in the opinion of the administrator, the member would have been employed for compensation but for the absence. (Last amended December 30, 2009 - Effective September 1, 2010)

Idem

(5) No member may purchase credited service for an absence for the purpose of service in political office if the member is contributing to or is entitled to a pension under another registered pension plan other than the *Canada Pension Plan* or the *Quebec Pension Plan* in respect of the service.

Amount of contribution

(6) A member who purchases credited service on a monthly basis during the period of the absence shall contribute,

(a) the required contributions, based on the pensionable salary that the member's employer advises the administrator that the member would have earned, if the member were not absent, and as if the member were not required to contribute to the *Canada Pension Plan* or to the *Quebec Pension Plan*; and

(b) for any late monthly payments, interest thereon calculated at the standard interest rate from the date each contribution would have been made and ending on the day before the payment is made. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(6a) A member who purchases credited service other than on a monthly basis during the period of the absence shall contribute, on or before the end of the month in which the fifth anniversary of the end of the absence occurs, a lump sum which is equal to,

(a) the required contributions, based on the pensionable salary that the member's employer advises the administrator that the member would have earned, if the member were not absent, and as if the member were not required to contribute to the *Canada Pension Plan* or to the *Quebec Pension Plan*; and

(b) interest thereon calculated at the standard interest rate from the date each contribution would have been made and ending on the day before the payment is made. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(6b) Despite subsections (6) and (6a), a member who purchases credited service on or after the 1st day of September, 2010, shall contribute, on or before the end of the month in which the fifth anniversary of the end of the absence occurs,

(a) the required contributions, based on the pensionable salary as determined in accordance with section 14, and as if the member were not required to contribute to the *Canada Pension Plan* or to the *Quebec Pension Plan*; and

(b) interest thereon calculated at the standard interest rate from the first day of the month following the month in which the end of the absence occurs and ending on the day before the payment is made. (Last amended December 30, 2009 - Effective September 1, 2010)

Transition

(6c) Subsection (6b) shall only apply where the member has not previously completed payment for the purchase of the entire eligible absence period. (Last amended October 19, 2012 - Effective September 1, 2010)

Transition: Interest calculation for the portion of an absence previously considered complete

(6d) Despite subsections (6b) and (6c), where, in the opinion of the administrator, payment was considered to be complete as of the 1st day of September, 2010 for a portion of the entire eligible absence period, the interest applicable to that portion of the absence shall be calculated in accordance with subsection (6) (b) or (6a) (b). (Last amended October 19, 2012 - Effective September 1, 2010)

Due date

(7) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Return date

(8) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Matching contributions for purchases

(9) A contribution under subsection (6), (6a) or (6b) is considered to be a required contribution for the purpose of sections 25 and 26, and the required matching contribution shall be paid by the employer making the employer contributions in respect of the member immediately before the absence. (Last amended December 30, 2009 - Effective September 1, 2010)

Idem

(9a) Despite subsection (9), where a member was employed by a designated private school or a designated organization immediately before the absence and the employer is dissolved or in receivership at the time of the member's application to purchase credited service, the required matching contribution for a purchase of credited service for a break in service shall be paid by the member. (Last amended August 4, 2011 – Effective December 2, 2010)

Amount of contribution, delayed election

(10) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Advance payments

(11) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(12) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

No refund

(13) A member who makes contributions for an absence is not entitled to a refund of those contributions at any time, except to the extent that the member's purchase is not completed in accordance with subsection 92a.(1). (Last amended April 2, 2001 – Effective September 1, 2001)

Proportionate credit

(14) A member who does not complete payment for the full period of an absence shall receive proportionate credit. (Last amended April 2, 2001 – Effective September 1, 2001)

Maximum purchase, birth or adoption

(15) Despite subsection 92 (1) a member may also purchase a maximum of three years of credited service in respect of absences after the 31st day of December, 1990 taken at the birth or adoption of the member's children. (Last amended April 2, 2001 – Effective September 1, 2001)

Idem

(16) For the purposes of subsection (15) a member may purchase a maximum of one year of credited service for an absence taken at the birth or adoption of the member's child or if more than one child is born or adopted at once, in respect of one such birth or adoption. (Last amended April 2, 2001 – Effective September 1, 2001)

Eligibility for purchase

(17) Revoked. (Last amended May 5, 2010 – Effective September 1, 2009)

Lump sum payments

(18) Revoked. (Last amended June 28, 1990 - Effective June 28, 1990)

End Date

(19) For the purposes of this section, the end of an absence occurs on the last day that, in the opinion of the administrator, the member could have worked if not for the absence. (Last amended December 30, 2009 - Effective September 1, 2010)

End date

(20) Despite subsection (19), the end of an absence for a member who purchases credited service for a break in service shall be no later than the fifth anniversary of the start of the break in service. (Last amended October 19, 2012 - Effective September 1, 2010)

Transitional rules

94a. (1) A member whose absence ended prior to September 1, 2001 and who,

(a) returned to employment in education, following the absence, on or after September 1, 1996 but prior to September 1, 2001, or

(b) did not return to employment in education, following the absence, prior to September 1, 2001,

shall have until December 31, 2004 to complete a purchase of the absence. (Last amended April 2, 2001 – Effective September 1, 2001)

(2) A member who completes a purchase in accordance with subsection (1) shall contribute a lump sum on a contributions plus interest basis calculated in accordance with subsection 94 (6a). (Last amended April 2, 2001 – Effective September 1, 2001)

(3) A member whose absence ended prior to September 1, 2001 and who returned to employment in education, following the absence, prior to September 1, 1996 shall have until December 31, 2002 to complete a purchase of the absence by notifying the administrator by that date and by making the purchase within 90 days of the provision of a purchase cost quotation. (Last amended April 2, 2001 – Effective September 1, 2001)

(4) A member who completes a purchase in accordance with subsection (3) shall contribute a lump sum which is, on the date of the purchase, equal to the actuarial cost of the expected pension improvement. (Last amended April 2, 2001 – Effective September 1, 2001)

(5) This section shall only apply where the member has not previously completed a purchase of the absence, in which case the member may complete the purchase in accordance with this section without having to meet the requirements of subsection 94 (3) as it read on August 31, 2001. (Last amended April 2, 2001 – Effective September 1, 2001)

Transitional application deadline re: breaks in service

94b. (1) A member may purchase credited service for a break in service in accordance with subsection 94 (2) as it read on the 1st day of December, 2010, if the member delivers to the administrator a completed application to purchase credit, in the form provided by the administrator, including all supporting documents, by the 31st day of August, 2011. (Last amended August 4, 2011 – Effective December 2, 2010)

Transitional payment deadline re: breaks in service

(2) Despite subsections 94 (6) to (6c), a member described in subsection (1) shall have until the 30th day of December, 2011 to complete payment of the amount required under subsection 94 (6b). (Last amended August 4, 2011 – Effective December 2, 2010)

Absence during a school year

95. (1) Revoked. (Last amended June 20, 2012 – Effective January 1, 2012)

Amount of contribution

(2) Revoked. (Last amended June 20, 2012 – Effective January 1, 2012)

Interest payable

(3) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Status of contributions

(4) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Due date

(5) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Required contribution

(6) Revoked. (Last amended April 2, 2001 – Effective September 1, 2001)

Absence re strike or lockout

96. (1) A member may contribute for days that the member is absent from employment in education for the purpose of participating in a legal strike or because of a lockout. (Last amended April 2, 2001 – Effective September 1, 2001)

Amount of contribution

(2) The member shall contribute the amount of the member's required contribution for each day of absence plus the amount of the corresponding employer's contribution.

Interest payable

(3) The member shall pay interest, calculated at the standard rate, on any contribution received by the administrator more than one month after the end of the absence. (Last amended June 1, 1995 - Effective June 1, 1995)

For former membership

97. (1) This section applies with respect to a member who previously received a refund of required contributions under the pension plan. (Last amended April 2, 2001 – Effective September 1, 2001)

Eligibility

(2) No member may purchase credited service under this section until the member has accumulated, through employment in education, seventy days of credited service in one school year after returning to active membership.

Election within one year

(3) A member who elects to purchase credited service on or before the later of the first anniversary of the member's return to active membership and the 1st day of January, 1994 shall contribute the amount previously refunded together with interest thereon from the date the refund was made to the first day of the month in which the contribution is paid, calculated at the standard interest rate in effect on the date the refund was made. (Last amended April 2, 2001 – Effective September 1, 2001)

Limit

(4) No member may purchase more days of credited service under subsection (3) than the number of days in respect of which the member received the refund.

Due date

(5) A contribution under subsection (3) shall be paid as a lump sum before the later of the third anniversary of the member's return to active membership and the 1st day of January, 1995.

Required contribution

(6) A member who elects to purchase credited service after the deadline referred to in subsection (3) or who fails to make the payment before the deadline in subsection (5) shall contribute a lump sum which is, on the date of the purchase, equal to the actuarial cost of the expected pension improvement.

Repurchase of credited service

97a. (1) A member referred to in section 37 who becomes re-employed in education for more than 20 days in one school year may purchase credited service in an amount not greater than the credited service in respect of which a transfer and refund were made under that section. (Last amended February 28, 1992 - Effective January 1, 1992)

Amount of contribution

(2) A member who elects to purchase credited service under subsection (1) shall contribute a lump sum equal to the greater of,

(i) the amounts transferred and refunded under section 37 together with interest thereon calculated at the standard rate from the day of the transfer or refund to the day before the payment is made; or

(ii) the actuarial cost, on the date of the purchase, of the expected pension improvement. (Last amended February 28, 1992 - Effective January 1, 1992)

Approved service outside Ontario

98. (1) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

Idem

(2) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

Limit

(3) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Amount of contribution

(4) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

Transitional re designated private schools

99. (1) This section applies to an active member,

(a) who is employed in an organization designated under the *Teachers' Superannuation Act, 1983* or in a school within the meaning of section 1 of the *Education Act*;

(b) who was employed before the 1st day of September, 1986 in a private school designated under a predecessor of this Act;

(c) who was employed on the 1st day of September, 1986 and for at least twenty days during the school year beginning on that date in an organization designated under the *Teachers' Superannuation Act, 1983* or in a school within the meaning of section 1 of the *Education Act*; and

(d) who elected before the 1st day of September, 1986 to be excluded from the benefits and obligations of the predecessor Act.

Purchase

(2) An active member may purchase credited service in accordance with subsections 13 (4), (6) and (7) of Ontario Regulation 423/84 as they read on the 31st day of December, 1989, with necessary modifications, for past teaching service in a private school designated under a predecessor of this Act.

Idem

(3) No member is entitled to apply to purchase credited service under this section after the 31st day of December, 1991.

C. For other Employment

For war service

100. (1) Revoked. (Last amended September 8, 2006 – Effective December 31, 2006)

Idem

(2) Revoked. (Last amended September 8, 2006 – Effective December 31, 2006)

For teaching special subjects

101. (1) Revoked. (Last amended September 8, 2006 – Effective December 31, 2006)

Idem

(2) Revoked. (Last amended September 8, 2006 – Effective December 31, 2006)

For foreign service as an educator

102. (1) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

Eligibility

(2) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

Limit

(3) Revoked. (Last amended February 28, 1992 - Effective January 1, 1992)

Amount of contribution

(4) Revoked. (Last amended December 20, 1999 - Effective January 1, 1992)

For other employment, R.S.C. 1952, c. 148

103. (1) A member may purchase credited service in the pension plan for employment not otherwise described in this Part if the employment was pensionable service under another pension plan registered under the *Income Tax Act* (Canada). (Last amended April 2, 2001 – Effective September 1, 2001)

Transfer from other plan

(2) For service prior to January 1, 1992, all funds associated with the service under the other plan shall be transferred to the pension plan and applied to the cost of the member's expected benefit improvement. Where no funds remain in the other plan, the member is not entitled to purchase pre-1992 credited service under this section. (Last amended September 8, 2006 - Effective January 1, 1992)

Amount of contribution

(3) For service after December 31, 1991, the member shall contribute an amount equal to the actuarial cost of the expected benefit improvement. (Last amended June 29, 1994 - Effective January 1, 1992)

(4) If the amount transferred under subsection (2) is less than the actuarial cost of the expected benefit improvement, the member shall contribute a lump sum which, on the date of the purchase, is equal to the difference. (Last amended June 29, 1994 - Effective January 1, 1992)

D. Reciprocal Agreements

Reciprocal agreements

104. (1) The administrator may enter into an agreement with the authorized representative of another pension plan respecting the terms upon which persons may transfer benefits and contributions between that plan and the pension plan.

Idem

(2) A reciprocal agreement must provide that a person transferring benefits and contributions to the pension plan acquires a benefit under the plan based upon the actuarial cost of the expected benefit on the date of the transfer.

(3) If a reciprocal agreement provides that a person may elect to pay directly to the administrator part or all of the difference between the required amount and the amount transferred (the "shortfall"), and provides the administrator with the authority to establish a deadline by which a person must complete payment of the shortfall, a person who elects to pay the shortfall shall complete such payment on or before the end of the month in which the fifth anniversary of the date the application to transfer was received by the administrator occurs. (Last amended June 20, 2012 – Effective September 1, 2001)

Reciprocal agreements, transitional

105. (1) Subject to subsection (2), reciprocal agreements entered into before the 1st day of January, 1990 by the Teachers' Superannuation Commission under section 49 of the *Teachers' Superannuation Act, 1983* are continued and expire on the 31st day of December, 1996.

Idem

(2) Reciprocal agreements referred to in subsection (1) do not expire on the 31st day of December, 1996 if, before that date, the reciprocal agreement is amended to include a term described in subsection 104 (2) or if the agreement includes such a term.

E. Administration

Application for purchase

106. An application to purchase credited service shall be made in a form provided by the administrator and shall be delivered to the administrator.

Applicability

106a. (1) Subsections 11 (6) to (9), 14 (1a) to (1i), 15 (2b), 94 (4a), (6b), (6c) and (9), as they read on the 1st day of September, 2010 apply to members who cease to be employed in education before the 1st day of September, 2010. (Last amended August 4, 2011 – Effective September 1, 2010)

Idem

(2) Subsections 94 (2) to (2e) and section 94b, as they read on the 2nd day of December, 2010 apply to members who cease to be employed in education before the 2nd day of December, 2010. (Last amended August 4, 2011 – Effective December 2, 2010)

Idem

(3) Section 84, as it read on the 1st day of January, 2014, applies to members who cease to be employed in education before the 1st day of January, 2014. (Last amended January 15, 2014 – Effective January 1, 2014)

Employed in education

106b. For a member who ceases to be employed in education before, on or after the 1st day of January, 2011, credited service purchased in accordance with subsection 94 (2) in respect of a period on or after the 1st day of January, 2011 is considered to be employment in education for the purposes of determining benefits. (Last amended August 4, 2011 – Effective January 1, 2011)

Effective date of purchase

107. A purchase of credited service is effective on the day the payment in relation to the purchase is made. (Last amended April 2, 2001 – Effective September 1, 2001)

Purchase of partial credit

108. A member who is entitled to purchase credited service for a period of employment or an absence may purchase credited service for a part of the employment or absence. (Last amended April 2, 2001 – Effective September 1, 2001)

Contribution by spouse, etc.

109. A member who dies before completing a purchase of credited service shall receive credited service in an amount based upon the contributions plus interest which he or she has made. (Last amended June 29, 1994 - Effective January 1, 1992)

Idem

(2) Revoked. (Last amended June 29, 1994 - Effective January 1, 1992)

Lump sum payments

109a. A lump sum payment under this Part may consist of,

(a) a partial payment by means of a transfer permitted under the *Income Tax Act* (Canada); and

(b) a second payment of the balance of the amount required to pay for the credited service being purchased by the lump sum. (Last amended June 28, 1990 - Effective June 28, 1990)

Eligibility for purchase

109b. A member is not eligible to purchase credited service while receiving a pension. (Last amended May 5, 2010 – Effective September 1, 2009)

PART X
ADMINISTRATION OF THE PLAN

A. General

Extension of time

110. The administrator may extend any time limit under the pension plan before or after the expiration of the time if the administrator is satisfied that there are reasonable grounds for the extension, and may give such directions as the administrator considers appropriate consequent upon the extension.

Provision of information

111. (1) The administrator shall provide to each member of the pension plan the information and documents required under this Act or any other Act.

Idem, to administrator

(2) A member, a person who applies for, or receives, a pension, refund or other payment from the pension fund, a board of education or an employer of a member shall provide the administrator, upon request, with such information as the administrator may require to administer the pension plan.

(2a) The administrator may conduct an audit of the records of a board of education or an employer for the purpose of validation of information required for administration of the pension plan. (Last amended June 20, 2012 – Effective January 1, 2012)

Idem, to members

(3) The administrator shall provide within a reasonable time to a member, upon written request, all information relating to the member's contributions and entitlements under the pension plan.

Fiscal year

112. The fiscal year of the pension plan is the twelve-month period that begins on the 1st day of January.

Actuarial calculations

113. Actuarial calculations and determinations required under the pension plan shall be made using such actuarial assumptions, principles and methods as may be required or adopted by the administrator.

B. Pension Fund

Payments from pension fund

114. A payment required under the pension plan must be paid from the pension fund.

Requirement to invest

115. Moneys in the pension fund that are not required to be paid out must be invested to meet the obligations of the pension plan.

C. Surplus and Deficiency

Actuarial gain

116. Revoked. (Last amended January 24, 1992 - Effective January 1, 1992)

Surplus

117. Revoked. (Last amended January 24, 1992 - Effective January 1, 1992)

Requirement to contribute to deficit

118. Revoked. (Last amended November 15, 1993 - Effective November 15, 1993)

PART XI
DESIGNATION OF PRIVATE SCHOOLS AND ORGANIZATIONS

Private schools

119. (1) The Partners' Committee by notice to the administrator may designate a school, college, academy or other educational institution as a designated private school for the purpose of the pension plan,

(a) if it gives instruction equivalent to that given in elementary or secondary schools in Ontario;

(b) if it is not supported in any way by school taxes or by provincial or municipal grants; and

(c) if it meets the criteria set out in subsection (3). (Last amended June 1, 1995 - Effective January 1, 1992)

Organizations

(2) The Partners' Committee by notice to the administrator may designate an organization as a designated organization for the purpose of the pension plan,

(a) if it provides services related to elementary or secondary education; and

(b) if it meets the criteria set out in subsection (3). (Last amended June 1, 1995 - Effective January 1, 1992)

Criteria

(3) The school, college, academy or other educational institution or the organization,

(a) must not be operated for profit or gain and any profits must be used to carry out its objects; and

(b) by its governing body must undertake in writing to make the reports described in subsection (5), to pay the amounts described in subsection (6), and to perform all administrative functions required of an employer for the purposes of the pension plan.

Effective date of designation

(4) A notice of designation under subsection (2) shall specify the effective date. (Last amended April 15, 1998 - Effective January 1, 1992)

Reports

(5) The administrator may require a designated private school or designated organization to make annual reports for the purpose of the administration of this Act and the pension plan and to supply such information as to its constitution, operations, teaching staff and otherwise as the administrator may require.

Payments under the plan

(6) A designated private school or designated organization shall, in accordance with the pension plan, make the employer contributions and collect and remit the contributions by its employees who become active members of the pension plan.

Past service in prescribed schools and institutions

119a.(1) Revoked. (Last amended June 1, 1995 - Effective January 1, 1992)

(2) Revoked. (Last amended June 1, 1995 - Effective January 1, 1992)

Termination of designation

120. (1) Revoked. (Last amended June 1, 1995 - Effective January 1, 1992)

Grounds

(2) The Partners' Committee by notice to the administrator may terminate the designation of a designated private school or a designated organization,

(a) if the designated private school or designated organization, by its governing body, has requested the termination of the designation;

(b) if the designated private school or designated organization is not complying with its undertakings; or

(c) if there is a change in the objects or mode of carrying out the objects of the designated private school or designated organization. (Last amended June 1, 1995 - Effective January 1, 1992)

Notice and submissions

(3) The Partners' Committee shall give notice of the termination to the governing body and to the employees of the designated private school or designated organization who are active members of the pension plan. (Last amended June 1, 1995 - Effective January 1, 1992)

Effective date

(4) A notice of termination of designation shall specify the effective date. (Last amended June 1, 1995 - Effective January 1, 1992)

Effect of termination of designation

(5) Upon the termination of a designation, the employees of the private school or the organization cease to be eligible to be active members of the pension plan.

Idem

121. (1) Revoked. (Last amended December 21, 2007 - Effective September 1, 2008)

Effective date

(2) Revoked. (Last amended December 21, 2007 - Effective September 1, 2008)

Designations, transitional

122. The designation of a designated private school, designated organization and a designated capacity under the *Teachers' Superannuation Act, 1983* that is in effect on the 31st day of December, 1989 shall have effect as a designation made under this Part.

PART XII-ONTARIO TEACHERS' PENSION PLAN BOARD (REVOKED)

(Last amended January 24, 1992 - Effective January 1, 1992)

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20150928 amendment.pdf

ONTARIO TEACHERS' PENSION PLAN

AMENDMENT TO THE ONTARIO TEACHERS' PENSION PLAN

This is an agreement

B E T W E E N

Her Majesty the Queen
in right of the Province of Ontario
as represented by the Minister of Education

(the "Minister")

and

The Ontario Teachers' Federation
as represented by its Executive

(the "OTF")

WHEREAS the Minister and the OTF (collectively the "Partners") have established a partnership to administer the Ontario Teachers' Pension Plan and Fund, pursuant to an agreement between the Partners dated July 15, 1991 (the "Partners' Agreement"); and

WHEREAS paragraph 104 of the Partners' Agreement provides that the Partners may at any time agree to change any of the provisions of the Ontario Teachers' Pension Plan being Schedule 1 to the *Teachers' Pension Act*, as amended (the "Plan"); and

WHEREAS the Plan was most recently amended on September 22, 2015;

WHEREAS the Partners wish to amend the Plan further;

NOW THEREFORE the Partners agree as follows:

WIND UP

1. Section 118a is added to the Plan:

Wind Up

118a. If the pension plan is wound up within the meaning of the *Pension Benefits Act*, the assets of the pension fund shall first be used to pay or satisfy properly incurred liabilities to creditors, following which the remaining assets of the pension fund shall be used to pay or satisfy the accrued benefit entitlements of members, former members, retired members and any other persons entitled to a benefit under the pension plan in respect of a member, former member, or retired member before any other distribution is made.

Effective on the date this agreement is countersigned by both Partners.

Her Majesty the Queen
in right of the Province of Ontario
as represented by the
Minister of Education

Liz Sandals
Minister of Education

Date: Sept 28/15

The Ontario Teachers' Federation
as represented by its Executive

Francine LeBlanc-Lebel
OTF President

Date: 27 September, 2015

20150922 amendment.pdf

TEACHERS' PENSION PLAN

AMENDMENT TO THE TEACHERS' PENSION PLAN

This is an agreement

B E T W E E N

Her Majesty the Queen
in right of the Province of Ontario
as represented by the Minister of Education

(the "Minister")

and

The Ontario Teachers' Federation
as represented by its Executive

(the "OTF")

WHEREAS the Minister and the OTF (collectively the "Partners") have established a partnership to administer the Ontario Teachers' Pension Plan and Fund, pursuant to an agreement between the Partners dated July 15, 1991 (the "Partners' Agreement"); and

WHEREAS paragraph 104 of the Partners' Agreement provides that the Partners may at any time agree to change any of the provisions of the Ontario Teachers' Pension Plan being Schedule 1 to the *Teachers' Pension Act*, as amended (the "Plan"); and

WHEREAS the Plan was most recently amended on July 21, 2014; and

WHEREAS the Partners wish to amend the Plan further;

NOW THEREFORE the Partners agree as follows:

Credit for Service

1. Effective April 20, 2015, subsection 10 (4) of the Plan is revoked and replaced with the following:

Limitation

10. (4) Except for periods of lockout or legal strike or the strikes declared illegal by the Ontario Labour Relations Board on May 26, 2015 for the following periods:

(a) Durham District School Board – April 20, 2015 - May 26, 2015
(b) Rainbow District School Board – April 27, 2015 - May 26, 2015
(c) Peel District School Board – May 4, 2015 - May26, 2015,

a person shall not receive credited service for employment unless contributions in respect of the employment are made by or on behalf of that person.

For Employment in Education

2. Effective April 20, 2015, subsection 96 (1) of the Plan is revoked and replaced with the following:

Absence re strike or lockout

96. (1) A member may contribute for days that the member is absent from employment in education for the purpose of participating in a legal strike or the strikes declared illegal by the Ontario Labour Relations Board on May 26, 2015 for the following periods:

(a) Durham District School Board – April 20, 2015 - May 26, 2015
(b) Rainbow District School Board – April 27, 2015 - May 26, 2015
(c) Peel District School Board – May 4, 2015 - May26, 2015,

or because of a lockout.

Her Majesty the Queen
in right of the Province of Ontario
as represented by the
Minister of Education

Liz Sandals
Minister of Education

Dated at Toronto this 22nd day
of September, 2015.

The Ontario Teachers' Federation
as represented by its Executive

Francine LeBlanc-Lebel
OTF President

Dated at Toronto this ____ day
of _____, 2015.

20151128 amendment.pdf

ONTARIO TEACHERS' PENSION PLAN

AMENDMENT TO THE ONTARIO TEACHERS' PENSION PLAN

This is an agreement

B E T W E E N

Her Majesty the Queen
in right of the Province of Ontario
as represented by the Minister of Education

(the "Minister")

and

The Ontario Teachers' Federation
as represented by its Executive

(the "OTF")

WHEREAS the Minister and the OTF (collectively the "Partners") have established a partnership to administer the Ontario Teachers' Pension Plan and Fund, pursuant to an agreement between the Partners dated July 15, 1991 (the "Partners' Agreement"); and

WHEREAS paragraph 104 of the Partners' Agreement provides that the Partners may at any time agree to change any of the provisions of the Ontario Teachers' Pension Plan being Schedule 1 to the *Teachers' Pension Act*, as amended (the "Plan"); and

WHEREAS the Plan was most recently amended on September 28, 2015; and

WHEREAS the Partners wish to amend the Plan further;

NOW THEREFORE the Partners agree as follows:

Re-employment

1. Effective September 1, 2010, subsection 46 (5) of the Plan is revoked and replaced with the following:

"Re-employed pensioner" limitation

46. (5) The term "re-employed pensioner" shall include a member who provides services, other than as a teacher, to a ministry of the Government of Ontario only if:

(a) the ministry is the Ministry of Education, and

(b) the member's retirement pension under the plan begins after September 1, 2010.

2. Effective September 1, 2010, subsection 46(6) of the Plan is amended by adding the words "Despite subsection 46(5)," at the beginning of the subsection.

3. Effective September 1, 2015, subsection 46 (6) of the Plan is revoked.

Her Majesty the Queen
in right of the Province of Ontario
as represented by the
Minister of Education

Liz Sandals

Liz Sandals
Minister of Education

Date: Nov 28/15

The Ontario Teachers' Federation
as represented by its Executive

Francine LeBlanc-Lebel

Francine LeBlanc-Lebel
OTF President

Date: Nov. 23, 2015

Current - Partners’ Agreement - 03-06-15.pdf

This is an AGREEMENT

BETWEEN:

Her Majesty the Queen
in right of the Province of Ontario
represented by the Minister of Education and Training
("the Minister")

and

The Ontario Teachers' Federation
represented by its Executive
("the OTF")

These are the terms to which the Minister and the OTF agree;

Introduction

1. The Minister and the OTF have agreed to establish a partnership for the purpose of designing and administering the Ontario Teachers' Pension Plan and managing the Ontario Teachers' Pension Fund.

2. It is the intention of the partners that this partnership will start on the 1st day of January, 1992.

3. In this agreement,

(a) the Minister and the OTF will be referred to as the "partners" or the "partnership",

(b) the Ontario Teachers' Pension Plan Board continued by the *Teachers' Pension Act, 1989* will be referred to as "the Board",

(c) the Ontario Teachers' Pension Plan continued by the *Teachers' Pension Act, 1989* will be referred to as the "pension plan" or the "plan" and,

(d) the Ontario Teachers' Pension Fund continued by the *Teachers' Pension Act, 1989* to provide benefits in respect of the pension plan will be referred to as the "pension fund" or the "fund".

4. The partnership established by this agreement is intended to govern all aspects of the plan and the fund. Wherever this agreement differs with any law, that part of the agreement is of no effect but the rest of the agreement continues to govern the plan and the fund.

5. The Minister agrees to do everything possible to make sure that the Teachers' Pension Plan Board will not be considered a Scheduled Agency under the Guidelines of the Management Board of Cabinet.

6. The Minister agrees to do everything possible to have subsection 43(3) of Ontario Regulation 708/87 amended to provide that the pension fund is no longer exempted from the application of subsection 23(1) of the *Pension Benefits Act.*

7. The Minister may designate one or more persons to act in the Minister's place under this agreement. The OTF may designate one or more persons to act in its place under this agreement.

Role of the partners

8. The partners will be responsible for designing the plan structure, setting the benefits of the plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, making changes to the plan, this agreement or other plan documents, deciding whether or not to file a valuation more frequently than required by the *Pension Benefits Act*, appointing the Board, and defining the role of the Board.

9. The partners will enter into a memorandum of understanding with the Board setting out,

(a) the duties of the Board,

(b) the process for consultation in the preparation of valuations,

(c) the process for consultation on the amount of money to be paid to members of the Board, including the Chair and to members of committees appointed by the Board,

(d) the actuarial methods which the Board will use in valuing the plan and,

(e) any other terms of the relationship between the partners and the Board to which the partners agree.

10. The partners agree that every three years they will follow the procedure described in this agreement to meet and negotiate changes to the plan.

11. Either partner may ask the other to meet at any time to discuss changes to any of the matters referred to in paragraph 8 and the partners agree to make their best efforts to do so.

11a. The partners agree to meet as required to discuss the amount of the Minister's contribution due on the first business day of January that is to be deferred to the first business day of April of the same year and to determine the interest rate to be applied for the period of the deferral; determination of such interest rate to be guided by the principle that the Teachers' Pension Plan not be disadvantaged by the deferral. (Last amended May 29, 1992 - Effective May 29, 1992)

11b. The partners agree that the payment of a portion of the Minister's contribution that is due on the first business day of January of 1994 and a portion of the Minister's contribution that is due on the first day of January of 1995 may be deferred to March 31 of each respective year; the amount of the deferral, with interest, to equal $200 million in 1994 and $125 million in 1995; amounts to be adjusted to reflect payments authorized under Paragraph 65. (Last amended November 15, 1993 - Effective November 15, 1993)

12. If the Board advises the partners that a change must be made to the plan to comply with any law the partners agree that they will meet as soon as possible to discuss it.

13. The partners will establish a Partners Committee by each appointing three members. Either partner may refer to the Committee any matter referred to in paragraph 8 or 12 when no agreement results from discussion of the matter.

14. The Partners Committee may by agreement use the services of the manager of negotiations referred to in paragraph 76 to resolve any dispute. The Committee may by agreement use any dispute resolution mechanism including voluntary arbitration to resolve any dispute.

15. Either partner may ask the actuary hired by the Board to provide or prepare any information which that partner thinks it needs in discussing changes to the plan. The cost of the actuary in preparing that information will be paid out of the fund. The information will be provided to both partners.

15a. The partners may initiate, with the Board, discussions, reviews and research regarding the funded status of the plan including the design of conditional inflation protection, the reasonable costs of such reviews and research to be paid out of the fund subject to the prior approval of the Board. (Last amended October 9, 2008 – Effective January 1, 2009)

16. Either partner may audit the plan and the fund at any time at the expense of that partner. The Board will cooperate in the audit.

Role of the Board

17. The Board is responsible for the administration of the pension plan, the management of the pension fund and all other matters set out in this agreement.

18. The Board may exercise every power necessary to administer the pension plan, manage the pension fund and fulfil every other task which the partners assign to it.

19. The responsibilities of the Board include,

(a) investing and managing the pension fund to do all things possible so that the obligations of the pension plan will be met,

(b) preparing a valuation at least every three years to comply with the *Pension Benefits Act,*

(c) preparing annual valuations if the Board decides it is appropriate and providing preliminary results to the partners as soon as they are available,

(d) deciding on the actuarial assumptions used in administering the plan and in preparing valuations of the plan,

(e) consulting with the partners during the preparation of a valuation and making its best effort to respond to any comments and recommendations of the partners. The content of a final valuation is the decision of the Board,

(f) giving a copy of every valuation prepared for the Board to each partner and giving any information requested by a partner to each partner as quickly as possible,

(g) having the plan and the fund audited every year,

(h) preparing a report at the end of every fiscal year that tells how the plan and the fund have been doing in that year,

(i) holding a meeting with both partners at least once each year to explain the annual report to them and to answer any questions about the plan and fund,

(j) making sure that the plan and the fund are administered and managed to comply with all laws that affect them,

(k) advising the partners about any changes to the plan that need to be made to comply with the law,

(l) advising the partners about changes that would improve the administration of the plan,

(m) interpreting the plan and determining benefit entitlements,

(n) developing an investment policy and giving a copy to each partner and to the Financial Services Commission of Ontario,

(o) making rules regarding the conduct of its business,

(p) appointing or electing a vice Chair and any other officers that the Board feels are necessary for the conduct of its business.

The Board

20. The Board will have a maximum of nine members. The partners will each appoint four members.

21. The ninth member of the Board will be the Chair. The process for appointing a Chair is set out in the next section of this agreement.

22. The Minister and the OTF will each appoint two members to the Board to terms ending on the 31st day of December, 1992.

23. The Minister and the OTF will each appoint two members of the Board whose terms will end on the 31st day of December, 1993.

24. If a person appointed under paragraph 19 or 20 is a member of the Board when the partnership starts, the Lieutenant Governor in Council will make an Order changing the length of that person's term.

25. After the expiry of the term of a member of the Board who holds office on the 1st day of January, 1992 the partner who recommended to the Lieutenant Governor in Council the appointment of that member will fill the vacancy by appointing or re-appointing.

26. Unless a member cannot complete his or her term, is removed or is appointed after a member whose term was extended because of a delay in the appointment of his or her successor, the term of all members appointed after the 1st day of January, 1992 will be two years.

27. No person may be a member of the Board for more than four consecutive terms. The initial term of a member who is appointed as a successor under paragraph 29, or as a new member under paragraph 30 or 31, shall not be counted in the number of consecutive terms a member may serve. (Last amended January 15, 2014 – Effective January 1, 2014)

28. If no appointment is made to fill the vacancy at the end of a member's term, the member will continue in office until an appointment is made.

29. When a successor is appointed to a term after his or her predecessor's term has been extended for failure to appoint a successor, the successor's term will end two years after the predecessor's term would have ended but for the delay in appointment.

30. If a member of the Board cannot finish his or her term then the partner who appointed the member may appoint a new member for a term ending on the date when the term of the departing member would have ended.

31. At any time either partner may remove a board member whom that partner has appointed and appoint a new member for a term ending on the date when the term of the departing member would have ended.

The Chair

32. The partners may decide together on the person to be appointed as Chair of the Board. The partners agree to meet six months before the term of the Chair of the Board expires to discuss candidates, and attempt to agree upon the Chair.

33. Either partner may initiate the selection of a Chair in the following way as an alternative to the discussion referred to in paragraph 32,

(a) The partners will each prepare a list of at least three persons that they would like to be Chair. The partners will give each person named a number indicating priority. The lowest priority will be indicated by the number equal to the number of persons on the list.

(b) The partners will then examine the list prepared by the other.

(c) If one name appears on both lists that person will be appointed Chair.

(d) If two or more persons appear on both lists the priority ratings given to those persons by each partner will be added together. The person whose priority rating adds to the lowest number will be appointed Chair.

(e) If no name appears on both lists the partners agree to consult together and to prepare and exchange lists until a name does appear on lists prepared by each.

34. The person selected by the partners will be the Chair for a term of two years beginning on the 1st day of January of the year following selection.

35. No person may be Chair for more than four consecutive terms. Previous terms served by a Chair as a board member shall not be counted in the number of consecutive terms a Chair may serve. (Last amended December 16, 1994 - Effective December 16, 1994)

36. The Lieutenant Governor in Council will make an order making the term of the current Chair of the Board end on the 31st day of December, 1991.

37. If no appointment is made to fill the vacancy at the end of a Chair's term then the Chair will continue in office until an appointment is made.

38. If the Chair cannot finish his or her term then the Minister and the OTF will select a new Chair. The new Chair will be appointed for a term ending on the date when the term of the departing Chair would have ended.

39. The Chair may vote on any matter the Board is considering.

Operation of the Board

40. The Board may appoint committees and delegate to them any function of the Board. The Board may appoint persons who are not Board members to sit on any committee.

41. Committee members will be appointed for a term of up to two years.

42. A quorum of the Board or a Committee is a majority of the members. No meeting of the Board or a Committee may conduct any business unless a member appointed by each partner is present.

43. The Board will decide on a reasonable amount of money to be paid to the Board members, Committee members and the Chair for time and effort spent on Board business. The money will be paid out of the pension fund.

44. If any Board or Committee member is a public servant of Ontario that person will only be paid for any income the person loses as a result of time spent on Board business and for his or her expenses of doing Board business.

45. Any expenses that the Board must pay to operate and to administer the pension plan and manage the pension fund will be paid out of the pension fund.

46. The Board will employ a Chief Executive Officer and such other staff as are necessary to carry out its responsibilities.

47. The Board may decide which of its employees will be able to participate in the Public Service Pension Plan established under the *Public Service Pension Act, 1989* and the Minister agrees to do all things possible to ensure that those employees are covered.

48. The Board may employ persons to provide it with professional, technical or other help.

49. The Board must employ an external actuary and an external auditor.

50. The Board's employees will be paid out of the pension fund.

Indemnification

51. (a) Subject to subsection (e), the Board shall indemnify a person or his or her heirs or legal representatives (the "Indemnee") against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment (collectively "Expenses"), reasonably incurred by the person in respect of any civil, criminal, administrative or investigative action or proceeding (collectively a "Proceeding") to which the person is made or threatened to be made a party by any person including the Board, by reason of being or having been a member, committee member, officer or employee of the Board or a person who acts or acted at the Board's direction as a member, director, officer, employee, partner or agent of another corporation, partnership, joint venture, trust or other enterprises (collectively "enterprise"), if,

i) the person acted honestly and in good faith with a view to the best interests of the Board or such other enterprise; and

ii) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, the person had reasonable grounds for believing that his or her conduct was lawful.

(Last amended August 4, 2011 – Effective September 1, 2000)

(b) In furtherance of its obligations under subsection (a) the Board may purchase and maintain insurance for the benefit of any person referred to in subsection (a) in relation to any Expenses that may be indemnifiable under subsection (a). (Last amended August 4, 2011 – Effective September 1, 2000)

(c) The Board's indemnification of a person referred to in subsection (a) and any cost of purchasing and maintaining insurance for the benefit of such person are expenses of operating and administering the pension plan and managing the pension fund and may be paid out of the pension fund. (Last amended August 4, 2011 – Effective September 1, 2000)

(d) The Board or a person referred to in subsection (a) may apply to the court for an order approving an indemnity under this section and the court may so order and make any further order it thinks fit. (Last amended August 4, 2011 – Effective September 1, 2000)

(e) An indemnity given pursuant to subsection (a) extends only to Expenses that exceed amounts otherwise recoverable (and, in fact, recovered) by the Indemnee under any indemnity or policy of insurance applicable in respect of a Proceeding, and is to be regarded specifically as excess to any such amounts. An indemnity given pursuant to subsection (a) shall be subject to the condition that, in the event any indemnor or insurer against whom an Indemnee may have a claim for indemnity shall decline to pay, deny liability or otherwise contest either a claim by a person or the due amount thereof, the Indemnee must, if so requested by the Board, co-operate with and assist the Board in pursuing any claim against the other indemnor or insurer as the case may be, in such manner and to the extent that counsel to the Board may recommend or advise in the circumstances. (Last amended August 4, 2011 – Effective September 1, 2000)

(f) In any case where the Board reasonably considers that a person has fulfilled the conditions set out in clauses (a)(i) and (ii), above, and that it is otherwise appropriate to do so, prior to any settlement or judgment the Board may make an advance to an Indemnee in respect of a person referred to in subsection (a) to defray Expenses incurred or to be incurred by the Indemnee in relation to a Proceeding on such conditions as the Board considers appropriate and necessary. Any advance made under this subsection (f) shall be repayable by the Indemnee if the Indemnee fails to meet the conditions set out in clauses a(i) and (ii), above, in respect of such person. (Last amended August 4, 2011 – Effective September 1, 2000)

(g) Where the Board considers it appropriate, the Board may enter into an indemnity agreement with any person and such agreement shall reflect the limitation of this provision. (Last amended August 4, 2011 – Effective September 1, 2000)

(h) The application of paragraph 51 is effective as of September 1, 2000. (Last amended August 4, 2011 – Effective September 1, 2000)

52. The Board may buy, sell or lease real estate either as an investment or to provide a place to carry on business.

53. The Board may delegate any of its powers or duties to a committee or to an employee. It may impose conditions on any delegation it makes.

54. A committee of the Board may delegate any of its tasks to an employee of the Board if the Board approves.

Initial unfunded liability

55. The going concern unfunded actuarial liability disclosed by the initial valuation of the pension fund as at the 1st day of January, 1990 will be paid by the Treasurer of Ontario out of the Consolidated Revenue Fund according to Schedule 2 of the *Teachers' Pension Act, 1989*.

56. Revoked. (Last amended November 15, 1993 - Effective November 15, 1993)

Gains and losses

57. A valuation which is prepared for filing with the Superintendent of Financial Services shall be actuarially balanced so that the present value of,

(a) benefits and costs to be paid out of the fund, and

(b) any contingency reserve,

are equal to the sum of the value of the plan's assets, including

(c) the present value of,

(i) the members' contributions,

(ii) the employers' contributions,

(iii) the outstanding balance of special payments to liquidate the going concern unfunded actuarial liability disclosed by the valuation as at January 1, 1990, and

(iv) any outstanding payments required to discharge a solvency deficiency. (Last amended March 5, 2002 - Effective April 2, 2001)

The IUL Settlement

57a. Notwithstanding any other provision in this agreement, and including without limitation, paragraphs 10, 55, 59, 60, 60a and paragraphs 73 to 101, during the IUL settlement period this paragraph shall apply to the application of actuarial gains.

(i) In this paragraph,

(a) the "initial unfunded liability settlement period" (the "IUL settlement period") means the period between January 1, 1998 and December 31, 2002 and includes any period of extension pursuant to subparagraph (v).

(b) the "initial unfunded liability" means the going concern unfunded actuarial liability disclosed by the initial valuation of the pension fund referred to in paragraph 55 of the agreement.

(ii) Notwithstanding subparagraph 19(c), during the IUL settlement period, an actuarial valuation for funding purposes of the pension fund shall be prepared by the Board's actuary as at the 1st day of January and filed annually with the Superintendent of Financial Services, unless the partners jointly agree to instruct the Board not to file the valuation.

(iii) Effective with the valuation as at January 1, 1998, any actuarial gains disclosed in a valuation prepared in accordance with subparagraph (ii) will be applied in the following order of priority:

(a) (1) to provide an early retirement pension calculated in accordance with subsection 43(4) of Schedule 1, to members who have accumulated at least that number of years of qualifying service that, when added to the member's age upon termination of employment in education, totals eighty-five years (the "factor 85 entitlement"), provided that such member so qualifies on or after June 1, 1998, and on or before December 31, 2002;

(2) to provide early retirement reductions measured from 85 points rather than 90 points for benefits calculated under sections 44 and 52 of Schedule 1 for members who cease to be employed in education between June 1, 1998 and December 31, 2002;

(b) to provide for a permanent reduction in the amount of the Canada Pension Plan or Quebec Pension Plan reduction for pension instalments payable on or after January 1, 1999 as provided for in subsection 81(3) of Schedule 1 by substituting "0.0060" for "0.0068" in the formula;

(c) to provide to members on an absence, as defined in subsection 94(1) of Schedule 1, that commences during the period from the 1st day of June, 1998 to the 31st day of December, 2002, an exemption from the requirement in subsection 94(3)(b) of Schedule 1 where the member is otherwise eligible to purchase credited service under that section, and where the member, at the beginning of the leave,

(1) was at least 60 years of age;

(2) has accumulated at least that number of years qualifying service that, when added to the member's age, totals 75 years; or

(3) has credited service which totals at least 30 years; and

(d) to eliminate the obligation on the Minister of Finance to make special payments on account of the initial unfunded liability, in accordance with this agreement.

(iv) Subject to subparagraphs (v) and (vi), if there are any actuarial gains remaining after providing for (iii) (a), (b), (c) and (d), such gains disclosed in the annual actuarial valuations for funding purposes up to and including the valuation as at January 1, 2002, will be available for benefit enhancements including, but not limited to, the renewal on a permanent or temporary basis of the factor 85 entitlement, member contribution rate reductions, or to be allocated to a contingency reserve, as determined by the OTF in its sole discretion. (Last amended March 5, 2002 - Effective April 2, 2001)

(v) (a) The sum of the actuarial gains available to the OTF under subparagraph (iv), including the actuarial gains disclosed in the valuation as at January 1, 2002, shall be equal to the present value of the special payments, before the application of actuarial gains pursuant to subparagraph (iii)(d), required to amortize the initial unfunded liability as determined by the Board's actuary and disclosed in the valuation as at January 1, 1998 (the "IUL amount"), and the increase in the going concern liabilities required to provide the benefits conferred by (iii)(a), (b) and (c) as determined by the Board's actuary as at January 1, 1998, (the "benefit cost amount"). The partners agree that, effective April 3, 2001, after recognition of plan changes adopted to that time, there remains $76 million in actuarial gains available to the OTF under subparagraph (iv). (Last amended March 5, 2002 - Effective April 2, 2001)

(b) In the event that the sum of the actuarial gains available to the OTF under subparagraph (iv) up to and including the actuarial gains disclosed in the valuation as at January 1, 2002 is less than the difference between the IUL amount and the benefit cost amount, all actuarial gains disclosed in any actuarial valuation for funding purposes subsequent to the valuation as at January 1, 2002, will be available for such benefit enhancements, member contribution rate reductions, or to be held in a contingency reserve, as determined by the OTF in its sole discretion, until the sum of the actuarial gains available to the OTF for such purposes equals the difference between the IUL amount and the benefit cost amount.

(c) In the event that the sum of the actuarial gains available to the OTF under subparagraph (iv) up to and including the actuarial gains disclosed in the valuation as at January 1, 2002 is less than the difference between the IUL amount and the benefit cost amount, the IUL settlement period shall be extended to the date that the sum of the actuarial gains available to the OTF under subparagraph (iv) and (v) equals the difference between the IUL amount and the benefit cost amount.

(vi) (a) Prior to April 1, 2001, if actuarial gains are available after provision has been made for (iii)(a) to (d), and the OTF wishes to apply such gains pursuant to subparagraph (iv) for benefit enhancements or member contribution rate reductions, the partners shall meet to determine the effective date for the implementation of such benefit enhancements or contribution rate reductions.

(b) Subsequent to April 1, 2001, the OTF may, at its sole discretion, determine when such benefit enhancements or contribution rate reductions, are to be implemented. The Minister agrees to waive his consent to the plan amendments necessary to implement such benefit enhancements or member contribution rate reductions, provided these amendments are not filed by the OTF prior to April 1, 2001. Pursuant to paragraphs 8 and 104 of this agreement, the partners agree that Schedule 1 shall be amended by the OTF, to implement such benefit enhancements or contribution rate reductions, and the OTF shall promptly deliver the amendment(s) to the Board, and the Board shall promptly file the amendment(s) with the Superintendent of Financial Services upon receipt of same from the OTF.

(vii) The Minister of Finance will continue to make special payments out of the Consolidated Revenue Fund in accordance with paragraph 55 of the agreement during the IUL settlement period until the obligation to make special payments on account of the initial unfunded liability is eliminated in accordance with this agreement. The amount of the special payments payable pursuant to this subparagraph shall be in accordance with the schedule of payments set out in Appendix H to the Report on the Actuarial Valuation for Funding Purposes for the plan as at January 1, 1996 ("Appendix H") until December 1, 2001, and in accordance with Schedule 2 subsequent to December 1, 2001, if the Minister of Finance continues to be obligated to make special payments on account of the initial unfunded liability beyond this date. If subsection 3(12) of Schedule 2 to the *Teachers' Pension Act* is applicable with respect to any actuarial gains disclosed in a valuation pursuant to subparagraph (ii), the Minister of Finance shall not exercise his discretion in subsection 3(12) of Schedule 2 to reduce the remaining special payments as set out in Appendix H, until the obligation of the Minister of Finance to make special payments on account of the initial unfunded liability is eliminated.

(viii)The issue raised in the "part-time leave" case pending before the Ontario Court of Appeal shall be referred to mediation by Mr. M. Stanley Beck. Mr. Beck will be asked to provide a non-binding opinion on the merits of the case by no later than July 15, 1998. The cost of the mediation pursuant to this subparagraph shall be paid from the fund.

(ix) The partners shall establish a committee to deal on a priority basis with accounting matters relating to joint pension plan sponsorship, and agree to contact the Public Sector Accounting and Auditing Board (PSAAB) to raise issues of concern to the partners. The committee shall report to the Partners by May 1, 1999. The reasonable costs of the committee shall be paid from the fund.

(x) Subject to any extension of the IUL settlement period pursuant to subparagraph (v), at the end of the IUL settlement period, the provisions of this agreement respecting the use of actuarial gains or losses, other than this paragraph 57a, will apply. The next triennial negotiation pursuant to paragraphs 73 to 101 will be based on the actuarial valuation for funding purposes as at January 1, 2002, unless the IUL settlement period is extended beyond this date, or the partners agree otherwise.

(xi) Any dispute regarding the interpretation, application, administration and implementation of the provisions in this paragraph 57a may be resolved in accordance with paragraph 14 of the agreement, and/or through such other proceedings as are otherwise available to either partner.

58. If the preliminary results of a valuation prepared for filing with the Financial Services Commission of Ontario as at a date after the 1st day of January, 1993 indicate a need to increase the contribution rate the partners agree to meet as soon as possible to discuss how to adjust for that need on an equally shared basis. If the partners cannot agree on how to adjust they will refer the issue to the mediation and arbitration procedures described elsewhere in this agreement to adjust the contribution rate and/or benefits. (Last amended November 15, 1993 - Effective November 15, 1993)

59. If the preliminary results of a valuation prepared for filing with the Financial Services Commission of Ontario as at a date after the 1st day of January, 1993 indicate that the contribution rate can be decreased the implicit actuarial gain disclosed by the valuation will be applied to reduce and, if possible, eliminate the payments required to liquidate any unamortized balance of a solvency deficiency. (Last amended November 15, 1993 - Effective November 15, 1993)

60. An implicit actuarial gain remaining after the elimination of a deficiency mentioned in paragraph 59, will be used to establish a contingency reserve in an amount agreed upon by the partners or for any of the following purposes upon which the partners have agreed or which an arbitrator has awarded,

(i) to reduce contributions which members and employers are required to pay, and/or

(ii) to improve benefits payable to members.

60a. The portion of the gain disclosed by the January 1, 1996 valuation remaining after the implementation of the benefit improvements contained in the December 30, 1996 arbitration award shall be placed in a contingency reserve called the Rate Stabilization Fund for the period January 1, 1996 to December 31, 1998. (Last amended February 20, 1997 - Effective January 1, 1996)

60b. The $76 million of actuarial gains that, effective April 3, 2001, remain available to the OTF under the subparagraph 57a (iv) shall be allocated to a contingency reserve until such time as the OTF, in its sole discretion, may determine, at which time such gains shall be used toward the provision of future benefit enhancements and/or member contribution rate reductions as determined by the OTF, in its sole discretion. (Last amended March 5, 2002 – Effective April 2, 2001)

60c. The portion of the actuarial surplus disclosed by the January 1, 2001 valuation that remains after providing for,

(a) the benefit improvements contained in the plan amendments dated April 2, 2001, and

(b) the contingency reserve pursuant to paragraph 60b,

shall be allocated to a contingency reserve called the Rate Stabilization Fund for the period January 1, 2001 to December 31, 2001, or until such later date agreed to by the partners. (Last amended March 5, 2002 – Effective April 2, 2001)

60d. The partners acknowledge that the $76 million referred to in paragraph 60b will be used towards reducing the additional contributions payable by active members in accordance with section 19 of Schedule 1 in 2008 from 3.1% to 2.3% and that this application will fully discharge the credit owing the Ontario Teachers' Federation under paragraph 60b. (Last amended December 21, 2006 – Effective January 1, 2007)

60e. The partners agree that $7 million shall be allocated to a contingency reserve, to the credit of the Minister, to reflect the additional $7 million that was used, in addition to the $76 million referred to in paragraph 60d, towards reducing the additional contributions payable by active members in accordance with section 19 of Schedule 1 in 2008 from 3.1% to 2.3%. (Last amended December 21, 2006 – Effective January 1, 2007)

61. The valuation as at January 1, 1992 that was prepared and provisionally filed with the Pension Commission of Ontario shall be considered invalid. (Last amended November 15, 1993 - Effective November 15, 1993)

62. The board will prepare a valuation of the plan as at the 1st day of January, 1993. (Last amended November 15, 1993 - Effective November 15, 1993)

63. A portion, in the amount of $1.2 billion, of the gain disclosed by the January 1, 1993 valuation is to be applied to reduce the Minister's scheduled special payments under Schedule 2 of the Act, in the period from January 1, 1993 until the entire amount is exhausted. (Last amended November 15, 1993 - Effective November 15, 1993)

64. A further portion, in the amounts of $200 million as at March 31, 1994 and $125 million as at March 31, 1995, of the gain disclosed by the January 1, 1993 valuation, is to be applied to reduce scheduled government payments to the plan on or before the 31st of March, 1995. (Last amended November 15, 1993 - Effective November 15, 1993)

65. The partners may authorize the use of an additional portion of the gains from the 1993 valuation to offset social contract targets for those members of the plan who are not covered by the Teachers' Sub-Sectoral Framework Agreement and who meet the set of principles agreed on by the partners; these gains will be allocated in the same proportion as members of the plan who are covered by the Teachers' Sub-Sectoral Agreement. (Last amended November 15, 1993 - Effective November 15, 1993)

66. Any residual portion of the gain disclosed by the January 1, 1993 valuation is to be placed in a contingency reserve for rate stabilization until at least January 1, 1996. (Last amended November 15, 1993 - Effective November 15, 1993)

67. Revoked. (Last amended November 15, 1993 - Effective November 15, 1993)

68. If a solvency valuation of the plan, conducted as at a date on or before the 1st day of January, 1996, discloses a solvency deficiency the contributions of members, the Minister and employers required to contribute to the fund under Schedule 1 will be adjusted in the following way,

(1) The members will during each of the fifteen years following the date of the solvency valuation contribute the members' contribution required under Schedule 1 plus an amount equal to "B" as defined in subparagraph (2).

(2) The Minister and employers will during each of the five years following the date of the solvency valuation contribute the Minister's and employers' contributions required under Schedule 1 plus an amount equal to,

$$A - B$$

where

"A" is equal to the amount of the annual payment required to amortize the solvency deficiency amortized over the five years following the date of the solvency valuation, and

"B" is equal to one half of the amount of the annual payment required to amortize the solvency deficiency over the fifteen years following the date of the solvency valuation.

(3) The Minister and employers will during each of the sixth through fifteenth years following the date of the solvency valuation contribute the contributions required of them under Schedule 1 less an amount equal to "B". (Last amended November 15, 1993 - Effective November 15, 1993)

69. If a solvency valuation of the plan, conducted as at a date after the 1st day of January, 1996, discloses a solvency deficiency the contributions of members, the Minister and employers required to contribute to the fund under Schedule 1 will be adjusted in the following way,

(1) The members will during each of the ten years following the date of the solvency valuation contribute the members' contribution required under Schedule 1 plus an amount equal to "B" as defined in subparagraph (2).

(2) The Minister and employers will during each of the five years following the date of the solvency valuation contribute the Minister's and employers' contributions required under Schedule 1 plus an amount equal to,

$$A - B$$

where

"A" is equal to the amount of the annual payment required to amortize the solvency deficiency amortized over the five years following the date of the solvency valuation, and

"B" is equal to one half of the amount of the annual payment required to amortize the solvency deficiency over the ten years following the date of the solvency valuation.

(3) The Minister and employers will during each of the sixth through tenth years following the date of the solvency valuation contribute the contributions required of them under Schedule 1 less an amount equal to "B". (Last amended November 15, 1993 - Effective November 15, 1993)

70. If a valuation done after one which showed a solvency deficiency discloses that there is no solvency deficiency or one that is less than would be expected based on the first valuation, the partners agree to adjust on an equally shared basis for any payments that have been made under paragraphs 68 or 69. (Last amended November 15, 1993 - Effective November 15, 1993)

71. Revoked. (Last amended November 15, 1993 - Effective November 15, 1993)

Triennial negotiation of changes to the plan

72. The Board will prepare a valuation of the plan as at the 1st day of January, 1996 as soon as possible after that date. This will be the valuation to be used for the first set of negotiations. (Last amended November 15, 1993 - Effective November 15, 1993)

73. The subject of the negotiations and of all subsequent triennial negotiations will be any of the matters referred to in paragraphs 8 and 12.

74. As soon as preliminary results of the valuation are available the partners will 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.

75. The partners will advise the Board what changes affecting benefits and contribution rates they are proposing and the Board will provide cost estimates and comments on the administrative impact of the changes to both partners as soon as possible.

76. There will be a manager of negotiations whose fees and expenses shall be paid by the fund. The manager will be appointed by agreement of the partners or if they cannot agree the Chief Executive Officer of the Board will act as manager. When the manager is appointed, the partners may give the manager any role in the negotiation process in addition to the role described in this agreement. (Last amended March 27, 1996 - Effective January 1, 1996)

77. At any time after the preliminary results of a valuation are available the partners may agree to appoint a mediator. The mediator will be chosen by the agreement of the partners or by a method to which they agree at that time.

78. If no agreement is reached on all proposed changes by the 1st day of May, 1996 and no mediator has been appointed by agreement the manager will appoint a mediator to mediate proposed changes to the contribution rate or benefits under the plan. The manager will do so by preparing a list of five persons willing to act as mediator and asking each partner to select three names from the list. The manager will appoint one of the persons chosen by both partners. (Last amended November 15, 1993 - Effective November 15, 1993)

79. Any proposed changes to the plan not involving the contribution rate or benefits which remain unresolved on the 1st day of May, 1996 will be referred to the Partners Committee established under paragraph 13. The Partners Committee will make every effort to resolve those issues referred to it. (Last amended November 15, 1993 - Effective November 15, 1993)

80. If the partners 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.

81. If the partners do not agree on mediation/arbitration the mediator will meet with them and try to mediate an agreement.

82. 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. The report will be delivered to the partners.

83. The mediator may extend the deadline for delivering the report by 14 days if he or she is of the opinion that the partners are likely to reach an agreement during the extension.

84. 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.

85. At any time after a mediator has been appointed the partners may agree to appoint a board of arbitration.

86. If the partners agree to appoint a board of arbitration or if 14 days have passed since the mediator's report each partner will appoint one person to the board of arbitration and the two appointees will select a final member who will be the umpire.

87. This agreement together with a referral to a board of arbitration constitutes a submission under the *Arbitrations Act*, R.S.O. 1980, c. 25, as amended.

88. If the persons appointed by the partners to a board of arbitration do not appoint an umpire within 14 days of the appointment of the latter of them, the manager will prepare a list of five persons who are willing to act as umpire and ask each partner to select three names from the list. The manager will appoint as umpire one of the persons chosen by both partners.

89. The umpire will establish the procedure for conducting the arbitration but will allow each partner an opportunity to present evidence and make representations. The persons appointed by the partners will consult with the appointing partner during the arbitration.

90. The board of arbitration will hold a hearing within 30 days of its appointment and make an award within 60 days of the conclusion of the hearing. The board of arbitration will provide reasons for its award.

91. The board of arbitration in making an award will consider prevailing economic conditions and the overall state of the provincial economy.

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). (Last amended March 26, 2003 – Effective January 1, 2003)

92.1 In the event that a board of arbitration is appointed pursuant to any provision of the agreement, other than paragraph 57a, to determine the application of actuarial gains disclosed in a valuation for funding purposes where a portion of the actuarial gains disclosed in such valuation is subject to the provisions of paragraph 57a, the board of arbitration shall not issue an award regarding that portion of the actuarial gains which is subject to the provisions of paragraph 57a. (Last amended May 27, 1998 - Effective April 18, 1998)

93. The board of arbitration will give the partners a copy of the award and reasons as soon as they are prepared.

94. 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. The changes will take effect on the 1st day of January, 1997 or on such earlier date to which the partners have agreed. (Last amended November 15, 1993 - Effective November 15, 1993)

95. The final valuation will be filed with the Financial Services Commission of Ontario and Schedule 1 will be amended to reflect the changes agreed to and the award if any.

96. Every three years, after January 1, 1996, the process described in this section will be repeated unless the partners agree that no changes will be made to the plan. (Last amended November 15, 1993 - Effective November 15, 1993)

97. The manager and the umpire may agree to extend the timelines set out by this agreement if they think it will help the partners reach an agreement.

98. The partners may agree to change the procedure described in this agreement, either for one round of negotiations or for all future negotiations.

99. The costs of mediation and arbitration will be paid out of the fund. (Last amended March 27, 1996 - Effective January 1, 1996)

100. The mediator or the umpire may employ experts to assist her or him. The cost of employing experts will be shared equally by the partners. The mediator or umpire will consult with the partners about a reasonable budget for such costs.

101. Revoked. (Last amended March 26, 2003 – Effective January 1, 2003)

General

102. Schedule 1 to the *Teachers' Pension Plan, 1989* as amended is adopted by the partners as part of this agreement.

103. The partners agree that this agreement forms part of the plan documents of the pension plan and that they will file a copy of this agreement with the Pension Commission of Ontario.

104. The partners may at any time agree to change any of the provisions of Schedule 1. A change to Schedule 1 will be effected when it is filed with the Financial Services Commission of Ontario by the partners.

105. The partners will not make any change to Schedule 1 which is contrary to the laws of Ontario. Any change which is inconsistent will be void to the extent of the inconsistency.

106. Sections 116, 117, 118 and all of Part XII of Schedule 1 are revoked.

107. Revoked. (Last amended November 15, 1993 - Effective November 15, 1993)

108. The Board will print a new consolidation of Schedule 1 as soon as possible after any changes to it have been filed with the Financial Services Commission of Ontario.

109. The Minister will submit a copy of Schedule 1 and the annual report to the Lieutenant Governor in Council and lay it before the Assembly at the first opportunity after the report is prepared by the Board.

110. The partners agree that the Funding Management Policy attached hereto, and as amended from time to time, forms part of this agreement. (Last amended June 3, 2009 – Effective January 1, 2009)

July 15, 1991

APPENDIX "A"

Funding Management Policy

Article I. Application

Section 1.01 *Best Estimates Assumptions*: For the purposes of this Funding Management Policy, except as otherwise provided herein, the Board shall provide the required reports using the Board's best estimates assumptions including, in the case of the discount rate, a margin for adverse deviation. The Board's best estimate economic assumptions may be based on market data, smoothed data, the reference rate or the Board's expectation if the Board believes future experience may differ from market data. The Board's assumptions shall be used only if they would be consistent with accepted actuarial practice. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.02 *Escalated Adjustments Indices*: The Board shall also maintain indices to record escalated adjustments for post-2009 service. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.03 *Different Discount Rate*: If a preliminary valuation uses a discount rate lower than the restoration basis for valuations prepared under Article III and Article VI, lower than the temporary basis for valuations prepared under Article IV, or lower than the distribution basis for valuations prepared under Article V, then the Board shall notify the partners and the partners shall meet with the Board. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.04 *Exit Provision*: The provisions in Article II to Article IX shall expire twelve months after the notification referred to in Section 1.03 unless both partners otherwise notify the Board. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.05 This Funding Management Policy shall be applied as follows:

(a) *If there is a restoration basis excess when current contributions exceed basic contributions and/or current benefits are less than run-rate benefits, the excess can be used to reduce contributions and/or increase benefits in accordance with Article III*: If the results of a preliminary valuation, using the restoration basis, the definitions in Section 3.01 and the provisos in Section 3.02 and Section 3.03, satisfy the conditions in Section 3.04, then Section 3.05, Section 3.06, Section 3.07 and Section 3.08 shall apply;

(b) *If there is a restoration basis deficit using current contributions and current benefits, contributions must be increased and/or benefits must be reduced in accordance with Article III to eliminate the deficit*: If the results of a preliminary valuation, using the restoration basis, the definitions in Section 3.01 and the provisos in Section 3.02 and Section 3.03, satisfy the conditions in Section 3.09, then Section 3.10, Section 3.11, Section 3.12, Section 3.13, and Section 3.14 shall apply;

(c) *If there is a restoration basis excess when contributions are less than or equal to basic contributions and benefits are greater than or equal to run-rate benefits, prepare a temporary basis valuation in accordance with Article IV*: If the results of a preliminary valuation, using the restoration basis, the definitions in Section 3.01 and the provisos in Section 3.02 and Section 3.03, either:

(i) do not satisfy the conditions in either Section 3.04 or Section 3.09; or

(ii) satisfy the conditions in Section 3.04, and

1) the present value of revised benefits is equal to the present value of run-rate benefits, and

2) the present value of revised contributions is equal to the present value of basic contributions;

then the preliminary valuation shall be performed using the temporary basis, the definitions in Section 4.01 and the proviso in Section 4.02;

(d) *Temporary and Distribution Basis Valuations*:

(i) *If there is a temporary basis excess, prepare a distribution basis valuation in accordance with Article V*: If the results of a preliminary valuation, using the temporary basis, the definitions in Section 4.01 and the proviso in Section 4.02, satisfy the conditions in Section 4.03, then the preliminary valuation shall be performed using the distribution basis, the definitions in Section 5.01 and the proviso in Section 5.02, and

1) *If there is a distribution basis excess, the distribution basis excess can be used to make plan improvements in accordance with Article V*: if the results of that preliminary valuation satisfy the conditions in Section 5.03, then Article V shall apply;

2) *If there is a distribution basis deficit but a temporary basis excess, the temporary basis excess can be used to make temporary plan improvements in accordance with Article IV*: if the results of that preliminary valuation do not satisfy the conditions in Section 5.03, then the preliminary valuation shall be performed using the temporary basis, the definitions in Section 4.01 and the proviso in Section 4.02, and Article IV shall apply;

(ii) *If there is a temporary basis deficit, the restoration basis valuation will apply in accordance with Article III*: If the results of a preliminary valuation, using the temporary basis, the definitions in Section 4.01 and the proviso in Section 4.02, do not satisfy the conditions in Section 4.03, then the preliminary valuation shall be performed using the restoration basis, the definitions in Section 3.01 and the provisos in Section 3.02 and Section 3.03, and Section 3.05, Section 3.06, Section 3.07 and Section 3.08 shall apply;

(e) *Post-December 30, 2017 Valuations*: If the results of a preliminary valuation prepared as of a date after December 30, 2017, using the restoration basis and the definitions in Section 6.01, satisfy the conditions in Section 6.02, then Section 6.03 shall apply;

(f) *2013 Term Sheet Precedence*: The provisions of the 2013 Term Sheet shall take precedence over this Funding Management Policy. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.06 *Actions Subject to Pension Legislation*: Prior to the commitment of a surplus distribution or a contribution decrease, the partners shall ensure such distribution or contribution decrease is in accordance with the *Income Tax Act* (Canada), the *Pension Benefits Act* (Ontario) and their respective regulations. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.07 *Conditions on Temporary Improvements*: Any commitment to provide temporary improvements shall be made conditional on the results of a preliminary valuation for each year of the commitment period indicating that the conditions in Section 3.04(a) are met prior to and after such temporary improvement. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 1.08 *Headings*: Headings are underlined and are for convenience only and shall not affect the interpretation or meaning of any provision of this Funding Management Policy. (Last amended May 27, 2015 – Effective March 6, 2015)

Article II. Definitions

Section 2.01 For the purposes of this Funding Management Policy:

(a) "2013 Term Sheet" means the March 13, 2013 OTPP Term Sheet entered into by the partners;

(b) "basic contributions" are the contributions required by subsections 19(1) or (2) of Schedule 1 as it read on January 1, 2012;

(c) "commitment period" means the three-year period during which a temporary improvement is provided;

(d) "commitment value" means the present value of the portion of the temporary improvement value provided during the commitment period;

(e) "Consumer Price Index" means the Consumer Price Index for Canada as published by Statistics Canada under the authority of the *Statistics Act* (Canada);

(f) "CPI adjustment" means the ratio between 1.000 and 1.080 of the average for the Consumer Price Index over the last twelve months of the twenty-four-month period ending with the 30th day of September in the immediately preceding year to the average for the Consumer Price Index over the first twelve months of that period - 1. If the ratio would have been less than 1.000 or greater than 1.080, but for those limits, the difference shall be carried forward in a manner consistent with that set out in section 80 of Schedule 1;

(g) "current accumulated adjustment ratio" is an index maintained by the Board that begins with "1.000000" for 2010 and is the product of all current ratios for the years in the period commencing with 2010 and ending with the year prior to the year for which the current accumulated adjustment ratio is being determined. The index may differ in respect of service accrued before 2014 and service accrued after 2013 with both indices beginning with "1.000000" for 2010;

(h) "current benefits" are the pension benefits, current escalated adjustments and ancillary benefits calculated in accordance with Schedule 1 as it read at the current valuation date without taking into account any amendment made, or changes agreed to by the partners, on or after the current valuation date;

(i) "current contributions" are the contributions required by Schedule 1 as it read at the current valuation date without taking into account any amendment made on or after the current valuation date;

(j) "current escalated adjustments" are the escalated adjustments in respect of post-2009 service that were applied prior to the January 1st following the current valuation date and assumed thereafter at the rate set out in the most recent filed valuation;

(k) "current ratio", for a year, means 1 + the proportion of the CPI adjustment granted as agreed to by the partners, and as may have been revised from time to time, provided that the proportion shall not be less than 50% in respect of service accrued before 2014, but not including any revision agreed to by the partners in relation to the current valuation;

(l) "current valuation date" in respect of a valuation is the date provided in Section 7.01;

(m) "distribution basis" is the reference rate with a positive adjustment of 0.5% together with the Board's best estimate actuarial assumptions for all other factors;

(n) "freeze period" means the period from December 31, 2012 to December 30, 2017;

(o) "going concern liabilities" are the going concern liabilities within the meaning of Regulation 909 made under the *Pension Benefits Act* and must also include the present value of the pension benefits and escalated adjustments that both accrued prior to the valuation date and that will accrue on or after the valuation date to the persons who were members of the plan on the valuation date and the present value of the ancillary benefits for which the eligibility requirements will be satisfied on or after the valuation date by the persons who were members of the plan on the valuation date;

(p) "preliminary valuation" means a valuation referred to in Section 7.01;

(q) "reference rate" means the interest rate chosen by the Board representing the Government of Canada long bond yield (currently, CANSIM Series V39056 nominal and CANSIM Series V39057 real, or their reasonable respective replacements) that may be based on market data or smoothed data;

(r) "remaining amortization value" means the difference between the temporary improvement value and the commitment value;

(s) "restoration basis" is the reference rate with a positive adjustment of 1.55% together with the Board's best estimate actuarial assumptions for all other factors;

(t) "revised accumulated adjustment ratio" is an index maintained by the Board that begins with "1.000000" for 2010 and is the current accumulated adjustment ratio, as modified by an agreement between the partners to change the proportion of the CPI adjustment in respect of post-2009 service prior to the year following the current valuation date. The index may differ in respect of service accrued before 2014 and service accrued after 2013 with both indices beginning with "1.000000" for 2010;

(u) "revised benefits" are the current benefits including any amendment made, or changes agreed to by the partners, on or after the current valuation date based on that valuation;

(v) "revised contributions" are the current contributions including any amendment made on or after the current valuation date based on that valuation;

(w) "revised escalated adjustments" are the current escalated adjustments including any amendment made, or changes agreed to by the partners, on or after the current valuation date based on that valuation and assumed thereafter at the rate set out in that valuation;

(x) "run-rate accumulated adjustment ratio" is an index maintained by the Board that begins with "1.000000" for 2010 and is the product of all run-rate ratios for the years in the period commencing with 2010 and ending with the year prior to the year for which the run-rate accumulated adjustment ratio is being determined;

(y) "run-rate benefits" are the pension benefits, run-rate escalated adjustments and ancillary benefits calculated in accordance with Schedule 1 as it read on January 1, 2009, together with any benefits provided by amendments described in Article IX;

(z) "run-rate escalated adjustments" are the escalated adjustments in respect of post-2009 service that would have applied at the rate of 100% of the CPI adjustment prior to the January 1st following the current valuation date and that would be assumed thereafter at the rate of 100% of the CPI adjustment;

(aa) "run-rate ratio", for a year, means 1 + the CPI adjustment for the year;

(bb) "temporary basis" is the reference rate with a positive adjustment of 1.25% together with the Board's best estimate actuarial assumptions for all other factors;

(cc) "temporary improvement" means an improvement provided in accordance with Section 4.05;

(dd) "temporary improvement value" is the present value of a contribution decrease, a distribution of surplus and/or a benefit improvement that is amortized over a period of up to ten years, but is committed to for the duration of the commitment period only, provided that at the establishment of the commitment:

(i) the partners may elect an amortization period between three and ten years; and

(ii) for amortization periods of less than ten years, any temporary improvement for a given year shall be limited such that the present value of that given year's temporary improvement is not greater than the present value of basic contributions, calculated using the temporary basis, to be paid in the same year.

(Last amended May 27, 2015 – Effective March 6, 2015)

Article III. **<u>Funding Zone - Restoration</u>**

Section 3.01 *<u>Definitions</u>*: For the purposes of Article III, as at the current valuation date, using the restoration basis:

(a) "assets" are the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the *Pension Benefits Act*;

(b) "current liabilities" are the difference between:

(i) the going concern liabilities calculated using current benefits, and

(ii) the present value of current contributions;

(c) "revised liabilities" are the difference between:

(i) the going concern liabilities calculated using revised benefits, and

(ii) the present value of revised contributions.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.02 *Restoration Basis Plus an Adjustment*: For the purposes of Article III, current liabilities and revised liabilities may be calculated as at the current valuation date using the restoration basis plus an adjustment. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.03 *CPI Adjustment*: For the purposes of Article III, and subject to a subsequently filed valuation, the proportion of the CPI adjustment for the period covered by the current valuation, in respect of each applicable period of service, will be the same for each year in that period and assumed at the same rate thereafter. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.04 *Restoration Basis Excess, but Basic Contributions and/or Run-Rate Benefits Not Restored*:

(a) If assets are greater than current liabilities; and

(b) if:

(i) the present value of current contributions is greater than the present value of basic contributions, or

(ii) the present value of current benefits is less than the present value of run-rate benefits, or

(iii) both (i) and (ii);

then Section 3.05, Section 3.06, Section 3.07 and Section 3.08 shall apply.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.05 *Restoration Basis Excess Report*: The Board shall report to the partners:

(a) the excess of assets over current liabilities; and

(b) the extent to which the excess can be used to provide the changes specified in Section 3.06.

(Last amended May 27, 2015 – Effective March 6, 2015)

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 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).

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.07 *Conditions on Application of Excess*: Subject to Section 3.06 and Section 3.08 or any mutual agreement to the contrary, the partners shall apply the excess of assets over current liabilities to change benefits, contributions, or both, provided that no change or amendment shall be made unless, after such change or amendment:

(a) assets are equal to or greater than revised liabilities;

(b) the revised accumulated adjustment ratio is equal to or less than the run-rate accumulated adjustment ratio;

(c) the revised accumulated adjustment ratio is equal to or greater than the current accumulated adjustment ratio;

(d) the present value of revised benefits is equal to or less than the greater of the present value of current benefits and the present value of run-rate benefits;

(e) the present value of revised benefits is equal to or greater than the lesser of the present value of current benefits and the present value of run-rate benefits;

(f) the present value of revised contributions is equal to or greater than the lesser of the present value of current contributions and the present value of basic contributions; and

(g) the present value of revised contributions is equal to or less than the greater of the present value of current contributions and the present value of basic contributions.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.08 *2013 Term Sheet Limits*: As set out in further detail in the 2013 Term Sheet, during the freeze period:

(a) The partners may provide escalated adjustments pursuant to Section 3.06(a), Section 3.06(b), Section 3.06(c) and Section 3.06(d) only if the assets are greater than 100% of the current liabilities and do not fall below 100% of the revised liabilities after the adjustment; and

(b) The partners may agree to improve benefits, or to restore benefits that were reduced during the freeze period, pursuant to Section 3.06(e) only if the net assets available for benefits (as such term is used in the preliminary valuations) are equal to or greater than 105% of the current liabilities and do not fall below 105% of the revised liabilities after the benefit improvement or restoration.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.09 *Restoration Basis Deficit*: If current liabilities are greater than assets, then Section 3.10, Section 3.11, Section 3.12, Section 3.13 and Section 3.14 shall apply. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.10 *Restoration Basis Deficit Report*: The Board shall report to the partners:

(a) the excess of current liabilities over assets; and

(b) the amount required to change current benefits, current contributions, or both, to eliminate the excess referred to in Section 3.10(a) above, as requested by either partner.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.11 *Conditions on Elimination of Deficit*: Subject to Section 3.12 and Section 3.14, the partners may change benefits, contributions, or both, to eliminate the excess referred to in Section 3.10(a), provided that no change or amendment shall be made unless, after such change or amendment:

(a) assets are equal to or greater than revised liabilities; and

(b) revised member contributions shall be limited to 15% of pensionable salaries above the Year's Maximum Pensionable Earnings as prescribed under the *Canada Pension Plan*.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.12 *Restrictions on Benefit Reductions*: Current benefits shall not be reduced unless:

(a) the partners agree on the terms and conditions of any reduction in current benefits;

(b) the partners have entered into a written agreement governing the manner in which contributions by the Minister and the Employers will be adjusted to offset any reduction in benefits; and

(c) the revised accumulated adjustment ratio, in respect of each year, is equal to or greater than the current accumulated adjustment ratio for the year.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.13 *Restrictions on Contribution Increases*: Subject to Section 3.14, the partners have the authority to set the level of contributions that must be reached before current benefits are reduced below run-rate benefits, subject to the commitment that member contributions will not exceed 15% of pensionable salaries above the Year's Maximum Pensionable Earnings (as prescribed under the Canada Pension Plan). (Last amended May 27, 2015 – Effective March 6, 2015)

Section 3.14 *Further Restrictions on Contribution Increases*: As set out in further detail in the 2013 Term Sheet, during the freeze period there will be no employer contribution increases except as provided under the 2013 Term Sheet. (Last amended May 27, 2015 – Effective March 6, 2015)

Article IV. Funding Zone – Temporary Improvements

Section 4.01 *Definitions*: For the purposes of Article IV, as at the current valuation date, using the temporary basis:

(a) "assets" are either:

(i) the market value of net assets available to provide benefits as determined by the Board, if the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data is less than the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data; or

(ii) the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act, if the excess of the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data is less than the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data;

(b) "current liabilities" are the sum of:

(i) the difference between:

1) the going concern liabilities calculated using the greater of current benefits and run-rate benefits, and

2) the present value of the lesser of current contributions and basic contributions;

and

(ii) the remaining amortization value (equal to zero with respect to a particular commitment period if, as of the valuation date, the payment in respect of the last year of a commitment period will be paid in that year);

(c) "revised liabilities" are the sum of:

(i) the difference between:

1) the going concern liabilities calculated using the greater of revised benefits and run-rate benefits, and

2) the present value of revised contributions;

and

(ii) the remaining amortization value (equal to zero with respect to a particular commitment period if, as of the valuation date, the payment in respect of the last year of a commitment period will be paid in that year);

(d) The reference rate for purposes of determining the temporary basis is based on:

(i) market data, if the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data is less than the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data; and

(ii) smoothed data, if the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data is less than the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.02 *Temporary Basis Plus an Adjustment*: For the purposes of Article IV, current liabilities and revised liabilities may be calculated as at the current valuation date using the temporary basis plus an adjustment. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.03 *Temporary Basis Excess*: If assets are greater than current liabilities, then Section 4.04, Section 4.05 and Section 4.06 shall apply, provided that no temporary improvements may be provided unless the partners have provided all of the changes specified in Section 3.06. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.04 *Temporary Basis Excess Report*: The Board shall report to the partners:

(a) the amount by which assets exceed current liabilities;

(b) the commitment value;

(c) the extent to which the commitment value can be used to provide a reduction to current contributions, beginning with the year following the year in which a preliminary valuation is filed and lasting for the commitment period;

(d) the extent to which the commitment value can be used to provide annual surplus distributions, beginning with the year following the year in which a preliminary valuation is filed and lasting for the commitment period;

(e) the extent to which the commitment value can be used to provide a temporary benefit improvement, beginning with the year following the year in which a preliminary valuation is filed and lasting for the commitment period; and

(f) the extent to which the commitment value can be used to provide a combination of Section 4.04(c), Section 4.04(d) and Section 4.04(e).

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.05 *Conditions on Application of Excess*: Subject to Article VI and Section 4.06, the partners may apply all or part of the commitment value to change temporarily current contributions, provide surplus distributions on a temporary basis, or provide a temporary benefit improvement, provided that no amendment shall be made unless, after such amendment, the excess of assets over revised liabilities is equal to or greater than zero. (Last amended May 27, 2015 – Effective March 6, 2015)

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. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.07 *Temporary Basis Deficit*: If assets are equal to or less than current liabilities, then Section 4.08 and Section 4.09 shall apply. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.08 *Temporary Basis Deficit Report*: The Board shall report to the partners the amount by which current liabilities exceed assets. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 4.09 *No Action on Temporary Basis and Return to Restoration Basis*: Subject to Article VI, the partners shall not provide new temporary improvements and Article III shall apply. (Last amended May 27, 2015 – Effective March 6, 2015)

Article V. Funding Zone – Permanent Improvements

Section 5.01 *Definitions*: For the purposes of Article V, as at the current valuation date, using the distribution basis:

(a) "assets" are either:

(i) the market value of net assets available to provide benefits as determined by the Board, if the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data is less than the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data; or

(ii) the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act, if the excess of the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data is less than the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data;

(b) "current liabilities" are the sum of:

(i) the difference between:

1) the going concern liabilities calculated using the greater of current benefits and run-rate benefits, and

2) the present value of the lesser of current contributions and basic contributions;

and

(ii) the remaining amortization value (equal to zero with respect to a particular commitment period if, as of the valuation date, the payment in respect of the last year of a commitment period will be paid in that year);

(c) "current targeted funding amount" is 10% of current liabilities;

(d) "revised liabilities" are the sum of:

(i) the difference between:

1) the going concern liabilities calculated using the greater of revised benefits and run-rate benefits, and

2) the present value of revised contributions;

and

(ii) the remaining amortization value (equal to zero with respect to a particular commitment period if, as of the valuation date, the payment in respect of the last year of a commitment period will be paid in that year);

(e) The reference rate for purposes of determining the distribution basis is based on:

(i) market data, if the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data is less than the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data; and

(ii) smoothed data, if the excess of the assets in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the Pension Benefits Act over current liabilities calculated using a reference rate based on smoothed data is less than the excess of the market value of net assets available to provide benefits over current liabilities calculated using a reference rate based on market data;

(f) "revised targeted funding amount" is 10% of revised liabilities.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.02 *Distribution Basis Plus an Adjustment*: For the purposes of Article V, current liabilities and revised liabilities may be calculated as at the current valuation date using the distribution basis plus an adjustment. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.03 *Distribution Basis Excess*: If the excess of assets over current liabilities is greater than the current targeted funding amount, then Section 5.04 and Section 5.05 shall apply, provided that no changes pursuant to Section 5.05 may be provided unless the partners have provided all of the changes specified in Section 3.06. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.04 *Distribution Basis Excess Report*: The Board shall report to the partners:

(a) the amount by which assets minus current liabilities exceed the current targeted funding amount; and

(b) the amount required to change current benefits, current contributions, or both, as requested by either partner.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.05 *Conditions on Application of Excess*: Subject to Article VI, the partners may apply all or part of the amount by which assets minus current liabilities exceed the current targeted funding amount to change current benefits, current contributions, or both, provided that no amendment shall be made unless:

(a) after such amendment the excess of assets over revised liabilities is equal to or greater than the revised targeted funding amount; and

(b) 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 change in current benefits that is reflected in the value of the liabilities.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.06 *Distribution Basis Deficit*: If:

(a) the excess of assets over current liabilities is less than the current targeted funding amount;

(b) the present value of current contributions is equal to or less than the present value of basic contributions;

(c) the present value of current benefits is equal to or greater than the present value of run-rate benefits; and

(d) the current accumulated adjustment ratio is equal to the run-rate accumulated adjustment ratio;

then Section 5.07 and Section 5.08 shall apply.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.07 *Distribution Basis Deficit Report*: The Board shall report to the partners the amount by which assets minus current liabilities are less than the current targeted funding amount. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 5.08 *No Action on Distribution Basis and Return to Temporary Basis*: Subject to Article VI, the partners shall not apply, pursuant to this Article V, any part of the amount by which assets exceed current liabilities, and Article IV shall apply. (Last amended May 27, 2015 – Effective March 6, 2015)

Article VI. Post December 30, 2017 Valuations

Section 6.01 *Definitions*: For the purposes of Article VI, as at the current valuation date, using the restoration basis:

(a) "assets" are the assets described in paragraph (a) of the definition of "going concern assets" in Regulation 909 made under the *Pension Benefits Act*;

(b) "current liabilities" are the difference between:

(i) the going concern liabilities calculated using current benefits, and

(ii) the present value of current contributions;

(c) "revised liabilities" are the difference between:

(i) the going concern liabilities calculated using revised benefits, and

(ii) the present value of revised contributions.

(Last amended May 27, 2015 – Effective March 6, 2015)

Section 6.02 *Post-2017 Excess*: Notwithstanding any other provision of this Funding Management Policy, as set out in further detail in the 2013 Term Sheet, after the end of the freeze period, if a valuation report with a valuation date after December 30, 2017 provides that assets are greater than current liabilities as at the date of the current valuation, then Section 6.03 shall apply. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 6.03 *2013 Term Sheet Provisions*:

(a) the OTF will have 'first call' on 100% of the value of the excess of the assets over the current liabilities (to take the form of "surplus credits") up to a cumulative total of the value of the lesser of:

(i) the value of the benefit reductions made during the freeze period, including the value of benefit reductions made in the January 1, 2012 valuation, but excluding: (1) the value of benefit reductions for which matching contributions are made by the Minister and the Employers, and (2) the value of benefit reductions relating to the removal and replacement of the remaining 50% guaranteed indexing with full conditional inflation protection for post-2013 service and the resulting change to the discount rate, and

(ii) the benefit reduction limit as calculated under the 2013 Term Sheet;

(b) if inflation protection is invoked below 50% during the freeze period, 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 inflation protection invoked during the freeze period until such time as that inflation protection is restored at 50% or more during or after the freeze period; and

(c) the OTF may apply all or part of surplus credits to change current benefits, current contributions, or both, provided that no amendment shall be made unless assets are equal to or greater than revised liabilities after such amendment.

(Last amended May 27, 2015 – Effective March 6, 2015)

Article VII. Valuation Frequency and Timing

Section 7.01 The Board shall require the actuary to prepare a preliminary valuation of the plan as of January 1, 2003 and each January 1 thereafter and, in addition, on such other date as the partners mutually agree. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 7.02 Subject to the requirements of the *Pension Benefits Act*, the partners agree that valuations shall be filed with the Superintendent of Financial Services only by their mutual agreement. The partners shall direct the Board, no later than seven months following the valuation date, whether to file. No such filing shall affect the timing of triennial negotiations between the partners referred to in paragraph 96. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 7.03 The seven-month notice requirement referred to in Section 7.02 shall not apply to the January 1, 2005 valuation and shall not apply to the January 1, 2012 valuation. (Last amended May 27, 2015 – Effective March 6, 2015)

Article VIII. Arbitration

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. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 8.02 The limitations on amendments set out in Section 3.07, Section 4.05, Section 4.06, Section 4.09, Section 5.05, and Section 5.08 shall apply to an award made by a board of arbitration pursuant to paragraph 92. (Last amended May 27, 2015 – Effective March 6, 2015)

Section 8.03 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 paragraphs 72 to 100. (Last amended May 27, 2015 – Effective March 6, 2015)

Article IX. **Limitations**

Section 9.01 The limitations on amendments in this Funding Management Policy shall not apply to amendments:

(a) made pursuant to paragraphs 60b, 60d, or 60e;

(b) that are required to comply with provincial law or, where both partners agree, to maintain registration as a registered pension plan under the *Income Tax Act (Canada*); or

(c) made by mutual agreement of the partners that do not increase liabilities by more than 0.5%.

(Last amended May 27, 2015 – Effective March 6, 2015)

20150521 amendment.pdf

AMENDMENT TO THE TEACHERS' PENSION PLAN

This is an agreement

B E T W E E N

Her Majesty the Queen
in right of the Province of Ontario
as represented by the Minister of Education

(the "Minister")

and

The Ontario Teachers' Federation
as represented by its Executive

(the "OTF")

WHEREAS the Minister and the OTF (collectively the "Partners") have established a partnership to administer the Ontario Teachers' Pension Plan and Fund, pursuant to an agreement between the Partners dated July 15, 1991 (the "Partners' Agreement"); and

WHEREAS the Partners' Agreement was most recently amended on January 15, 2014; and

WHEREAS the Partners wish to amend the Partners' Agreement further;

NOW THEREFORE the Partners agree as follows:

The Board

1. Effective January 1, 2016, paragraphs 20 and 21 of the Partners' Agreement are revoked and replaced with the following:

    20. The Board will have a maximum of eleven members. The partners will each appoint five members.

    21. The eleventh member of the Board will be the Chair. The process for appointing a Chair is set out in the next section of this agreement.

Her Majesty the Queen
in right of the Province of Ontario
as represented by the
Minister of Education

Liz Sandals
Minister of Education

Dated at Toronto this 21st day
of May, 2015.

The Ontario Teachers' Federation
as represented by its Executive

Rian McLaughlin
OTF President

Dated at Toronto this 6 day
of May, 2015.

FW_ OTTP -- history re_ use of surplus.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: FW: OTTP -- history re: use of surplus
Date: Sunday, September 18, 2016 12:39:57
Attachment 1: Key Funding Decisions.pdf

Key Funding Decisions.pdf

Key Funding Decisions Since 1990

Plan Funding

The Ontario Teachers' Federation (OTF) and the Ontario government, which jointly sponsor the Ontario Teachers' Pension Plan, must file a funding valuation with the provincial pension regulator at least every three years. A valuation must be filed with assets and liabilities (the cost of future pensions) in balance.

OTF and the Ontario government can file a valuation earlier than required to help manage the plan's funding status.

The following chart shows how OTF and the Ontario government have used surplus funds or resolved funding shortfalls for each valuation filed with the regulator since the inception of the Teachers' pension plan as an independent entity in 1990.

For more information on plan funding, visit the Corporate section of our website at www.otpp.com.

Funding decisions

Year	Valuation status and key decisions
1990	A preliminary unfunded liability of $7.8 billion to be amortized over 40 years by special payments from the Ontario government; basic contribution rate increased to 8% from 7%.
1993	A preliminary $1.5 billion surplus was distributed: $1.2 billion used to reduce government's special payments; $0.3 billion used to offset government cost reductions in the education sector (social contract days).
1996	A preliminary $0.7 billion surplus was distributed: $0.6 billion used to reduce early retirement penalty to 2.5% from 5% for each point short of 90 factor and lower the CPP reduction after age 65 (to 0.68% from 0.7%).
1998	A preliminary $6.8 billion surplus was distributed: $2.2 billion to pay for the 85 factor window from 1998 to 2002 and further lower the CPP reduction to 0.6%; $4.6 billion to reduce the value of special payments owed by the Ontario government. OTF and the Ontario government agree future surplus would be used to eliminate the government's remaining special payments, and the next $6.2 billion surplus would be available to OTF for benefit improvements.

Year	Valuation status and key decisions
1999	A preliminary $3.5 billion surplus was distributed to eliminate government's remaining special payments.
2000	$4.5 billion surplus; no changes to benefits or contribution levels.
2001	A preliminary $6.8 billion surplus was distributed: $6.2 billion to pay for benefit improvements, including a permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average Year's Maximum Pensionable Earnings (YMPE) to calculate CPP reduction; pension recalculation based on approximate best-5 salary years for older pensioners; and top-up waived for Long-Term Income Protection (LTIP) contributions. The remaining $76 million was set aside in a contingency reserve to be used by OTF at a later date.
2002	$1.9 billion surplus; no changes to benefits or contribution levels.
2003	$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary $6.1 billion shortfall was resolved, leaving plan with a $0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary $12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary $2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary $17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.

Year	Valuation status and key decisions
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	$6.8 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 for pension credit earned after 2009 to 70% from 60% of the increase in the cost of living. Both changes go into effect in 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.

FW_ Public Accounts Related Q’s.rtf

From: Petsche, Nadine (TBS) []
To: Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Public Accounts Related Q's
Date: Monday, June 12, 2017 11:30:13

Hi Christina.

I received an out of office assistant message from Shayan. Please let us know if we shall plan to set up a call with you as we will want to bring closure to the pension analysis as soon as possible.

Thanks.

Nadine

From: Petsche, Nadine (TBS)
Sent: June 12, 2017 11:26 AM
To: Shayan Jafrani
Cc: Fong, Pauline (TBS); Sun, Alicia (TBS); Ma, Patricia (TBS); Virani, Shyrose (TBS); Patel, Bharat (TBS); Uros Karadzic; Christina Chan
Subject: Fw: Public Accounts Related Q's

Shayan,

Below is the advice that we received from our legal services branch regarding liabilities for non-OPS employers. I think we should discuss implications to the analysis.

Nadine

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

Sent: Thursday, June 8, 2017 4:09 PM

To: Petsche, Nadine (TBS)

Cc: Hatzis, Len (TBS); Compagnone, Lisa (TBS)

Subject: RE: Public Accounts Related Q's

Nadine, here is an analysis of the potential funding risks for the Crown relating to the participation of non-OPS employers in the OTPP and OPSEUPP. The discussion of the OTPP reflects input from EDU legal and staff who are familiar with the OTPP.

I have kept this high level given the urgency but can elaborate on specific areas as necessary. I haven't included a discussion of the general obligations of employers and members to contribute to Jointly Sponsored Pension Plans under the *Pension Benefits Act* (PBA), or discussed the implications of the exemption from solvency funding requirements under the PBA that I understand both of these plans enjoy, as I understood the focus of your question to be specific to the relationship between the Crown and other employers.

If you require anything further please let us know.

Paul

OTPP:

· The OTPP is governed by the *Teachers' Pension Act* (TPA), the Plan text for the OTPP (the "Plan Text"), a Partners' Agreement between the Minister of Education and the Ontario Teachers' Federation, and a Funding Management Policy ("FMP") that is an appendix to the Partners' Agreement.

· The OTPP is also subject to the *Pension Benefits Act* ("PBA"), under which the OTPP is a Jointly Sponsored Pension Plan (JSPP)

· Under Section 24(1) of the Plan Text, the Minister of Education is required to pay employer contributions in respect of certain active employees. These types of active employees include teachers at school boards and teachers at provincial schools (run by the Ministry of Education and where teachers are the employees of the Provincial Schools Authority).

· However, the Minister is not required to make employer contributions under the Plan Text in respect of some other employers whose employees may participate in the

OTPP, including participating private schools.

· Nothing in the Plan Text (or any other applicable OTPP document or statute) expressly requires the Minister of Education to make contributions in place of private schools and other ‘excluded’ employers who have failed to make their own required contributions to the OTPP.

· However, the Crown could be exposed to a funding risk where a private school or similar employer fails to make their contributions in the following ways:

o Subsection 5(3) of the TPA requires the Province to make contributions to the OTPP fund if the assets in the fund are insufficient to make required payments in a particular year

o Private schools and other ‘excluded employers’ not making required payments could impact on the overall funded status of the plan, in turn affecting the ability of the Minister of Education and OTF to access surpluses in accordance with the FMP

OPSEUPP:

· The OPSEUPP is governed by a Sponsorship Agreement dated April 18, 1994, as amended, between Ontario and OPSEU (“Sponsorship Agreement”); a trust agreement dated October 25, 1994, as amended, the OPTrust Plan Text and the *Ontario Public Service Employees' Union Pension Act, 1994*.

· Like the OTPP, the OPSEUPP is also a JSPP under the PBA.

· A list of participating employers for the OPSEUPP is set out below (this information is derived from the OPSEUPP’s most recent audited financial statements, but you may wish to verify it with the TBS Employee Relations Division). A number of the participating employers that are not part of the Province itself are nevertheless provincial agencies (AGCO, LCBO, OLGC, Public Health Ontario, etc.). The majority of the remaining employers are either public hospitals (that the Province funds) or public sector pension plan administrators. Therefore, the practical risk of a non-OPS employer failing to provide required contributions to the OPSEUPP seems quite low.

· However, in the event that such an employer did fail to make its contributions, and that failure resulted in a deficiency in the OPSEUPP fund, the Province (likely in conjunction with the other employers whose employees are members of the OPSEUPP), and the members would jointly be required to provide further contributions to the fund to address any such deficiency, pursuant to section 58 of the Sponsorship Agreement and section 6.3(5) of the OPTrust Plan Text.

- The Province of Ontario (civil servants and crown employees)
- Alcohol and Gaming Commission of Ontario
- Centre for Addiction and Mental Health
- Legislative Assembly of Ontario
- Liquor Control Board of Ontario
- Niagara Parks Commission
- North Bay Regional Health Centre (Northeast Mental Health Centre)
- Ontario Agency for Health Protection and Promotion
- Ontario Lottery and Gaming Corporation
- Ontario Pension Board
- Ontario College of Trades
- Ontario Public Service Employees Union (seconded or acting employees)
- Ontario Shores Centre for Mental Health Sciences
- Ontario Teachers' Pension Plan Board
- OPSEU Pension Plan Trust Fund (includes non-bargaining unit employees)
- Providence Continuing Care Centre
- St. Joseph's Care Group – Lakehead Psychiatric Hospital
- Waypoint Centre for Mental Health Care
- Workplace Safety and Insurance Appeals Tribunal

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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FW_ Request to share Accounting Opinion.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: Request to share Accounting Opinion
Date: Friday, October 21, 2016 12:58:46

Cindy,

Below is the request language shared previously. Please advise if you would like any edits. In the meantime, I had also asked Matt if they want different wording in light of a 'panel' related request vs. PwC. N

From: Petsche, Nadine (TBS)
Sent: October 18, 2016 10:43 AM
To: Veinot, Cindy (TBS)
Subject: FW: Request to share Accounting Opinion

Cindy,

Please see below. Once the request para has been edited, we can seek permission to share with the Panel as well. Because sharing with the Panel carries a higher level of risk, we may want Legal to review the request before we send it.

Nadine

From: Danyluk, Kerry (CA - Toronto)

Sent: Friday, October 14, 2016 5:06 PM

To: Petsche, Nadine (TBS); Colley, Matthew (CA - Toronto)

Subject: RE: Request to share Accounting Opinion

Hi, Nadine. We consent to our S. 7600 report dated October 2 being provided to PwC for the purpose you have noted below. This consent only applies to a release to PwC at this time.

Thank you.

Kerry

--

Kerry Danyluk

Partner | National Accounting and Assurance

D: +1 (416) 775 7183

kdanyluk@deloitte.ca | deloitte.ca

--

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of the Canadian Olympic team

Please consider the environment before printing.

From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Friday, October 14, 2016 10:45 AM
To: Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Cc: Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>
Subject: Request to share Accounting Opinion

Matt,

Further to our discussion, we are seeking permission to share the Section 7600 report with PricewaterhouseCoopers, today if possible.

Please see our request below. We look forward to hearing back from you.

Thanks.

Nadine

This note is to confirm that Deloitte LLP (“Deloitte”) consents to the disclosure of its work product, including the accounting opinion, developed by Deloitte as part of or in connection with the work being done by PricewaterhouseCoopers LLP to assist Treasury Board Secretariat in compiling a Whitepaper describing the Province’s position on Pension Asset accounting. The purpose of the disclosure is to allow PricewaterhouseCoopers LLP to review and consider the Deloitte LLP documentation in compiling the above-noted Whitepaper. The Whitepaper will not be based solely on Deloitte’s work, but for purposes of consistency and completeness, it is considered beneficial to allow PricewaterhouseCoopers LLP to access the Deloitte’s document. Please confirm your consent by responding to Karen Hughes and cc’ing me on your response.

Best regards,

Nadine

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FW_ Review_ Valuation Allowance.rtf

From: Petsche, Nadine (TBS) []
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
CC: Killoch, Alex (MOF) [Alex.Killoch@ontario.ca]
Subject: FW: Review: Valuation Allowance
Date: Thursday, September 22, 2016 19:20:25

Cindy,

We've been sending a variety of requests to OTPP. If they are going to be asked about this item, are there other items we might want to enquire about based on today's discussions?

Nadine

From: Killoch, Alex (MOF)
Sent: September 22, 2016 5:02 PM
To: Petsche, Nadine (TBS)
Subject: RE: Review: Valuation Allowance

I would think that I have to ask the OTPP if they have the analysis.

This would assume that the partners did not spend the surplus as it arose. Now that I have thought more about it, the partners are unlikely to leave enough surplus in the plan to get to the cap. They will want to spend it as it arrives. As you can see in the temporary funding zone deck, we are very unlikely to get to the permanent improvement zone due to the creation of the temporary zone.

Do you want me to pursue the question with OTPP?

From: Petsche, Nadine (TBS)
Sent: Thursday, September 22, 2016 4:49 PM
To: Killoch, Alex (MOF)
Subject: Fw: Review: Valuation Allowance

On meetings for the rest of the day. Are you able to belp? N

From: lucy.durocher@ca.pwc.com

Sent: Thursday, September 22, 2016 4:30 PM

To: Veinot, Cindy (TBS)

Cc: Petsche, Nadine (TBS)

Subject: Re: FW: Review: Valuation Allowance

Thanks for sending that through Cindy. I will take a look at it.

I forgot to ask on the call whether you and Nadine had given any consideration to the impact of scheduling out anticipated (funding) surplus growth assuming that current service cost remains the same in perpetuity and minimum funding requirements are greater than current service cost under the current Schedule 1 contributions. It might take a long time, but eventually there would be a significant build up of surplus such that the cap on contributions in Schedule 1 section 19 (2a) would kick in (i.e. when the income tax act would not cap contributions). As soon as the minimum contributions under the Schedule 1 drops below the current service cost then you can start to recognize a benefit under paragraph 056 (a) calculations. The only question is, depending on the expectations of surplus growth and when the ITA caps kick in, is when does this occur, and how big is the effect. You have until perpetuity to reach the caps, but obviously the further away the cap is reached, then the lower the benefit when discounted back.

I have reached out to find the right contact in the Netherlands. Given the time difference, I am not sure I will know by tomorrow morning, but I will keep you posted on that avenue.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223

PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Veinot, Cindy (TBS)" <Cindy.Veinot@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
Date: 09/22/2016 03:48 PM
Subject: FW: Review: Valuation Allowance

See line 41 of the first tab -- Cindy

From: Fong, Pauline (TBS)
Sent: September-21-16 4:37 PM
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca)
Cc: Veinot, Cindy (TBS); Patel, Bharat (TBS)
Subject: FW: Review: Valuation Allowance

Thank you.

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-21-16 4:10 PM
To: Fong, Pauline (TBS)
Cc: Veinot, Cindy (TBS); Patel, Bharat (TBS); Colley, Matthew (CA - Toronto); Danyluk, Kerry (CA - Toronto)
Subject: RE: Review: Valuation Allowance

Pauline

I did look into your file and seems reasonable vs the previous illustrations that we have exchanged, just one adjustment
You will see in liability sheet I have a line 29 adjustment for other unamortized (this is the transitional asset amortization that goes back to the initial application which is to be included in the test of unamortized losses) this likely affects your 2002 / 2003 valuation allowance.

Also to note is the flaw of the PS3250 that I have highlighted in previous communication :

- In 2008 we did have very bad asset returns and this creates a significant income

through reduction of valuation allowance
- In opposite, the years 2010 and 2011 had good returns but you have significant expense through increase of valuation allowance

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services
Deloitte
1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada
Tel / Direct : 514-393-7367
Fax : 514-390-4104
maraymond@deloitte.ca | www.deloitte.ca

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De : Fong, Pauline (TBS) [mailto:Pauline.Fong@ontario.ca]
Envoyé : 21 septembre 2016 10:36
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>; Patel, Bharat (TBS) <Bharat.Patel3@ontario.ca>
Objet : Review: Valuation Allowance

Hi Martin,

I mocked up the annual valuation allowance based on our discussion yesterday. We went through it with Cindy this morning and she would like you to take a look at the mock-up to confirm that it is consistent to your understanding. In particular bringing the unamortized gain/loss from market related values to market values. Thank you in advance.

Regards,

Pauline Fong, CPA, CA
Senior Analyst, External Reporting
Office of the Provincial Controller Division |Office of the Treasury Board |Treasury Board Secretariat
7 Queen's Park Crescent, Frost South, 2nd Floor, Toronto, ON, M7A 1Y7
Phone: (416) 212-4007

Pauline.fong@ontario.ca

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FW_ Review_ Valuation Allowance.rtf

From: Veinot, Cindy (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Review: Valuation Allowance
Date: Thursday, September 22, 2016 15:48:34
Attachment 1: image002.png
Attachment 2: image003.png
Attachment 3: OTPP (incl RCA) Calculations 2015-16 PAv3 (Basis 3) with Valuation Allowance_check.xlsx

---

See line 41 of the first tab -- Cindy

From: Fong, Pauline (TBS)
Sent: September-21-16 4:37 PM
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca)
Cc: Veinot, Cindy (TBS); Patel, Bharat (TBS)
Subject: FW: Review: Valuation Allowance

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From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: September-21-16 4:10 PM
To: Fong, Pauline (TBS)
Cc: Veinot, Cindy (TBS); Patel, Bharat (TBS); Colley, Matthew (CA - Toronto); Danyluk, Kerry (CA - Toronto)
Subject: RE: Review: Valuation Allowance

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Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Fong, Pauline (TBS) [mailto:Pauline.Fong@ontario.ca]
Envoyé : 21 septembre 2016 10:36
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>; Patel, Bharat (TBS)

<Bharat.Patel3@ontario.ca>
Objet : Review: Valuation Allowance

Hi Martin,

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Regards,

Pauline Fong, CPA, CA

Senior Analyst, External Reporting

Office of the Provincial Controller Division |Office of the Treasury Board |Treasury Board Secretariat

7 Queen's Park Crescent, Frost South, 2nd Floor, Toronto, ON, M7A 1Y7

Phone: (416) 212-4007

Pauline.fong@ontario.ca

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TBS

OTPP (incl RCA) Calculations 2015-16 PAv3 (Basis 3) with Valuation Allowance_check.pdf

Ontario Teachers' Pension Plan - PSAB Calculations

Pension Liability

Calendar Year	Source	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013-14 2013	2014-15 2014	2015-16 2015
Market Value of Assets (MVA)																							
Accrued Benefit Obligation (100%)	Data input	36,848	39,007	41,833	46,470	48,635	50,346	55,087	64,369	67,319	71,009	74,089	80,371	83,120	88,356	92,022	96,608	99,117	103,693	105,954	109,524	113,801	116,367
Market Value of Assets (100%)	Data input	34,494	40,137	47,429	54,479	59,170	68,303	73,121	69,456	66,213	75,677	84,326	96,128	106,014	108,546	87,433	96,408	107,590	117,099	129,524	140,764	154,476	171,440
(Asset)/Liability or (Surplus)/Deficit (100%)	*formula*	2,354	(1,130)	(5,596)	(8,009)	(10,535)	(17,957)	(18,034)	(5,087)	1,106	(4,668)	(10,237)	(15,757)	(22,894)	(20,190)	4,589	200	(8,473)	(13,406)	(23,570)	(31,240)	(40,675)	(55,073)
Accrued Benefit Obligation (50%)	*formula*	18,424	19,504	20,917	23,235	24,318	25,173	27,544	32,185	33,660	35,505	37,045	40,186	41,560	44,178	46,011	48,304	49,559	51,847	52,977	54,762	56,901	58,184
Market Value of Assets (50%)	*formula*	17,247	20,069	23,715	27,240	29,585	34,152	36,561	34,728	33,107	37,839	42,163	48,064	53,007	54,273	43,717	48,204	53,795	58,550	64,762	70,382	77,238	85,720
(Asset)/Liability or (Surplus)/Deficit (50%)	*formula*	1,177	(565)	(2,798)	(4,005)	(5,268)	(8,979)	(9,017)	(2,544)	553	(2,334)	(5,119)	(7,879)	(11,447)	(10,095)	2,295	100	(4,237)	(6,703)	(11,785)	(15,620)	(20,338)	(27,537)
Market Related Value of Assets (MRVA)																							
Accrued Benefit Obligation (100%)	Data input	36,848	39,007	41,833	46,470	48,635	50,346	55,087	64,369	67,319	71,009	74,089	80,371	83,120	88,356	92,022	96,608	99,117	103,693	105,954	109,524	113,801	116,367
Market Related Value of Assets (100%)	Data input	34,242	38,092	43,013	48,901	54,382	61,039	68,780	72,429	75,857	79,157	82,791	88,694	94,850	104,917	106,957	109,112	114,246	115,685	119,864	130,867	143,076	156,998
(Asset)/Liability or (Surplus)/Deficit (100%)	*formula*	2,606	915	(1,180)	(2,431)	(5,747)	(10,693)	(13,693)	(8,060)	(8,538)	(8,148)	(8,702)	(8,323)	(11,730)	(16,561)	(14,935)	(12,504)	(15,129)	(11,992)	(13,910)	(21,343)	(29,275)	(40,631)
Accrued Benefit Obligation (50%)	*formula*	18,424	19,504	20,917	23,235	24,318	25,173	27,544	32,185	33,660	35,505	37,045	40,186	41,560	44,178	46,011	48,304	49,559	51,847	52,977	54,762	56,901	58,184
Market Related Value of Assets (50%)	*formula*	17,121	19,046	21,507	24,451	27,191	30,520	34,390	36,215	37,929	39,579	41,396	44,347	47,425	52,459	53,479	54,556	57,123	57,843	59,932	65,434	71,538	78,499
(Asset)/Liability or (Surplus)/Deficit (50%)	*formula*	1,303	458	(590)	(1,216)	(2,874)	(5,347)	(6,847)	(4,030)	(4,269)	(4,074)	(4,351)	(4,162)	(5,865)	(8,281)	(7,468)	(6,252)	(7,565)	(5,996)	(6,955)	(10,672)	(14,638)	(20,316)
Province's 50% Share																							
Unamortized gains/(losses) on **Market Related Value of Assets (MRVA)**	"liability" sheet	747	1,618	2,252	2,676	3,727	5,476	6,066	2,750	2,646	2,112	2,028	1,493	2,888	4,560	2,617	277	772	(1,648)	(1,237)	1,851	4,816	9,001
Add: Difference between MVA vs. MRVA	*formula*	126	1,023	2,208	2,789	2,394	3,632	2,171	(1,487)	(4,822)	(1,740)	768	3,717	5,582	1,815	(9,762)	(6,352)	(3,328)	707	4,830	4,949	5,700	7,221
Unamortized gains/(losses) determined by Market Value of Assets (MVA)	*formula*	**873**	**2,641**	**4,460**	**5,465**	**6,121**	**9,108**	**8,236**	**1,264**	**(2,176)**	**372**	**2,795**	**5,210**	**8,470**	**6,375**	**(7,145)**	**(6,075)**	**(2,556)**	**(941)**	**3,593**	**6,800**	**10,516**	**16,222**
OTHER UNAMORTIZED AMOUNTS		2090	1916	1742	1568	1394	1220	1046	871	698	524	350	176	0	0	0	0	0	0	0	0	0	0
difference 3 months		404.8175	401.3175	351.3175	338.3175	351.8175	410.3175	421.3175	435.800315	449.178902	472.2073145	497.1354975	522.530731	529.4575806	649.8355402	687.3208344	763.5210495	773.8754106	799.4542262	825.9110373	853.0183569	881.6033156	895.469566
other adjustments		214	175.5	12	-237.5	-453	-437.5	-404.5	-363.51719	-315.138598	-267.6101855	-214.6820025	-155.786769	-113.8452135	54.047452	136.047452	206.2532665	219.5216191	221.6828321	241.7861416	256.7256986	273.2409646	271.7546695
Check		4,758	4,569	3,768	3,130	2,147	1,322	282	(336)	(791)	(1,233)	(1,691)	(2,126)	(2,562)	(3,016)	(4,027)	(5,005)	(5,799)	(6,623)	(7,124)	(7,711)	(8,667)	(10,147)
Accrued Benefit Liability (Asset) before any valuation allowance (50% share)	"Liability" Sheet	4,758	4,569	4,018	3,130	2,147	1,322	282	(336)	(791)	(1,233)	(1,691)	(2,126)	(2,562)	(3,016)	(4,027)	(5,005)	(5,799)	(6,623)	(7,124)	(7,711)	(8,667)	(10,147)
Less: Unamortized losses of MVA if any	*above*	-	-	-	-	-	-	-	-	(1,478)	-	-	-	-	-	(7,145)	(6,075)	(2,556)	(941)	-	-	-	-
Adjusted Accrued Benefit Liability (Asset)		4,758	4,569	4,018	3,130	2,147	1,322	282	(336)	687	(1,233)	(1,691)	(2,126)	(2,562)	(3,016)	3,118	1,070	(3,243)	(5,682)	(7,124)	(7,711)	(8,667)	(10,147)
Expected Future Benefit	if assumed zero								-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Valuation Allowance		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**336**	**-**	**1,233**	**1,691**	**2,126**	**2,562**	**3,016**	**-**	**-**	**3,243**	**5,682**	**7,124**	**7,711**	**8,667**	**10,147**
Expense as result of Increase (reduction) in valuation Allowance		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**336**	**(336)**	**1,233**	**458**	**435**	**436**	**454**	**(3,016)**	**-**	**3,243**	**2,439**	**1,442**	**587**	**956**	**1,480**
Accrued Benefit Liability (Asset) before any valuation allowance (50% share)		4,758	4,569	4,018	3,130	2,147	1,322	282	(336)	(791)	(1,233)	(1,691)	(2,126)	(2,562)	(3,016)	(4,027)	(5,005)	(5,799)	(6,623)	(7,124)	(7,711)	(8,667)	(10,147)
Less: Valuation Allowance		-	-	-	-	-	-	-	336	-	1,233	1,691	2,126	2,562	3,016	-	-	3,243	5,682	7,124	7,711	8,667	10,147
Accrued Benefit (Asset) Liability after valuation Allowance		**4,758**	**4,569**	**4,018**	**3,130**	**2,147**	**1,322**	**282**	**-**	**(791)**	**-**	**-**	**-**	**-**	**-**	**(4,027)**	**(5,005)**	**(2,556)**	**(941)**	**-**	**-**	**-**	**-**
		-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

FW_ Revised Pension Asset Position Paper.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Jim Keates (jimkeates@hotmail.com) [jimkeates@hotmail.com]
Subject: FW: Revised Pension Asset Position Paper
Date: Monday, October 31, 2016 09:19:09
Attachment 1: compare doc oct 22 vs oct 28 position papers.docx
Attachment 2: Draft Pension Asset Position Paper Oct 28 clean to cv.docx

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Lucy,

Just as an FYI, sharing the version of the document provided to Cindy for her review on the weekend. Will also share a copy of the draft deck in a separate email.

Nadine

From: Petsche, Nadine (TBS)
Sent: October 28, 2016 10:27 PM
To: Veinot, Cindy (TBS)
Cc: Keates, James (TBS)
Subject: Revised Pension Asset Position Paper

Cindy,

Attached is the revised version of the Pension Asset Position Paper, both a clean copy as well as a compare doc to the initial version provided last week for your review. There are a couple of areas that are still being worked on as noted in the comments.

A draft briefing deck is also being drafted, based on the outline of this version of the report. A draft of the deck will be ready for your review early next week.

Nadine

compare doc oct 22 vs oct 28 position papers.pdf

Position paper for Ontario Teachers' Pension Plan

Preamble

Style Definition: Comment Text

This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

~~A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.~~

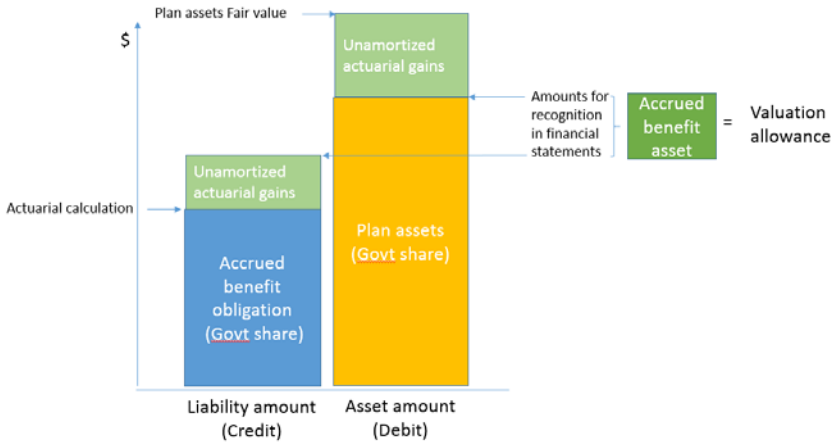
Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP. This position paper addresses the analysis for OTPP. A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

As described in PSAS, ~~a~~ an accrued benefit asset (pension asset) arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. ~~Contributions reflect the funding objectives of the plan. The benefit~~ An Accrued Benefit Asset (AcBA) includes the effect of net unamortized experience gains or losses. Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation. OTPP currently has net unamortized experience gains. The following illustration reflects the compilation of the net pension asset (accrued benefit asset) reported on the Province's

DRAFT

books for the OTPP.



It is important to note that contributions to the plan are based on funding objectives of the plan. In contrast, Benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (~~or~~ plan surplus for accounting purposes) in OTPP ~~and OPSEUPP are~~is an asset to the ~~province~~Province and it is ~~suitable~~appropriate to reflect ~~them~~it in the financial results in accordance with PSAS. The Province has also concluded that no valuation allowance under PSAS is required against the asset as at March 31, 2016.

The OAG disagrees with this position. The OAG 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~~as such that ~~right, because~~ the Province does not ~~have~~ control the assets which the OAG interprets PSAS as requiring. Further, the OAG considers the lack of an enforceable agreement ~~in place~~at year-end with the Ontario Teachers' Federation (OTF) ~~with respect to how~~dictating lower contributions in the ~~surplus would be utilized such~~future as requiring that ~~it would provide~~ a ~~benefit to the Province, a pension~~full asset ~~in the Public Accounts is not appropriate.~~valuation allowance be taken against the asset under PSAS.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. RETIREMENT BENEFITS, Section PS 3250 of the PSA Handbook addresses the accounting of obligations for employee retirement benefits in government financial statements. Since 2001, there have been no consequential changes to Section PS 3250. As a result Ontario ~~had~~has followed the same pension accounting treatment for ~~all of~~OTPP over the past 14 years. The pension liability (asset) and expense reported by the Province of Ontario for OTPP over the

Commented [NP1]:

LD – Pauline/Jim – please confirm that details are relevant to OTPP situation.

period is reflected in Appendix F. Unqualified audit reports have been received for each of the years from the OAG on the Public Accounts. ~~This~~ The pension accounting initially adopted by the Province for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals. ~~There has been no change to the relevant PSAS (i.e. RETIREMENT BENEFIT, Section PS 3250) over the past 14 years.~~ for the prior years.

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~~A regulation was made~~In light of the contrasting views on interpretation of PS 3250 to the Province's jointly sponsored pension plans, a regulation was necessary to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The ~~Province filed a~~regulation is time-limited ~~regulation, which~~and legislates the accounting for pension assets of its two jointly-sponsored pension plans (OTPP and OPSEUPP) for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The ~~impact of the~~ change in accounting treatment for 2015-16 resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the 2015-16 annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to ~~write off the pension assets.~~reflect the Auditor General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

~~**What is being asked of the Expert Advisory Panel**~~

~~The Expert Advisory Panel is being asked to review and deliver advice and recommendations to the government as to the application of PSAS to Ontario's pension assets. The future accounting by the Government of its pension assets will be guided by the report of the Expert Advisory Panel.~~

~~The Expert Advisory Panel 's advice and recommendations to the government will address:~~

- ~~The requirement regarding control (or shared control) with respect to recognizing a pension asset for a defined benefit plan, as it relates to the pension plans reported by the Province of Ontario, including OTPP, OPSEUPP, HOOPP, and CAAT.~~
- ~~Appropriate valuation techniques to measure a pension asset that take into consideration future decision-making authority by plan sponsors.~~
- ~~Recommendations to the Employment Benefits Task Force of the Public Sector Accounting Board (PSAB) regarding issues that should be considered in their review of the retirement and post-employment benefits standards.~~

Position paper for Ontario Teachers' Pension Plan

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1.

The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the ~~Ontario Teachers' Federation represented by its Executive (the "~~OTF~~")~~ (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the ~~Partners~~Partners' Agreement (FMP);
~~f) The Ontario Teachers' Pension Plan; and~~
~~g)~~f) ~~-~~The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
~~1~~a. It provides defined benefits.
~~2~~b. The defined benefits are contributory benefits.
~~3~~c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
~~4~~d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA 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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5][6] This clause has been interpreted as a short term solvency protection clause, rather than a clause that transfers substantive residual risk to the Province, as the rest of the arrangement is structured such that the risk of these payments is minimal and the risks of the long term funding of the plan must still be equitably shared. The Province is also permitted to make additional contributions in respect of a solvency deficiency[7] (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, 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 inception of the plan in 1917). [8] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

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[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).
[5] ~~TPA, subsection 5(3).~~
[6] TPA, subsection 5(3).
[7] TPA, subsection 5(7).
[8] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/~~101791209401 l5e47lc2b~~10179/20940/-/5e471c2b-23f1-44e6-~~b5cld22e3e50dbc3lHow~~b5c1d22e3e50dbc3/How+Contribution+Rates~~*HaverEvolved~~+Have+Evolved.pdf As noted above, for the period from January l, 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.~~20lo~~20% versus ~~l0.4yo/l2Vo,~~10.4%/12%, respectively). It ~~js~~is

~~Currently, the Sponsors are also required to mutually agree upon how any plan deficits are to be addressed.[9] 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 a JSPP, 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~~Partner's Agreement requires the Sponsors to negotiate and agree upon decisions relating to surplus or deficit utilization, which currently is outlined in the FMP. [10] The FMP indicates that deficits (or surpluses) may be addressed through increases (decreases) to the contribution rates, lowering (increasing) the amount of indexation and/or other decreases (increases) in benefits. While not binding upon the Sponsors, as the Sponsors can change the FMP at any time, any changes are required to have the mutual consent of both Sponsors. Accordingly, the Sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix ~~E~~B. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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

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.

~~[9] See, for example, Section 3.09 and 3.11 of the FMP.~~

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

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.

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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~~funding surpluses 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. ~~When negotiations~~Negotiations on the use of the surplus occur ~~is laid out~~as specified in the Partners' Agreement. The Partner's Agreement requires that any actuarial funding valuation submitted to the pension regulators must be "actuarially balanced" (Section 57 of the Partners' Agreement). This must occur at least once every three years, but can occur every year if the partners agree. If a preliminary funding valuation shows a funding surplus or deficit then the joint sponsors must negotiate how this surplus or deficit is to be resolved prior to filing the funding valuation.

Accounting for OTPP by the Province

Since fiscal year 2001-2002, the Province has recorded a pension asset for OTPP on the Statement of Financial Position. A pension asset has arisen because the government's share (50%) of the total

contributions to OTPP plus ~~the actual~~recognized investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense~~.~~ (see illustrative examples in Appendix J). The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

~~The~~With regards to any comparisons between surplus or deficit amounts reported in the Province's financial statements verses the OTPP's financial statements or funding reports, it is important to acknowledge the different objectives of funding and accounting for a pension plan which are also explicitly addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.*

~~Paragraph~~Section PS 3250 paragraph .051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: "Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…"

OTPP's most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website. The Province's relative portion of this surplus would be $6.6 billion. The OTPP's public financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015~~.~~, for which the Province's portion would be a deficit of $900 million. The following background helps to clarify the reasons for these different results. OTPP's financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook ("Part IV"), which is a different accounting framework than

the Province uses for its financial reporting and is also a different framework than is used to calculate the ~~funding~~net surplus or deficit~~.~~ for funding purposes.

Accounting for employee future benefits requires the use of assumptions and methodologies to calculate both the obligation incurred to date and the value of the assets already set aside to meet those obligations. Accounting frameworks differ in standards that must be applied in determining appropriate assumptions and methodologies. Further, the assumptions and methodologies used in developing a "funding valuation" on a going concern basis may also differ from those required by accounting standards. These differences result in a number of different valuations for the same plan, depending on the purpose of the valuation and can be affected by certain choices made between acceptable options within each framework. A summary of the main differences between the methodologies used to calculate a going concern funding valuation, OTPP's accounting valuation and the Province's accounting valuation is shown in Appendix ~~H~~D.

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Specifically, the discount rate used to value the obligations of the plan has a significant impact on the overall position of the plan. A lower discount rate results in a higher liability and a higher discount rate results in a lower liability, all else being equal. Put another way, a higher estimate of the time-value of money makes the promises made today that will be paid out in the future cheaper. ~~Both the PSAS accepted discount rate based on the expected asset return and the IFRS required discount rate of corporate/government bonds are "best estimate" rates. They must both be based on management's best estimate of the applicable discount rate.~~ OTPP uses a discount rate based on corporate/government bond rates in its financial statements, as permitted by Part IV. The Province uses a discount rate based on the expected asset return, as permitted by PSAS. ~~In both cases the estimates must be supportable. The difference result not from one being more "right" or "wrong" than the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.~~ The rationale for using a corporate or government bond approach is that a pension promise is akin to a bond as it is a promise to pay a series of cash flows in the future regardless of what the asset returns actually are (which could be higher or lower than expected). The rationale for using an asset return approach is that it represents the amount of contributions that, combined with investment returns, should be sufficient to pay the promised benefits, particularly as pension plans will often invest in higher risk/higher return assets then simple corporate bonds. Both a discount rate based on the expected asset return and one based on corporate/government bonds are "best estimate" rates; they must both be based on management's best estimate of the applicable discount rate. In both cases the estimates must be supportable. The difference results not from one being more "right" or "wrong" relative to the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.

Typically the funding discount rate used for the funding valuation falls between the bond discount rate and the expected asset return, but it differs in that it does not purport to be the "best estimate" of the discount rate, ~~but~~rather it is designed to indicate the contributions that are required to fund the promised benefits~~,~~ with an additional conservative margin for adverse deviations. Note that over the

long term the difference between funding valuations and accounting valuations would diminish as the impact of the discount rate unwinds and the asset valuation methods converge.

In practice, the discount rates used in the financial statements of government sponsored and joint defined benefit pension plans prepared under Part IV of the CPA Canada Handbook (Section 4600) use diverse methodologies. For example, in Alberta ~~7~~there are seven plans which prepare their financial statements under Part IV with reference to IFRS (same framework as OTPP). Of these none use a government bond discount rate and all use a discount rate calculated with some reference to a rate of return on invested assets, which may include factors for expenses, diversification and rebalancing. The analysis of a number of government sponsored plans is included as Appendix ~~[G]~~ E. The analysis demonstrates that a significant number of government sponsored plans use a discount rate aligned to an asset investment return rather than a bond discount rate. OTPP is actually in the minority of plans that choose to use the rate required by IFRS, resulting in a lower discount rate and higher liability for financial reporting purposes.

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~~The above analysis indicates that the presentation of a deficit~~The above analysis explains how different discount rates impact the net surplus/deficit reported on OTPP's financial statements, OTPP funding reports and the Province's financial statements. The fact that OTPP reports a deficit on its financial statements, or that the 50% of the net surplus reported by OTPP for funding purposes is lower than the surplus reported on the government's financial statements under PSAB standards is of no consequence or relevance to the pension asset amount or pension expense reported by the Province for OTPP.

To further clarify, that there is a deficit reported in the OTPP financial statements while the Province of Ontario calculates a surplus under PSAS requirements does not mean that there is no accounting surplus and therefore no reportable asset for the Province. ~~It would be acceptable under~~ In fact, if the ~~Part IV framework for~~ OTPP ~~to have selected,~~ had chosen (as an acceptable accounting policy~~,~~ choice) to use a discount rate more consistent with its counterparts in other jurisdictions (see Appendix E) such as a discount rate based on an asset return which would be closer to that used by the Province ~~which~~, it would eliminate ~~a significant element~~much of the existing differences between the reported net surplus/deficit ~~for accounting purposes in~~ amounts between the OTPP statements and the ~~net surplus/deficit of the~~ Province's share of OTPP reported for accounting purposes in the Public Accounts.

~~Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook.~~ **Sufficiency of PS 3250 in assessing appropriate accounting for pension assets**

~~Unqualified audit reports have been received for each of the years from the OAG on the Public Accounts.~~

~~RETIREMENT BENEFIT, Section PS 3250 of the PSA Handbook addresses the accounting of obligations for employee retirement benefits in government financial statements. The Province has followed this standard over the prior 14 years. Over this period of time, there have been no consequential changes to~~

~~Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years.~~

~~The prior pension accounting for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals during this period of time.~~

~~Over the prior 14 years, the Province has classified OTPP as a joint defined benefit plan as per Section PS 3250 (this classification will be discussed more in this document). Over this period of time, the pension expense and pension liability (asset) for OTPP reported by the Province is reflected in Appendix F.~~

~~**History regarding the PSA standards**~~

~~As mentioned, the financial statements for the Province have been prepared over the prior 14 years in accordance with the PSA Handbook.~~

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150 prescribes that, in developing and applying accounting policies, all primary sources of GAAP should be applied~~.~~ (Section PS 1150 paragraph .04). Primary sources of GAAP are Sections PS ~~1200~~1201-PS 3510, Public Sector Guidelines and appendices and illustrative material to those pronouncements. Only when there are no primary sources of GAAP that relate to the transactions or events under consideration, or more specific guidance is needed~~,~~ (Section PS 1150 paragraph .05), does an entity consider other primary sources of GAAP dealing with similar issues and also the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000~~.~~ (issued January 2003). Section PS 1000 is not, however, a "primary source of GAAP" under the PSA Handbook.

The primary sources of GAAP specific to the accounting for pension assets is RETIREMENT BENEFITS, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, Section PS 3250 which was based on Accounting Statement No. 5).

Other primary sources of GAAP that deal with similar issues might also be considered where additional interpretation or guidance ~~is needed~~may be required. For the issues dealt with in this paper - recognition and measurement of a joint defined benefit plan - this could include standards that relate to ~~joint~~shared control, as OTPP is a joint defined benefit plan, standards that relate to the definition of an asset and standards that relate to measurement uncertainty:

- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015, effective from April 1, 2017)
- MEASUREMENT UNCERTAINTY, Section PS 2130 (issued in April 2005)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 which is more recent and will be effective in for periods beginning on or after April 1, 2017. Section PS 3210 provides additional guidance on the various components of the existing asset definition found in Section PS 1000; it does not change the definition.

Accounting Analysis

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Question 1 – ~~Recognition~~Classification of a pension asset

The analysis below addresses whether the Province's share of the pension surplus in OTPP, calculated in accordance with PSA standards under Section PS 3250, represents ~~an~~a reportable asset to the Province of Ontario ~~for purposes of preparation of~~in the Public Accounts.

Standards in the PSA Handbook

The focus of the following analysis is on the accounting requirements in RETIREMENT ~~BENEFIT~~BENEFITS, Section PS 3250 as this standard is a primary source of GAAP which specifically addresses the accounting for pension assets. The following highlights some key concepts and guidance contained in this standard.

RETIREMENT BENEFIT, Section PS 3250 – Purpose and Scope

The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250~~, paragraph~~ .003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

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RETIREMENT ~~BENEFIT~~BENEFITS, Section PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*
>
> *(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;*
>
> *(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and*
>
> *(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.*
>
> *The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.*

Additional guidance on identifying Joint Defined Benefit Plans (JDBPs) is in Section PS 3250 paragraphs .79 to .80 which similarly ~~highlights~~highlight the importance of both ~~shares~~shared control and shared risks and rewards in a JDBP:

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

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

~~A joint defined benefit plan (JDBP)~~It should be noted that the definition of a Joint Defined Benefit Plan under Section 3250 is not the same as the definition of a JSPP under the PBA, although there are some overlapping concepts between the two. A JDBP is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. The Province has concluded that OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. The OTPP is a contractual arrangement between the Province and OTF in which:

(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees ~~(addressed in paragraph 8 of the Partners' Agreement for example),~~ ;

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph ~~5~~10(1~~.1~~)3 of the TPA for example).

~~There is no uncertainty regarding the joint control of OTPP shared by the Province of Ontario and the Ontario Teachers Federation.~~ The TPA, the Partners' Agreement and the plan text collectively set out this shared control and that the Province of Ontario has an equitable sharing of the risks and rewards (surpluses and deficits) of the plan ~~based on~~, thus meeting the definition of a joint defined benefit plan.

The classification of OTPP as a JDBP for accounting purposes [and a JSPP under the PBA] by the Office of the Provincial Controller has been consistent since 2001 and ~~has~~had been consistently accepted ~~by the~~

~~OAG~~without question by the Office of the Auditor General, including throughout the 2015/16 Public Accounts.

~~**RETIREMENT BENEFIT, Section PS 3250 – Accounting**~~

Question 2 – Recognition of a pension asset for a JDBP

RETIREMENT BENEFITS, Section PS 3250 paragraphs .081 to .082 ~~mandate~~provide guidance on the accounting for a JDBP in the financial statements of the government sponsor. As OTPP meets the definition of a JDBP for the reasons noted above, the ~~Province should follow this guidance which states:~~relevant guidance for the Province for purposes of reporting retirement benefits in the Public Accounts includes:

> *.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]*
>
> *.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.*

Section PS 3250.81 clearly states that "The government should account for its portion of the plan in accordance with the standards for defined benefit plans". It is clear from this that only the government's portion of the plan is included in the government's financial statements consistent with the requirements of Section PS 3250 (recognition) and the measurement of that portion is based on the requirements of Section PS 3250 (measurement). ~~This paper discusses the two elements of recognition and measurement separately~~It is also then clear that the requirements of the standard for recognition and measurement, including the Limit of the Carrying Amount of an Accrued Benefit Asset guidance, are designed to be applied to a shared control situation and not only to situations where there is unilateral control. If it was intended that no pension asset could be recognized because the asset was subject to shared control and not unilateral control Section 3250 paragraph .081 would have made this clear. This paper discusses the question of measurement separately in Question 3.

The balance sheet recognition guidance for retirement benefits is stated in Section PS 3250 paragraphs .016 to .017:

> *.016 The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date. [SEPT. 2001]*
>
> *.017 The components of the retirement benefit liability are:*
>
> > *(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;*
> >
> > *(b) plan assets, if any; and*
> >
> > *(c) unamortized actuarial gains and losses.*

As the OTPP is a funded plan there are plan assets that are recognized as part of the retirement benefit liability. When plan assets and the net impact of unamortized actuarial gains and losses exceed the accrued benefit obligation then there is an "Accrued benefit asset" (ABA). An ABA is defined in Section PS 3250 as follows:

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

Accordingly, the portion of the government's plan to be recognized includes their share of the accrued benefit obligation and also their share of the plan assets. In the case of the Province's portion of OTPP there is no uncertainty regarding the *existence* of an ABA for the government's portion of the plan~~,~~ ~~based on the best estimate assumptions used in measuring the~~; the ABA is calculated by reference to accrued benefit obligation and plan assets, ~~measured in accordance~~both determined based on the best estimate assumptions and the methodologies required by with Section PS 3250 ~~guidance~~ for these items. As noted above an ABA is defined as the sum of the government's ~~sum of the~~ accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance). For a jointly sponsored plan, this is the government's accumulated cash contributions less ~~the sum of~~ the government's share of the current and prior years' benefit expenses that are attributable to the government under the joint defined benefit plan. The Province's portion of OTPP resulted in an ABA of $10.1 billion as at March 31, 2016. There is no uncertainty regarding the occurrence of the cash contributions made (~~including~~and the interest earned thereon) measured in accordance with Section PS 3250 and the existence of the government's obligation. As ~~Paragraph~~Section 3250.80 *requires* a government to account for its portion of the plan in accordance with the standards for defined benefit plans, this would include the recognition of any asset that meets the definition of an ABA under the standard.

Further, Section PS ~~3250 paragraph~~ 3250.50 refers to the presentation of the ABA; this amount is presented in the financial statements, net of any valuation allowance. This indicates that an ABA should

be recognized in the financial statements, but measured in reference to the limit on the carrying amount of the asset - essentially a measurement requirement rather than a recognition requirement, as the limit could result in an ABA ~~could be~~being measured at anything from $nil to its full amount. Note that the *measurement* of any net asset is subject to guidance in Section PS 3250 paragraphs .50-.59 and is discussed later in this paper.

To recognize only their share of the liability and not their share of the plan assets, or to recognize only a net liability (accrued benefit obligation exceeds plan assets) but never a net asset (when plan assets exceeds the accrued benefit obligation, subject to the valuation allowance guidance discussed in the Measurement section below), would indicate that the ~~government~~Province does not share equitably in the risks and rewards of the ~~plan~~OTPP because they bear only the risk of increased liabilities without being able to bear ~~the~~any rewards of investment returns on the plan assets and under this interpretation the plan would not therefore be a joint defined benefit plan.

Concept of Shared Control and ~~asset recognition~~Asset Recognition

Included in the definition of a JDBP is the concept of shared control. Points (~~c~~b) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of ~~Shared Control~~shared control resulting in a recognition of an asset ~~may be seen~~could on the surface appear to conflict with the definition of an asset under FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210, as part of the definition of an asset ~~is~~under PS 1000 would suggest that the government ~~can~~must control the economic resource and access to the future economic benefits. ~~Joint~~Since shared control does not equate to control, ~~therefore the introduction of ASSETS, Section PS 3210 raises the question as~~there is a need to consider whether the recognition of any asset ~~for which~~under PS 3250 is appropriate where there is only shared control ~~is precluded under PSAS.~~.

The Province's position is that PSAS does not preclude asset recognition for assets under ~~joint~~shared control and specifically for plan assets of joint defined benefit plans for the following reasons:

- As discussed above GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity. Section PS 3250 is a primary source of GAAP for dealing specifically with joint defined benefit plans and, as noted above, requires the government to account for their portion of the plan – both the accrued benefit obligation and plan assets in accordance with Section PS 3250. As such, reference to Section PS 3250 is sufficient to indicate that the recognition criteria are met for joint defined benefit plan assets, no further source of PSAS guidance need be considered.

- ~~If~~Similarly, if other primary sources of GAAP are considered then it is relevant to consider GOVERNMENT PARTNERSHIPS, Section PS 3060 which also includes the concept of shared

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control. Under Section PS 3060, ~~joint~~shared control is sufficient for asset recognition~~. It is therefore consistent with this primary sources of GAAP to recognize an asset for a jointly controlled defined benefit plan, subject to measurement guidance including impairment considerations~~.

- The concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. With the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that PSAB did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

- ~~similarity~~The Province's reporting of a pension asset for the JDBP is therefore consistent with these primary sources of GAAP, subject to measurement guidance including impairment considerations.

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The similarities between the definitions of a JDBP and a government partnership under PSAS are demonstrated in Appendix ~~B~~F to this paper, and further support ~~Section~~ PS 3060 as being a relevant primary source of GAAP dealing with similar circumstances, should it be considered necessary to go outside of the requirements of Section PS 3250 to look for further clarification and guidance on recognition.

Under Section PS 3060 a critical condition for a Government partnership is shared control. Section PS 3060 explicitly acknowledges that under shared control "none of the partners is in a position to exercise unilateral control over the government partnership" (PS 3060.20), yet the accounting model required by Section PS 3060 for non- GBPs[11] is that of proportionate consolidation which is the ~~picking up~~recognition of a pro rata share of assets, liabilities, revenues and expenses of the partnership. Joint defined benefit plans are excluded from the scope of Section PS 3060 on the basis that control is shared with employees rather than with a party outside of the reporting entity (Section PS 3060 paragraph .06 footnote 3). This reason indicates that such plans are excluded because of a closer relationship between the government and the other party than normally exists for government partnerships. Even when an independent third party shares control, Section PS 3060 still requires the recognition of a share in an asset subject to ~~joint~~shared control, indicating that the PSAS framework does not require unilateral control in order to support asset recognition when there is ~~joint~~shared control. It would not be appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3060 for proportionate consolidation, and similarly it is not appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3250 to account for

[11] Government business partnerships (GBPs) are accounted for under the modified equity method rather than proportionate consolidation.

the government's portion of a joint defined benefit plan. In other words, PS 3250 is a primary source of GAAP and provides sufficient and complete guidance on how to account for assets related to joint defined benefit plans.

~~The~~

Concept of Contingent Asset

CONTINGENT ASSETS, Section PS 3320, provides guidance on the disclosure of contingent assets in a government's financial statements. It characterizes a contingent asset as one where there is uncertainty as to the existence of an asset (Section PS 3320 paragraph .04). It is the Province's position that the existence of the pension asset is not uncertain – there is an accrued benefit asset calculated in accordance with Section PS 3250 as noted above that is based on past transactions, being the impact of cumulative contributions and benefit expense. The fact that shared control exists with regards to access to the assets of the plan does not create additional uncertainty that would impact asset recognition under PSAS. The Province anticipates that in a broad sense, s any OTPP surplus would be shared in an "equitable manner" under the terms of the arrangement, and this is enabled through the ability to negotiate the utilization of the surplus including the ability to prevent the utilization of the surplus in a manner that does not benefit the Province. This expectation is further supported by past history of surplus utilization (see Appendix G). The method, extent and timing of which the Province will obtain the expected future benefits (contributions reductions vs increase in benefits) is not certain. However Section PS 3320 also states "The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset. For example, even though there may be measurement uncertainty related to income tax receivable, there is nothing uncertain about the fact that this asset exists. Any uncertainty is related solely to the amount thereof" (Section PS 3320 paragraph .07). Based on past history of surplus utilization for OTPP and based on the constating documents, expected future benefits for the Government are present. The uncertainty as with many types of assets relates to measurement uncertainty which will be discussed below.

- ~~concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. On the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that PSAB did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.~~

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Conclusion on recognition

Therefore the Province has concluded that PSAS permits the ~~conceptual~~ recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets must be subject to unilateral control. The Province's share of OTPP's pension surplus meets the definition of an

Accrued Benefit Asset under Section PS 3250. The measurement of that accrued benefit asset is determined by reference to the guidance in Section PS 3250 regarding the Limit on the Carrying Amount of an Accrued Benefit Asset, which is discussed in Question 2 of this position paper.

Question ~~2~~3 – Measurement of a pension asset

~~For an asset to be recognized it must be reliably measureable. Section PS paragraphs 3250.050 to .059 address how to measure a pension asset. "When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit." Paragraphs~~For an asset to be recognized it must be reliably measureable (Section PS 1000.55). Section PS 3250 paragraphs .050 to .059 address how to measure a pension asset. This is a two-step process. Firstly the accrued plan obligation (a Credit) and the plan assets (a Debit) are measured in accordance with the standard, and adjusted for any unamortized actuarial gains or losses (a Debit for gains not yet realized, a Credit for losses not yet realized). This measurement results in a retirement benefit liability when it is a net liability (a Credit) amount or an accrued benefit asset when it is a net asset (a Debit) amount. When the resulting amount is an asset, the standard requires a second step to test that the asset is not impaired. It should be noted that impairment testing in some form is required for all assets recognized under PSAS standards except those carried at fair value, although the methodology of impairment tests will vary depending on the nature of the asset. The amount that is tested is the "adjusted benefit asset". When there are net unamortized gains the ABA is equal to the adjusted benefit asset. When there are net unamortized losses the ABA is reduced by those net unamortized losses to calculate the adjusted benefit asset. A graphical illustration of the calculation of the Accrued Benefit Asset (AcBA) and the Adjusted Benefit Asset (AdBA) are shown in appendix C. Section PS 3250 paragraphs .052 to .059 go on to explain what the standard means by expected future benefit and how a government may benefit from the ABA~~.~~ or adjusted benefit asset. Note that for OTPP the accrued benefit asset equals the adjusted benefit asset as there are net unamortized actuarial gains.

Section PS 3250.50-.59 are included here for completeness and ease of reference:

> ***Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)***
>
> *.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]*

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

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

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

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

.055 The objective of the standard in Section PS 3250 paragraph PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

calculate this present value is the expected rate of return on plan assets used to determine the benefit expense in the period.

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

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

Note that for purposes of Section PS 3250.053 the Province has

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determined that the accrued benefit asset equals the adjustment benefit asset: (due to unamortized actuarial gains exceeding unamo

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~~rtized actuarial losses).~~ Section 3250 paragraph

~~Paragraph~~ .052 states that a government may benefit from an ABA by either i) withdrawing surplus assets from the plan or ii) by taking a contribution holiday or receiving a refund of contributions. ~~It~~This is an explanatory paragraph on how a government may benefit from an ~~accrued benefit asset~~ABA and why ~~an~~a valuation allowance may be needed, rather than detailing the test to be applied. Part of this justification is to note that that an ABA may be impaired when "the government is not entitled to benefit from [the ABA] fully". Examples of when a government may not be entitled to benefit from the ABA fully are given, such as a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

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~~As such, the Province's present~~Section PS 3250 paragraph .059 gives additional guidance to apply when an entity contemplates realizing future benefits through a surplus withdrawal: "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal". This introduces the concept of a legally enforceable right but only in the context of a government's withdrawal of surplus and not in the context of contribution holidays. If the standard setters had intended legal enforceability to be the test throughout the standard, they would not have raised it only in the context of a withdrawal of surplus, but as a more fundamental notion in the guidance on expected future benefit.

It is acknowledged that the Province does not have a unilateral legal right to reduce its contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to shared control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Section 3250 paragraph .052 does not state that being "entitled to benefit" means having a legally enforceable right as at the reporting date to take contribution holidays. When considering the

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ability to realize expected future benefits under Section PS 3250 paragraph .052, the Province's legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability~~.~~ which is not explicitly required by the standard to support recognition and measurement of JDBP pension assets. Specifically, the amount of ~~Pension Asset~~pension asset that gets recorded needs to ~~be subject to~~take into account considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a ~~Pension Asset.~~ pension asset in the Public Accounts. Pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". Expected does not equate to certainty (Section PS 1000.056).

~~While the Province does not have a unilateral legal right to reduce their contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to joint control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Paragraph .052 does not state that being "entitled to benefit" means having a current legally enforceable right to take contribution holidays or withdraw surplus. Under the plan text and Partners' Agreement means that if funding surpluses occur the partners must~~Under the Plan and Partners' Agreement, if funding surpluses occur the partners are required to negotiate the use of the funding surplus (at least once every three years) and the Province is entitled to negotiate a reduction in contributions in respect of ~~their~~its share of the surplus. Under the Partners' ~~agreement~~Agreement any funding surplus must be dealt with so that the funding valuation becomes actuarially balanced. *In other words when there is a funding surplus over a certain range the "status quo" cannot be maintained, the surplus must be reduced by a combination of reductions in contributions, increases in benefits or withdrawals of surplus*. This is confirmed by the Partners' Agreement Section 57 that requires an actuarially balanced valuation to be prepared at least once every three years, allowing for a contingency reserve, combined with the FMP which sets out the framework for determining when a surplus or deficit outside of agreed upon ranges are met and action must be taken. While the Province might choose to accept an increase in member benefits rather than to reduce funding ~~at their~~, any such decision is at the Province's discretion~~,~~ since the OTF cannot force the Province to increase benefits instead of reducing contributions. In other words ~~the Province can avoid that their~~it is at the Province's discretion whether to address the actuarial balancing requirements by allowing its portion of the surplus ~~is~~to be utilized ~~only~~ through increased benefits. The OTF equally has the right to not agree to reduced contributions from the Province, but they do not have the right to force an inequitable sharing of the surplus.

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Therefore, the Province is entitled to negotiate their share of the JDBP ~~and take~~which may include taking contribution holidays in future negotiations and can effectively use their power in negotiations to benefit from the ABA. The joint partners do have the ability to renegotiate all aspects of the partners' agreement including the FMP. However all changes require the agreement of both parties and as such the Province can veto any changes to the agreement. Note that while the negotiations are based on funding surplus amounts rather than accounting surplus amounts, any differences would be captured in the mechanics of the calculation of the expected future benefit rather than precluding an ability to benefit from any of the accounting surplus.

Further, Section PS 3250 paragraph ~~PS 3250~~.055 indicates "The objective of the standard in Section PS 3250 paragraph ~~PS 3250~~.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Many generally accepted accounting frameworks use "expected" in a number of principles and is typically used in the probabilistic sense – something is expected when it is probable at some level, it does not equate to certainty. The Province has an expectation that they will benefit fully from the ABA by exercising their current rights under the plan arrangements to negotiate the use of current and future surpluses in the form of contribution holidays. This position is supported by the review of the constating documents and past history of negotiations that indicate:

1. The TPA 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). 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.
2. 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 (refer to Appendix G for a history of surplus utilization for OTPP). 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.
3. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right[12]), and the requirement to negotiate and agree (or in the absence

[12] The OTF Call Right is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising the government initiated Freeze period. Part of a previously agreed upon arrangement to ensure equitable sharing of the risks and rewards over the long term of the plan, it is not a general unilateral right to utilize future surpluses beyond the recovery of the specific funding shortfalls.

of agreement, arbitrate) presents the Sponsors with an equal opportunity to benefit from surplus utilization.

4. 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. Under the plan, contributions are generally borne equally by the Province and the employees. Employees benefit economically from both an increase in benefits and from a reduction of contributions. The Province benefits economically directly from a reduction in contributions. This makes it reasonable that at least some contribution reductions would be agreed to by the joint sponsors as a highly unequal weighting towards increases in benefits would not balance the interests of taxpayers and teachers therefore may be unlikely to be a reasonable outcome of “good faith” negotiations between the Province and the OTF.

   This is further supported by the historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses, should also be considered. As previously discussed in respect of conditional indexing, a decrease in benefits by the employees were offset by an increase in payments by the Province. Similarly as the sponsors agreed to restore indexation, this increase in benefits resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.~~9~~98B for the 2015 change, and $1.~~6~~68B for the 2014 change). This demonstrates that historically and over the long term an equitable sharing of the deficits and surpluses has resulted in changes in the Province’s contributions, even when there are decreases or increases to benefits for employees.

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, a mediator may be chosen by agreement of the ~~matter can be submitted to~~sponsors (section 77 of the Partners’ Agreement). If the sponsors do not accept the report of the mediator, an arbitration board will be appointed (section 84 of the Partners’ Agreement). The arbitration board would consist 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-

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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).

~~Further to Section PS 3250.052 discussion regarding entitlement to benefit PS 3250.059 provides further guidance on what this means in respect of an entitlement to withdraw surplus. "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal." PS 3250.59 is clear that expected future benefit available from surplus withdrawal can only be asserted where the government has a current legally enforceable right to withdraw assets from the Plan. Section PS 3250.59 introduces the concept of a legally enforceable right, however it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions. Had PSAB intended legal enforceability to be the test, they would have included that notion throughout the guidance (for example in paragraph .052), instead of only raising it in the context of a withdrawal of surplus.~~

Based on the above analysis, the Province believes that the uncertainties around how and when to utilize a surplus in the OTPP do not result in an inability or lack of entitlement to utilize the surplus in accordance with Section ~~PS~~ 3250.52.

Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250.53 to .58 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where actual realization ~~includes~~ of the benefit would be reflected in a reduction in future contributions. A valuation allowance is recorded against the ~~Pension Asset~~ pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as ~~that expected future benefit is~~ defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province calculated the expected future benefit as the sum of:

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

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

Each of these is discussed separately.

Through withdrawal of the surplus (Section PS 3250.056 (b~~)~~))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph ~~3250~~.059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

The TPA for OTPP does not ~~provide~~specify a method for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

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As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution~~, the~~. The Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

The Province's position is that there is no amount of expected future benefit included in respect of withdrawable plan surplus ~~as government does not have a legally enforceable right to the surplus. The OAG agrees with this position.~~ .

Through reducing future contributions (Section PS 3250 paragraph .056 (a))

PS 3250.56(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per PS 3250 paragraph.81 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the ~~Pension Asset~~pension asset value to be recorded in the accounts. For example, if the ~~Pension Asset~~pension asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the ~~Pension Asset~~pension asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. It is therefore relatively straightforward and is typically calculated based on the Province's share of the current service cost reported in the actuarial valuation taken into perpetuity unless there is evidence to indicate the workforce will significant diminish over time (for example a closed plan).

The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for judgment in the above calculation is in ~~the determination~~this second part of the calculation. Note that

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consistent with the calculation of the expected future ~~minimum~~accruals for service, no amounts are considered for employee contributions ~~required~~as these relate to the OTF's portion of the plan. The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (3250.56(a)). ~~be made by the government regardless of any surplus.~~ There is no further guidance in S 3250 as to how ~~this~~the calculation of minimum required contributions should be performed and what restrictions or parameters should be factored into this calculation. Typically for defined benefit plans minimum contributions include those that are required by the pension regulator to be made for funding. However, minimum contributions regardless of any surplus, may be required by plan text, legislation or other agreements with employees. For OTPP a key element of judgment is determining what contributions are required by the current plan arrangements "regardless of any surplus". The constating agreements for OTPP require that the parties negotiate every 3 years as a minimum, and when there is a funding surplus.

Determining the number of years of contributions to include should involve an assessment of the facts and circumstances of the plan and should consider uncertainty. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the contractual agreements between the Sponsors that provide for the sharing of risks and benefits and specifically in respect of assessing the minimum contributions required by the plan agreements the following:

- One view of minimum contributions might be that the agreed upon level of contributions are the minimum contributions until they are altered in the plan text. As this can only happen with agreement from OTF it cannot be assumed that changes will be made and therefore that the contribution formula as stated in the current agreements will continue in perpetuity. This view provides the most conservative view of minimum payments. However as the current contribution amounts are greater than the government's share of the annual current service cost for the existing workforce this indicates that continued contributions at this rate will result in ever increasing surpluses. Extrapolating the surpluses, at a certain point other requirements that are currently incorporated into the plan text, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan will apply to reduce the contributions. The effect of these caps on contributions would have to be estimated but cannot be ignored as they form part of the current contribution arrangements. Modelling could be performed to develop expectations as to when these CRA ~~limited~~limits could be expected to be reached assuming no changes in the contribution levels. As is the most conservative view (highest minimum contributions) the impact of this has been considered, as discussed below.
- An alternative view of the minimum contributions required by the plan is that there is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'. On this basis it could be argued that any agreed upon contribution levels are mandatory for only a three year period,

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after which the contributions must be renegotiated to stay the same, increase or decrease, such that the stated contribution level in the plan text constitute minimum payments for only three years. ~~This view might be overly aggressive in~~It should be noted that the plan text requires an actuarially balanced funding valuation, so to the extent that a funding deficit currently existed a contribution holiday (contributions lower than the annual cost of the plan) could not be negotiated. However because the funding situation at the time of future negotiations is not known it could be argued that no amount is a fixed "minimum contribution" in this context, because all of the contribution amount is subject to future changes in funding and negotiation by the joint sponsors.

- Other views of what the minimum contributions are would fall between these two views, such as that the current funding level is set to ensure that there is no funding deficit over a 11 year period and after that changes in contributions would be negotiated. This view has been used in calculating the actuarial calculation of the asset ceiling as noted in the table below.
- ~~The~~Another consideration might be the specific framework within the Funding Management Plan for OTPP ~~that~~which contemplates ~~specific~~specified funding zones and ~~when~~expectations regarding possible contribution reductions ~~will be discussed~~ by the sponsors. ~~Modelling could~~Informed stochastic modelling would be ~~performed~~necessary to ~~help~~ estimate when the different funding zones will be reached and probability of contribution reductions may be increased.
- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to use some of the funding surplus to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change~~,~~~~$~~, $1.~~98~~98B for the 2015 change, and $1.~~68~~68B for the 2014 change).

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (PS 2130 paragraph .03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in Section PS 2130 paragraph .13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

~~Actuarial reports were completed to~~As part of the 2015/16 Public Accounts audit, the Office of the Provincial Controller engaged external consultants to conduct asset ceiling tests to assess the

requirement for a valuation allowance~~.~~ against the $10.1 billion of net pension assets reported by the Province for OTPP . The results of those reports are summarized ~~here:~~in Table 1 below.

Table 1: Summary of Asset Ceiling Models performed for OTPP

Model Assumptions			**Expected Future Benefit or Asset Ceiling ($ Billions)**	**Results**
1. There is no minimum employer contribution under the plan/legislation that is required even if a surplus is present.			$44.6	There is no reduction in the expected future benefit (EFB) as at March 31, 2016.
~~Plan~~	~~Asset recorded by Province (in billions)~~	2. ~~Asset ceiling computed (in billions) and assumption re: years of contributions~~The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of the current funding report. Contribution requirements are $1.7B per year for 2015, 2016 and 2017,	$41.2	~~Number~~ ~~be made~~ ~~valuation~~ contribut the curre report an completed. EFB is reduced for 2 years by $
~~OTPP~~	~~$ 10.1~~	The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of contribution requirement (i.e. 11 years through 2026) not just for the period of the current funding report.~~$29.3 (based on 11 years of contributions noted in the funding~~	$29.3~~3~~	Uses a pe period) b special co The EFB a reduced by $15.3B.

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		~~report as the period additional contributions are~~ ~~3. required)~~		
4. The surplus is never used until the time it reaches the Income Tax Act (ITA) threshold. Once attained, the excess surplus is used at 50% for employees and 50% for the Province to reduce contributions in the following years.			$23.2	The ITA s… the end o… contribut… EFB is reduced by $21.4B at March 31, 2016
5. Every year, 50% of current year surplus is applied to improve member benefits and the remaining 50% of the current year surplus is retained and continues to accrue. Once the ITA threshold is attained, the excess surplus is used 50%-50% to reduce contributions by employees and the Province.			$12.9	The ITA surplus limit is reached at the end of 2041 leading to forced contribution reductions from 2042. EFB is reduced by minimum $37.7B at March 31, 2016.

Note: Models above made no assumption on any value of the surplus withdrawal.

~~The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (3250.56(a)). There is no guidance on the meaning of minimum contributions for purposes of this calculation in PS 3250. For purposes of the OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.~~

~~An important consideration in performing these asset ceiling calculations is how long contributions will be required to be made.~~ Under the Partners' Agreement, the parties are mandated to negotiate benefits and contributions every three years as a minimum and if agreement is not reached, it is reasonable to expect that a change in contributions might occur rather than the 'status quo' being retained.

For purposes of the OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

~~However, in~~In addition to the above calculations, ~~we have considered~~ the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan~~.~~ should also be considered. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that

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no valuation allowance is required. ~~We would be happy to share this analysis with you, in addition to the actuarial reports we have already provided.~~

~~Determining~~The determination of the minimum contribution levels required ~~to calculated~~as input to the calculation of the expected future benefit involves significant judgements, estimation and assumptions about future funding surplus levels ~~that~~. These judgements, estimates and assumptions should be made on a consistent basis with ~~the~~ best estimates used in developing the accrued benefit obligations and plan asset amounts. ~~However, the fact that judgements, estimates and assumptions~~ Regardless of the need to ~~be made in respect of calculated expected future benefit should not~~ apply judgements, estimates and assumptions for the calculation, this does not imply that no asset can be recognized or that it cannot be reliably ~~measureable. Pension~~measured. In fact, pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". ~~Expected~~From the Province's perspective, 'expected' does not equate to ~~certainty~~'certainty'.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (3250.42) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (3250.41). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. 3250.57 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province ~~of Ontario~~ has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on Plan Assets, which is one of the acceptable references suggested on PS 3250.44.

The OAG and the Government differ regarding whether it needs to be "expected" that the Government will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in Section PS3250 paragraph .059. The Government considers that it needs to be expected that future economic benefits are to be obtained as reflected in the definition of an asset in Section PS 1000 and as reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to use a plan surplus.

Other guidance in the PSA Handbook on measurement

~~Furthermore~~ MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe would be a useful addition to the current year financial statements. Section PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.*
>
> *.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.*

~~We acknowledge that the~~The estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is ~~permissible~~an acceptable alternative under PSAB and consistent with rates followed by other senior Canadian governments. Historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets ~~on~~reported in the ~~Province's books.~~Public Accounts.

Impact of valuation allowance

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The ~~impact~~current AG's view challenges previous interpretations of the Provincial Controller and former Auditor Generals regarding the interpretation and application of PS 3250 to those JDBPs where the government is a joint sponsor. The impact of the OAG's view is that no pension accounting surplus ~~could ever~~should be recognized in the Province's Public Accounts for JDBPs until the joint sponsor agrees to a change in the plan text for the Province to provide for unilateral authority to access surplus or reduce future contributions to enters into an agreement by year-end enabling the government to take a contribution holiday. ~~Any~~In the absence of meeting either the criteria set out by the AG, any ABA would therefore be fully provided for through a valuation allowance~~. The impact of this in the~~, impacting each year's statement of operations ~~can be~~by the amount by which the asset would otherwise increase in value. These results are counterintuitive with pension expense being higher in years ~~when the impact of greater~~in which increased funding ~~or greater investments returns is recorded and a gain (income) in years when the impact of an increase in expected pension benefits or lower than expected~~is made and also higher when poor investment returns ~~is recorded. **[NTD – statements to be supplement by the visual aid requested by the Minister]**~~create actuarial losses that have not yet been amortized into the statement of operations. These examples are illustrated in Appendix C.

For information purposes, refer to Appendix ~~D~~H for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS. Of particular note is the impact in 2008 when the deficit would have be lower by $3 billion in a year when pension asset values fell significantly because of the financial crisis.

~~Comparison~~Comparability of Ontario accounting for JDBPs to other ~~provinces~~Provinces

Commented [NP2]: Section should focus on JDBPs in other jurisdictions. Pauline/Jim to update.

~~For your information, included~~Included in Appendix ~~C~~I is ~~the~~a legal opinion prepared by lawyers, Koskie Minsky, comparing access to the pension surplus of OTPP relative to ~~pension plans~~JDBPs in British Columbia. The Province of British Columbia does not ~~include~~report a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

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Quebec, Nova Scotia, Manitoba and New Brunswick also have pension plans that are in a net accrued benefit asset position before valuation allowance.

Commented [NP3]: Not JDBPs?

In New Brunswick, the target benefit pension plans are governed by an Agreement and Declaration of Trust which restricts the Province's access to the plan assets. These target benefit plans targets

retirement benefits as opposed to guaranteeing it. Two of the four target benefit plans are in net asset position, where a full allowance is taken against the net pension asset.

Conclusion on measurement

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~~There~~As discussed, there is significant professional judgement and estimation ~~and judgements to be applied~~ in determining how to measure the valuation allowance under Section PS 3250, including the determination of the minimum contributions required by the current plan arrangements. ~~The Province concluded~~It is the Province's position that the attributes of the joint defined benefit plan arrangements for the OTPP entitle ~~them~~the Province to access ~~to their~~its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surplus through reduced contributions.

The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of those models to date no valuation allowance appears to be required and the OTPP pension assets should continue to be recorded on the books of the Province.

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Appendix A– Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the ~~PSA Handbook – FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210~~various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
~~**Guidance in FINANCIAL STATEMENT CONCEPTS, Section PS 1000**~~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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the Sponsors to the OTPP have the authority to utilize

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Commented [LD4]: JIM Can you also insert references to Sections 10 and section 57.
Also to Section 58 to 60 that are relevant.
Section 19 requires a valuation to be prepared every three years. This is also important.

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ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years to comply with the PBA.

The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

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

~~.36 Assets have three essential characteristics:~~

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

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

~~(c) the transaction or event giving rise to the public sector entity's control has already occurred.~~ ~~[Former paragraph PS 1000.36 retained in Archived Pronouncements.]~~

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

~~(a) no future economic benefit;~~

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

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

~~(paragraph PS 1000.38 deleted) [Former paragraph PS 1000.38 retained in Archived Pronouncements.]~~

~~.39 **Financial assets** are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations.~~

~~.40 A financial asset is any asset that is:~~

~~(a) cash;~~

~~(b) a realizable asset that is convertible to cash;~~

~~(c) a contractual right to receive cash or another financial asset from another party;~~

~~(d) a contractual right to exchange financial instruments with another party under conditions that are potentially favourable to the government;~~

~~(e) an equity instrument of another entity;~~

~~(f) an investment in a government business enterprise or government business partnership;~~

~~(g) a financial claim on an outside organization or individual; or~~

~~(h) an inventory or item for sale that meets the criteria in FINANCIAL STATEMENT PRESENTATION,~~

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paragraph PS 1201.055. [Former paragraph PS 1000.40 retained in Archived Pronouncements.]

.41 Non-financial assets include tangible capital assets, and other assets such as prepaid expenses and inventories of supplies.

.42 **Non-financial assets** are acquired, constructed or developed assets that do not normally provide resources to discharge existing liabilities, but instead:

(a) are normally employed to deliver government services;

(b) may be consumed in the normal course of operations; and

(c) are not for sale in the normal course of operations.

RECOGNITION

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

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

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

.55 The recognition criteria are as follows:

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

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

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

.57 Purchased natural resources and Crown lands are recognized in government financial statements.

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However, when natural resources and Crown lands have been inherited by the government in right of the Crown and have not been purchased, they are not given accounting recognition as assets in government financial statements. These items are not recognized as assets because the costs, benefits and economic value of such items cannot be reasonably and verifiably quantified using existing methods. Similarly, art and historic treasures are also not recognized as assets.

.58 In the absence of appropriate public sector recognition and measurement criteria for intangibles, all intangibles, including those that have been purchased, developed, constructed or inherited in right of the Crown, are not recognized as assets in government financial statements. The intangible often called "human capital" that embodies the talent or intellectual capital of government employees is not recognized as an asset under existing accounting principles.

.59 Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting. The accrual basis of accounting recognizes the effect of transactions and events in the period in which the transactions and events occur, regardless of whether there has been a receipt or payment of cash or its equivalent. Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied. Accrual accounting recognizes an asset until the future economic benefit underlying the asset is partly or wholly used or lost.

MEASUREMENT

.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

.61 Present value is the discounted amount of future cash flows expected to be received from an asset or required to settle a liability. Present value is not a basis of measurement, but a valuation technique that may be used within historical cost based or current value models. This technique is used in the government reporting model, for example, to estimate the cost of retirement benefits, when determining the estimated total expenditure for closure and post closure care of a solid waste landfill site, and when determining the "grant portion" of concessionary loans and portfolio investments.

.62 Government financial statements are prepared on the basis that recognized economic resources used up are measured in financial terms with no adjustments made for the effect of a change in the general purchasing power of the currency during the period. Although a government's performance in the management of its service potential 2 is generally a focus more appropriate to the nature and objectives of government, it cannot entirely be measured in financial terms.

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~~2. Service potential embodies both the quality of service provided and the efficiency with which it is provided.~~

~~.63 Financial statements are prepared on the assumption that the government is a going concern, meaning it will continue in operation, and will be able to realize assets and discharge liabilities and meet its statutory obligations in the normal course of operations for the foreseeable future.~~ 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

In addition to the clauses identified above, the Partners' Agreement has an appendix called the Funding Management Policy which sets out the Sponsors' responsibilities in making funding decisions and

surplus allocation regarding the Plan.

~~**Guidance in ASSETS, Section PS 3210**~~Funding Management Policy (FMP)

~~Economic resources~~

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

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

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

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

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

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

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

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

~~.09 Economic resources can be:~~

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

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

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

~~Future economic benefits~~

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

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

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

~~.14 The future economic benefits may also take the form of a capacity to reduce cash outflows. For~~

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~~example, this may be the case when betterment of a tangible capital asset reduces the cost of providing goods and services.~~

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

~~Control~~

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

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

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

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

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

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

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

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

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

~~.22 Control of an economic resource and of access to the future economic benefits are essential characteristics of an asset, whereas possession or ownership is not. For example, a public sector entity may control the economic resource and access to the future economic benefits through a capital lease arrangement yet not own the economic resource.~~

~~.23 A public sector entity's ability to regulate an economic resource does not, in and of itself, constitute control of an asset. A public sector entity may establish the regulatory environment in an industry or sector within which organizations operate and impose conditions or sanctions on their operations. For example, a pollution control authority may have the ability to close down the operations~~

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~~of entities that are not complying with environmental regulations. However, this power does not constitute control because the pollution control authority's interest extends only to the regulatory use of the economic resources and does not include the ability to control access to the future economic benefits.~~

~~.24 A public sector entity may act as trustee when it administers trusts on behalf of the beneficiaries specified in the agreement or statute. As trustee, the public sector entity merely administers the assets, following the terms and conditions set out in the agreement. It does not control the asset because it does not have access to the future economic benefits. Those benefits flow to the beneficiaries.~~The FMP is an appendix to the Partners' Agreement that speaks to how the Plan should be funded and how surpluses should be utilized by both parties. The protocol for the use of a surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP.

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

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

If the Plan gets to either the temporary improvement zone or the permanent improvement zone,

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

Section 8.01 of the FMP provides the following:
Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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Appendix B – Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement 2 between the government and a party or parties outside of the government reporting entity 2 that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the	Consistent in concept with the definition of a GP focusing on investments in the partnership and the

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		non-government sponsor;	definition of a JDBP focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	~~government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]~~		

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~~In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.~~

~~While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.~~

~~There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.~~

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Appendix C– Impact of a Valuation Allowance on Pension Assets

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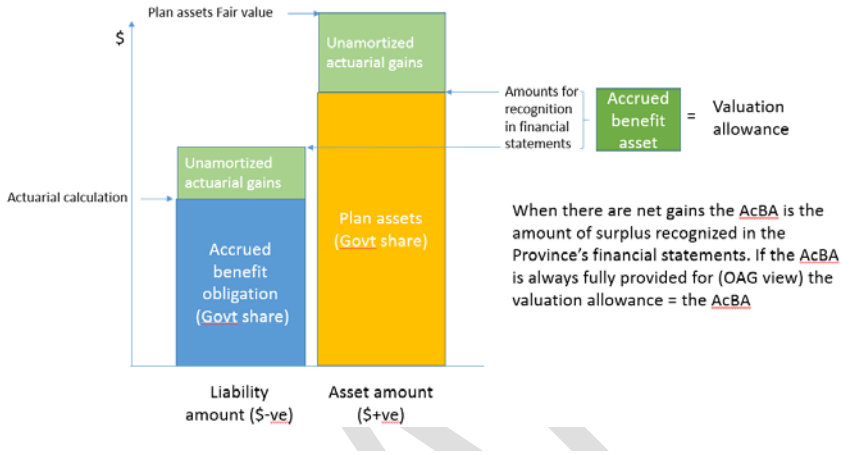
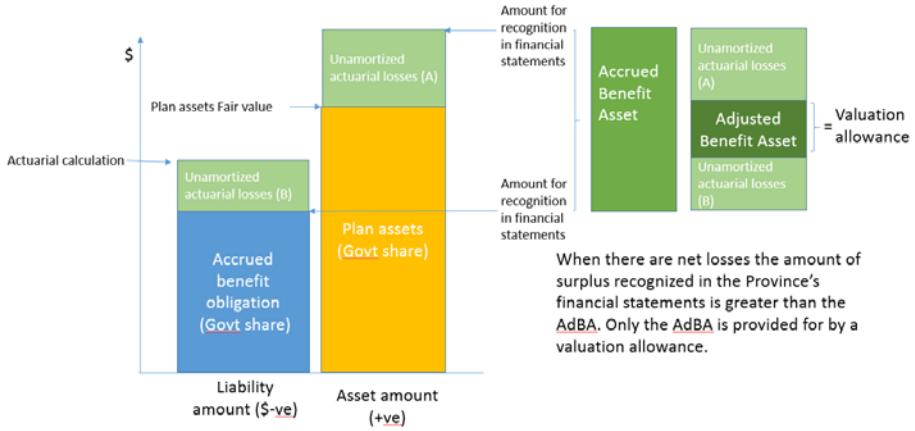
An Accrued Benefit Asset (AcBA) occurs when there is a plan surplus, including the effect of net unamortized experience gains or losses. OTPP currently has net unamortized experience gains.
Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation



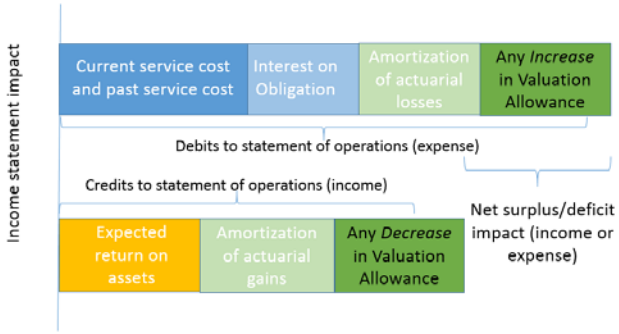
An Adjusted Benefit Asset (AdBA) is required when there are unamortized losses



Components of Expense

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

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



Changes in the Accrued Benefit Asset

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

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

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

Appendix D - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, Section PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the definition of a JDBP

			focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership.	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former Section PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

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Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	5.95%	LT return on plan assets
Alberta				
Teachers' Post-1992 Pension Plan	7.00%	LT return on plan assets	7.25%	LT return on plan assets
Universities Academic Pension Plan	6.10%	LT return on plan assets	6.25%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)				
Local Authorities Pension Plan	5.80%	LT return on plan assets	5.80%	LT return on plan assets
Public Service Pension Plan	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Management Employees Pension Plan	6.40%	LT return on plan assets	6.40%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.75%	LT return on plan assets	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Special Forces Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan				
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.80%	LT return on plan assets	6.80%	LT return on plan assets
British Columbia				
Public Service Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec				
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	6.40%	LT return on plan assets less inflation
Newfoundland				
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets
Nova Scotia				
Nova Scotia Public Service Superannuation Plan (PSSP)	6.75%	LT return on plan assets	6.35%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	6.40%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba				
Civil Service Superannuation Plan	6.00%	LT return on plan assets	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.50%	LT return on plan assets	6.25%	LT return on plan assets

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Appendix F – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension -Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

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Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared- on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation -to -the -MPP, -to utilize ongoing -surpluses to -reduce- contributions or improve Plan Member benefits.

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In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[13] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion- of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[13] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

We trust that these comments have been of assistance to you. Should you have any questions in regard to them, please do not hesitate to contact the undersigned.

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Appendix ~~D~~ ~~G~~- Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.

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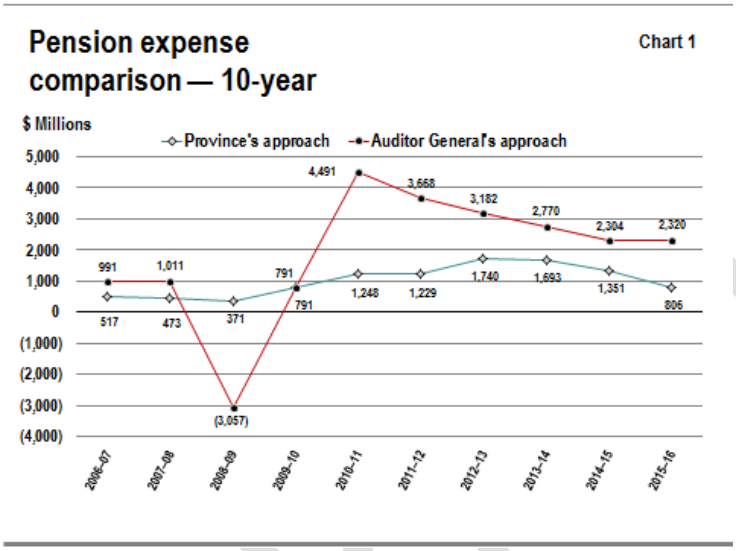
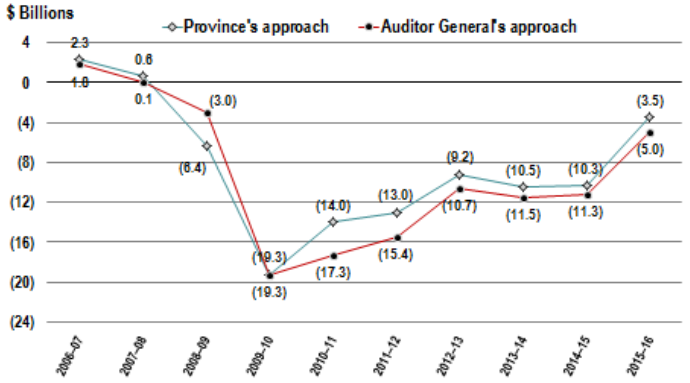


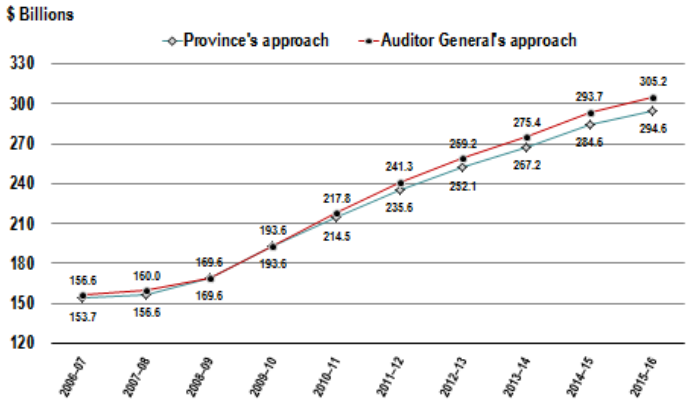
Surplus/(deficit) comparison — 10-year

Chart 2

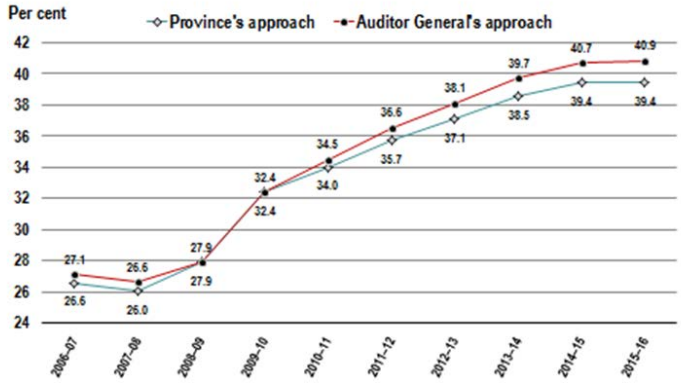


Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year Chart 4



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Appendix ~~E~~H – History of Surplus Utilization for OTPP

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The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			reduce the value of remaining special payments	
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		

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).

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Appendix I – Summary of different valuation methodologies for pension valuations

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The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits and pension obligations.	Measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered.
Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market -related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate.	In measuring a pension obligation amount, the defined benefit obligation amount determined by the	Not specified. However two methods are specifically acknowledged – a)

	For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.[14] The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

[14] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

Appendix A – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. ~~By contrast, section~~ Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the ~~-~~Partners ~~-~~Agreement ~~-~~sets out the responsibilities~~-~~ of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing ~~-~~surpluses ~~-~~either to improve ~~-~~benefits or reduce ~~-~~contributions. Only the Sponsors to the OTPP have the authority to utilize ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years

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Also to Section 58 to 60 that are relevant.
Section 19 requires a valuation to be prepared every three years.
This is also important.

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to comply with the PBA.

The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

In addition to the clauses identified above, the Partners' Agreement has an appendix called the Funding

Management Policy which sets out the Sponsors' responsibilities in making funding decisions and surplus allocation regarding the Plan.

Funding Management Policy (FMP)

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

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

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

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Section 8.01 of the FMP provides the following:

Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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

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2003 (from 2003 onwards the plan was mostly in deficit, with surpluses used to restore foregone escalated adjustments for members).

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Appendix ~~F—~~C – Impact of a Valuation Allowance on Pension ~~liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years~~Assets

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	**2000-01**	**2001-02**	**2002-03**	**2003-04**	**2004-05**	**2005-06**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	**2006-07**	**2007-08**	**2008-09**	**2009-10**	**2010-11**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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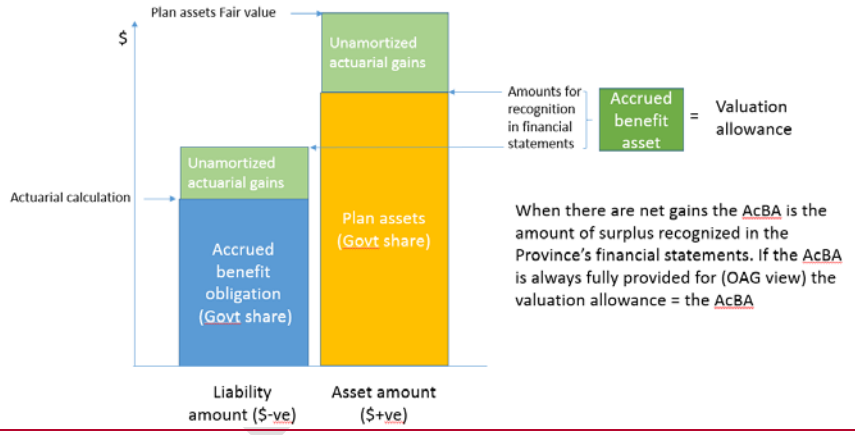
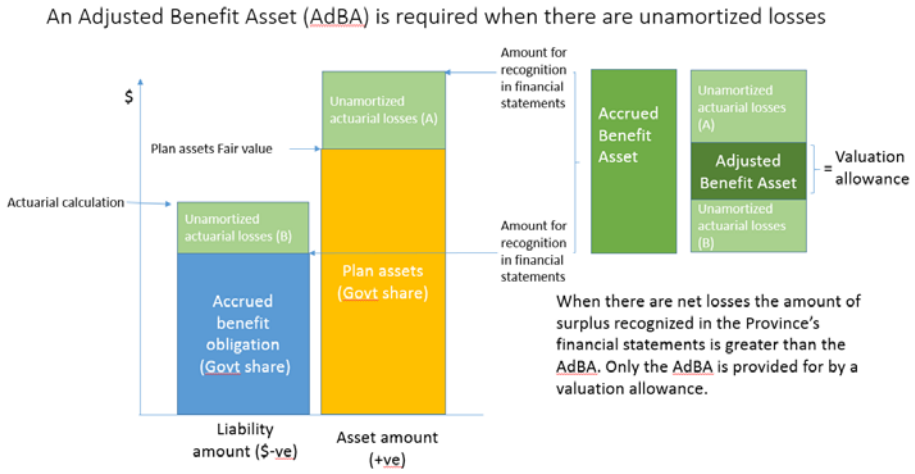
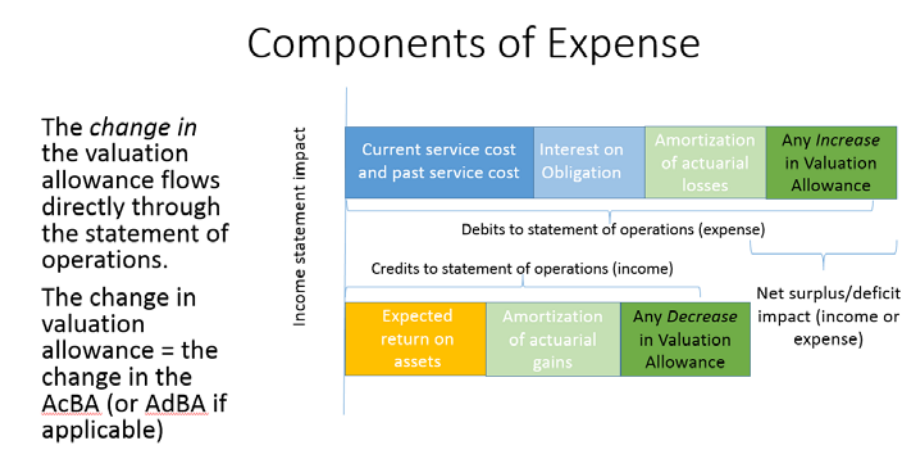
Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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



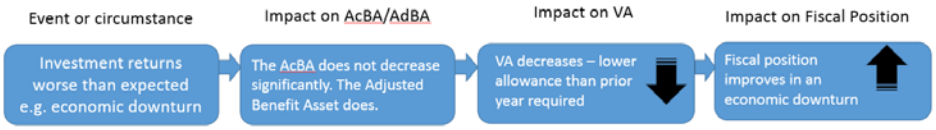
When there are net gains the AcBA is the amount of surplus recognized in the Province's financial statements. If the AcBA is always fully provided for (OAG view) the valuation allowance = the AcBA


An Adjusted Benefit Asset (AdBA) is required when there are unamortized losses
$
Plan assets Fair value
Actuarial calculation
Unamortized actuarial losses (A)
Unamortized actuarial losses (B)
Accrued benefit obligation (Govt share)
Plan assets (Govt share)
Liability amount ($-ve)
Asset amount (+ve)
Amount for recognition in financial statements
Amount for recognition in financial statements
Accrued Benefit Asset
Unamortized actuarial losses (A)
Adjusted Benefit Asset
Unamortized actuarial losses (B)
= Valuation allowance
When there are net losses the amount of surplus recognized in the Province's financial statements is greater than the AdBA. Only the AdBA is provided for by a valuation allowance.


Components of Expense
The change in the valuation allowance flows directly through the statement of operations.
The change in valuation allowance = the change in the AcBA (or AdBA if applicable)
Income statement impact
Current service cost and past service cost
Interest on Obligation
Amortization of actuarial losses
Any Increase in Valuation Allowance
Debits to statement of operations (expense)
Credits to statement of operations (income)
Net surplus/deficit impact (income or expense)
Expected return on assets
Amortization of actuarial gains
Any Decrease in Valuation Allowance

Changes in the Accrued Benefit Asset

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



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

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

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

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

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

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

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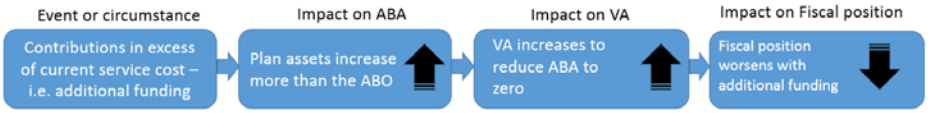
Changes in the Accrued Benefit Asset

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



2015-2016 example:
Contributions of $1,812M exceeded other elements of pension expense by $1,514M

2015-2016 example:
Additional contributions increase plan assets. AcBA increases by $1,514M

2015-2016 example:
AcBA increase of $1,514M results in an increase to the VA of $1,514M

2015-2016 example:
Deficit increases by $1,514M.

The cash paid for contributions has not resulted in an asset and so is an expense, despite the funding position of the Province's share of the plan has been improved by the additional contributions.

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

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Changes in the Accrued Benefit Asset

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

Event or circumstance	Impact on AcBA/AdBA	Impact on VA	Impact on Fiscal Position
Investment returns worse than expected e.g. economic downturn	The AcBA does not decrease significantly. The Adjusted Benefit Asset does.	VA decreases – lower allowance than prior year required	Fiscal position improves in an economic downturn
Plan assets fair values significantly lower in one year. Assuming no net amortized gains/losses in prior year this would create net *unamortized losses* as the use of market related values means the changes in plan assets are smoothed over 5 years.	The AcBA is based on the higher, smoothed value of plan assets and does not change significantly. However the actuarial losses are subtracted from the AcBA to calculate an AdBA, which is smaller than the AcBA.	Prior year allowance was based on AcBA (no net amortized actuarial losses). Current year is based on AdBA because there are unamortized actuarial losses. The AdBA is smaller than the AcBA because of the increase in unamortized losses. Therefore the VA is reduced correspondingly.	Fiscal position will be improved as a reduction in the VA results in a gain in the income statement in that year. The increased actuarial losses would only impact the statement of operations in future years. A similar impact would have been noted in 2008 if the OAG's position was reflected in the financial statements for that year.

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

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Appendix D – Summary of different valuation methodologies for pension valuations

Commented [NP9]: Request sent Oct 28 to ISPPD requesting to review details and confirm.

The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

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Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits and pension obligations.	Measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered.
Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market -related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate.	In measuring a pension obligation amount, the defined benefit obligation amount determined by the	Not specified. However two methods are specifically acknowledged – a)

	For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.15 The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

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Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

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[15] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	ON 1	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	ON 2	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	ON 3	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	ON 4	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	ON 5	5.95%	LT return on plan assets
Alberta					
Teachers' Post-1992 Pension Plan	6.80%	LT return on plan assets	AB 1	7.00%	LT return on plan assets
Universities Academic Pension Plan	6.00%	LT return on plan assets	AB 2	5.95%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)					
Local Authorities Pension Plan	5.60%	LT return on plan assets	AB 3	5.60%	LT return on plan assets
Public Service Pension Plan	6.00%	LT return on plan assets	AB 4	6.00%	LT return on plan assets
Management Employees Pension Plan	6.10%	LT return on plan assets	AB 5	6.10%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.40%	LT return on plan assets	AB 6	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.00%	LT return on plan assets	AB 7	6.00%	LT return on plan assets
Special Forces Pension Plan	5.90%	LT return on plan assets	AB 8	5.90%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan					
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.50%	LT return on plan assets	SK 1	6.50%	LT return on plan assets
British Columbia					
Public Service Pension Plan	6.50%	LT return on plan assets	BC 1	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	BC 2	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	BC 3	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	BC 4	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec					
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	QC 1	6.40%	LT return on plan assets less inflation
Newfoundland					
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	NF 1	5.80%	LT return on plan assets
Nova Scotia					
Nova Scotia Public Service Superannuation Plan (PSSP)	6.70%	LT return on plan assets	NS 1	6.15%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	NS 2	6.25%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba					
Civil Service Superannuation Plan	6.00%	LT return on plan assets	MB 1	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.25%	LT return on plan assets	MB 2	6.00%	LT return on plan assets

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Appendix F - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement 2 between the government and a party or parties outside of the government reporting entity 3 that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the definition of a JDBP

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			focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership.	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

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In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	5.95%	LT return on plan assets
Alberta				
Teachers' Post-1992 Pension Plan	7.00%	LT return on plan assets	7.25%	LT return on plan assets
Universities Academic Pension Plan	6.10%	LT return on plan assets	6.25%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)				
Local Authorities Pension Plan	5.80%	LT return on plan assets	5.80%	LT return on plan assets
Public Service Pension Plan	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Management Employees Pension Plan	6.40%	LT return on plan assets	6.40%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.75%	LT return on plan assets	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Special Forces Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan				
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.80%	LT return on plan assets	6.80%	LT return on plan assets
British Columbia				
Public Service Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec				
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	6.40%	LT return on plan assets less inflation
Newfoundland				
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets
Nova Scotia				
Nova Scotia Public Service Superannuation Plan (PSSP)	6.75%	LT return on plan assets	6.35%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	6.40%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba				
Civil Service Superannuation Plan	6.00%	LT return on plan assets	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.50%	LT return on plan assets	6.25%	LT return on plan assets

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			special payments	
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		

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).

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~~Appendix H – Summary of different valuation methodologies for pension valuations~~

Appendix H - Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.

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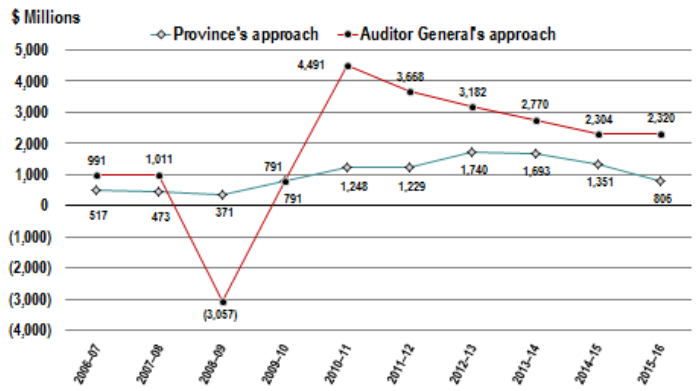
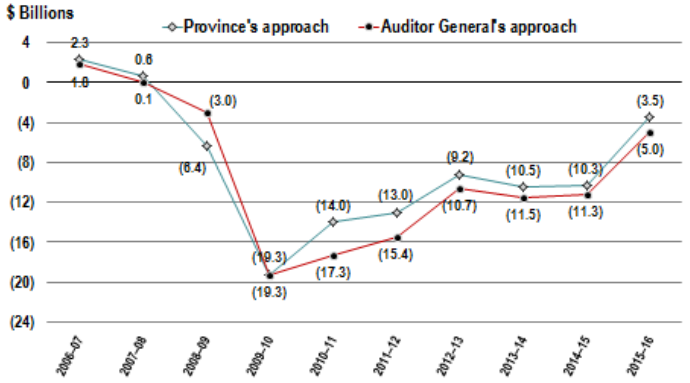


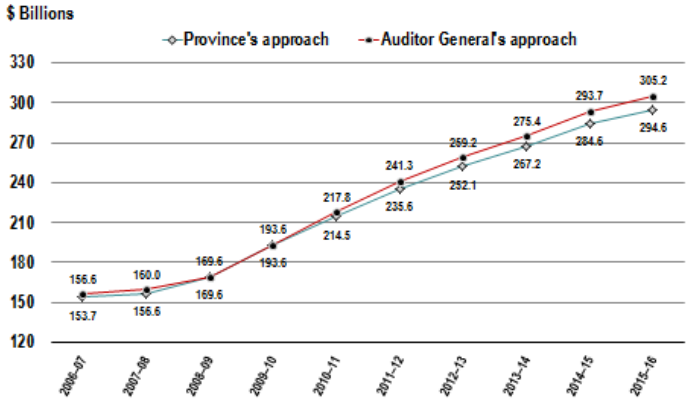
Surplus/(deficit) comparison — 10-year

Chart 2

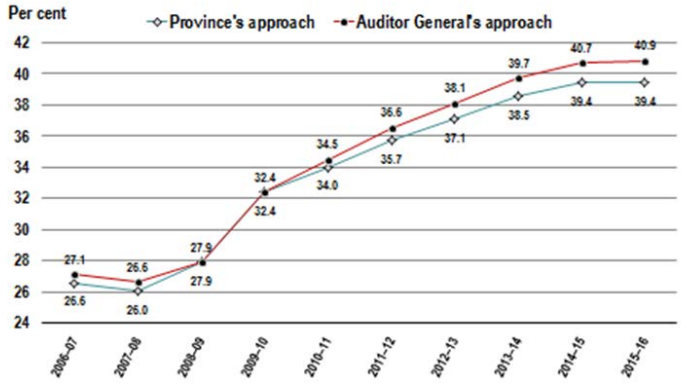


Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year Chart 4



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Appendix I – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

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Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

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In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[16] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[16] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

~~The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.~~

~~Assumption/ methodology~~	~~Funding valuation (Going concern basis)~~	~~Accounting Part IV – (OTPP Financial statements)~~	~~Accounting PSAS – (Province Financial statements)~~
~~Purpose~~	~~To inform plan sponsors of the~~	~~Financial statements [of~~	~~Measure and report the~~

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	amount that needs to be contributed each year to adequately fund benefits	pension plans] provide information about the pension plan including net assets available for benefits and pension obligations.	obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered.
Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market-related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate. For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the	In measuring a pension obligation amount, the defined benefit obligation amount determined by the plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in	Not specified. However two methods are specifically acknowledged – a) discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.[17]

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[17] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration

	yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high-quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

Draft Pension Asset Position Paper Oct 28 clean to cv.pdf

Position paper for Ontario Teachers' Pension Plan

Preamble

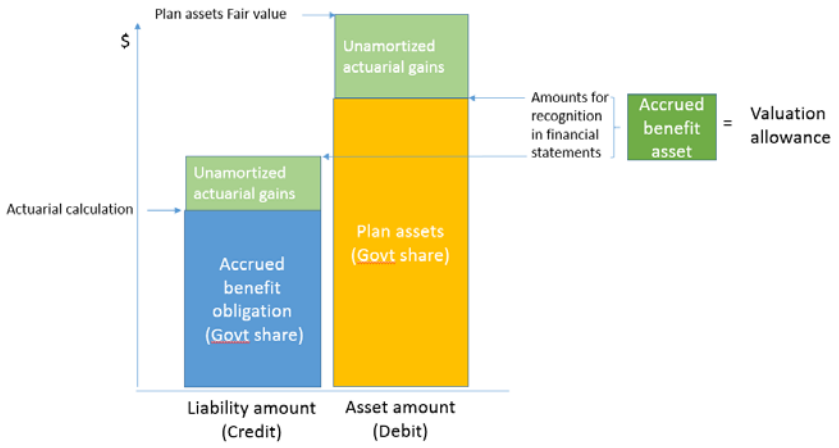
This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP. This position paper addresses the analysis for OTPP. A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

As described in PSAS, an accrued benefit asset (pension asset) arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. An Accrued Benefit Asset (AcBA) includes the effect of net unamortized experience gains or losses. Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation. OTPP currently has net unamortized experience gains. The following illustration reflects the compilation of the net pension asset (accrued benefit asset) reported on the Province's books for the OTPP.



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LD – Pauline/Jim – please confirm that details are relevant to OTPP situation.

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It is important to note that contributions to the plan are based on funding objectives of the plan. In contrast, Benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (plan surplus for accounting purposes) in OTPP is an asset to the Province and it is appropriate to reflect it in the financial results in accordance with PSAS. The Province has also concluded that no valuation allowance under PSAS is required against the asset as at March 31, 2016.

The OAG disagrees with this position. The OAG has indicated that the Province does not have the legally enforceable right to unilaterally access the assets of the plan, and as such that the Province does not control the assets which the OAG interprets PSAS as requiring. Further, the OAG considers the lack of an enforceable agreement at year-end with the Ontario Teachers' Federation (OTF) dictating lower contributions in the future as requiring that a full asset valuation allowance be taken against the asset under PSAS.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. RETIREMENT BENEFITS, Section PS 3250 of the PSA Handbook addresses the accounting of obligations for employee retirement benefits in government financial statements. Since 2001, there have been no consequential changes to Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years. The pension liability (asset) and expense reported by the Province of Ontario for OTPP over the period is reflected in Appendix F. Unqualified audit reports have been received for each of the years from the OAG on the Public Accounts. The pension accounting initially adopted by the Province for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals for the prior years.

In light of the contrasting views on interpretation of PS 3250 to the Province's jointly sponsored pension plans, a regulation was necessary to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The regulation is time-limited and legislates the accounting for pension assets of its two jointly-sponsored pension plans (OTPP and OPSEUPP) for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The change in accounting treatment for 2015-16 resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the 2015-16 annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to reflect the Auditor

General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1. The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the OTF (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners' Agreement (FMP);
f) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
a. It provides defined benefits.
b. The defined benefits are contributory benefits.
c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA 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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5] This clause has been interpreted as a short term solvency protection clause, rather than a clause that transfers substantive residual risk to the Province, as the rest of the arrangement is structured such that the risk of these payments is minimal and the risks of the long term funding of the plan must still be equitably shared. The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (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, 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 inception of the plan in 1917). [7] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).
[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).
[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf As noted above, for the period from January l, 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%/11.20% 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.

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Joint governance and cost sharing form two of the core features of the OTPP. Consistent with the equal sharing of risk permitted under a JSPP, there is a requirement for decisions relating to plan design and plan amendments to be made jointly by the Sponsors. In this regard, the Partner's Agreement requires the Sponsors to negotiate and agree upon decisions relating to surplus or deficit utilization, which currently is outlined in the FMP. [8] The FMP indicates that deficits (or surpluses) may be addressed through increases (decreases) to the contribution rates, lowering (increasing) the amount of indexation and/or other decreases (increases) in benefits. While not binding upon the Sponsors, as the Sponsors can change the FMP at any time, any changes are required to have the mutual consent of both Sponsors. Accordingly, the Sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix B. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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).

[8] See, for example, Section 3.09 and 3.11 of the FMP.

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> 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 funding surpluses that may arise under the plan.

4. Negotiations on the use of the surplus occur as specified in the Partners' Agreement. The Partner's Agreement requires that any actuarial funding valuation submitted to the pension regulators must be "actuarially balanced" (Section 57 of the Partners' Agreement). This must occur at least once every three years, but can occur every year if the partners agree. If a preliminary funding valuation shows a funding surplus or deficit then the joint sponsors must negotiate how this surplus or deficit is to be resolved prior to filing the funding valuation.

Accounting for OTPP by the Province

Since fiscal year 2001-2002, the Province has recorded a pension asset for OTPP on the Statement of Financial Position. A pension asset has arisen because the government's share (50%) of the total contributions to OTPP plus recognized investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense (see illustrative examples in Appendix J). The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

With regards to any comparisons between surplus or deficit amounts reported in the Province's financial statements verses the OTPP's financial statements or funding reports, it is important to acknowledge the different objectives of funding and accounting for a pension plan which are also explicitly addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial*

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> *valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.*

Section PS 3250 paragraph .051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: "Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…"

OTPP's most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website. The Province's relative portion of this surplus would be $6.6 billion. The OTPP's public financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015, for which the Province's portion would be a deficit of $900 million. The following background helps to clarify the reasons for these different results. OTPP's financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook ("Part IV"), which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the net surplus or deficit for funding purposes.

Accounting for employee future benefits requires the use of assumptions and methodologies to calculate both the obligation incurred to date and the value of the assets already set aside to meet those obligations. Accounting frameworks differ in standards that must be applied in determining appropriate assumptions and methodologies. Further, the assumptions and methodologies used in developing a "funding valuation" on a going concern basis may also differ from those required by accounting standards. These differences result in a number of different valuations for the same plan, depending on the purpose of the valuation and can be affected by certain choices made between acceptable options within each framework. A summary of the main differences between the methodologies used to calculate a going concern funding valuation, OTPP's accounting valuation and the Province's accounting valuation is shown in Appendix D.

Specifically, the discount rate used to value the obligations of the plan has a significant impact on the overall position of the plan. A lower discount rate results in a higher liability and a higher discount rate results in a lower liability, all else being equal. Put another way, a higher estimate of the time-value of money makes the promises made today that will be paid out in the future cheaper. OTPP uses a discount rate based on corporate/government bond rates in its financial statements, as permitted by Part IV. The Province uses a discount rate based on the expected asset return, as permitted by PSAS. The rationale for using a corporate or government bond approach is that a pension promise is akin to a bond as it is a promise to pay a series of cash flows in the future regardless of what the asset returns actually are (which could be higher or lower than expected). The rationale for using an asset return approach is that it represents the amount of contributions that, combined with investment returns, should be sufficient to pay the promised benefits, particularly as pension plans will often invest in higher risk/higher return assets then simple corporate bonds. Both a discount rate based on the expected asset return and one based on corporate/government bonds are "best estimate" rates; they must both be based on management's best estimate of the applicable discount rate. In both cases the estimates must be supportable. The difference results not from one being more "right" or "wrong" relative to the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.

Typically the funding discount rate used for the funding valuation falls between the bond discount rate and the expected asset return, but it differs in that it does not purport to be the "best estimate" of the discount rate, rather it is designed to indicate the contributions that are required to fund the promised benefits with an additional conservative margin for adverse deviations. Note that over the long term the difference between funding valuations and accounting valuations would diminish as the impact of the discount rate unwinds and the asset valuation methods converge.

In practice, the discount rates used in the financial statements of government sponsored and joint defined benefit pension plans prepared under Part IV of the CPA Canada Handbook (Section 4600) use diverse methodologies. For example, in Alberta there are seven plans which prepare their financial statements under Part IV with reference to IFRS (same framework as OTPP). Of these none use a government bond discount rate and all use a discount rate calculated with some reference to a rate of return on invested assets, which may include factors for expenses, diversification and rebalancing. The analysis of a number of government sponsored plans is included as Appendix E. The analysis demonstrates that a significant number of government sponsored plans use a discount rate aligned to an asset investment return rather than a bond discount rate. OTPP is actually in the minority of plans that choose to use the rate required by IFRS, resulting in a lower discount rate and higher liability for financial reporting purposes.

The above analysis explains how different discount rates impact the net surplus/deficit reported on OTPP's financial statements, OTPP funding reports and the Province's financial statements. The fact that OTPP reports a deficit on its financial statements, or that the 50% of the net surplus reported by OTPP for funding purposes is lower than the surplus reported on the government's financial statements

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under PSAB standards is of no consequence or relevance to the pension asset amount or pension expense reported by the Province for OTPP.

To further clarify, that there is a deficit reported in the OTPP financial statements while the Province of Ontario calculates a surplus under PSAS requirements does not mean that there is no accounting surplus and therefore no reportable asset for the Province. In fact, if the OTPP had chosen (as an acceptable accounting policy choice) to use a discount rate more consistent with its counterparts in other jurisdictions (see Appendix E) such as a discount rate based on an asset return which would be closer to that used by the Province, it would eliminate much of the existing differences between the reported net surplus/deficit amounts between the OTPP statements and the Province's share of OTPP reported for accounting purposes in the Public Accounts.

Sufficiency of PS 3250 in assessing appropriate accounting for pension assets

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150 prescribes that, in developing and applying accounting policies, all primary sources of GAAP should be applied (Section PS 1150 paragraph .04). Primary sources of GAAP are Sections PS 1201-PS 3510, Public Sector Guidelines and appendices and illustrative material to those pronouncements. Only when there are no primary sources of GAAP that relate to the transactions or events under consideration, or more specific guidance is needed (Section PS 1150 paragraph .05), does an entity consider other primary sources of GAAP dealing with similar issues and also the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 (issued January 2003). Section PS 1000 is not, however, a "primary source of GAAP" under the PSA Handbook.

The primary sources of GAAP specific to the accounting for pension assets is RETIREMENT BENEFITS, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, Section PS 3250 which was based on Accounting Statement No. 5).

Other primary sources of GAAP that deal with similar issues might also be considered where additional interpretation or guidance may be required. For the issues dealt with in this paper - recognition and measurement of a joint defined benefit plan - this could include standards that relate to shared control, as OTPP is a joint defined benefit plan, standards that relate to the definition of an asset and standards that relate to measurement uncertainty:

- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015, effective from April 1, 2017)
- MEASUREMENT UNCERTAINTY, Section PS 2130 (issued in April 2005)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 which is more recent and will be effective in for periods beginning on or after April 1, 2017. Section PS 3210 provides additional guidance on the various components of the existing asset definition found in Section PS 1000; it does not change the definition.

Accounting Analysis

Question 1 – Classification of a pension asset

The analysis below addresses whether the Province's share of the pension surplus in OTPP, calculated in accordance with PSA standards under Section PS 3250, represents a reportable asset to the Province of Ontario in the Public Accounts.

Standards in the PSA Handbook

The focus of the following analysis is on the accounting requirements in RETIREMENT BENEFITS, Section PS 3250 as this standard is a primary source of GAAP which specifically addresses the accounting for pension assets. The following highlights some key concepts and guidance contained in this standard.

RETIREMENT BENEFIT, Section PS 3250 – Purpose and Scope

The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250.003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

RETIREMENT BENEFITS, Section PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*
>
> *(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;*
>
> *(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and*
>
> *(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.*
>
> *The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.*

Additional guidance on identifying Joint Defined Benefit Plans (JDBPs) is in Section PS 3250 paragraphs .79 to .80 which similarly highlight the importance of both shared control and shared risks and rewards in a JDBP:

> *.079 Governments may participate jointly in defined benefit plans where the government shares the risks and rewards jointly with plan participants, represented by a sponsor or sponsors. Joint defined benefit plans are governed by a formal agreement between the sponsors, which establishes that the sponsors have shared control over the plan. A governing board is generally appointed by the joint sponsors with equal representation and a mutually agreed-upon chair.*
>
> *.080 A government would consider the characteristics of the plan to determine whether it meets the definition of a joint defined benefit plan. In a joint defined benefit plan, funding contributions are shared mutually between the government and the plan members. The sponsors have control over*

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> *decisions related to the administration of the plan and the level of benefits and contributions on an ongoing basis based on the terms of the contractual agreement. The sponsors share, on an equitable basis, the significant risks associated with the benefit plan. Risk would not be considered to be equitably shared in an arrangement where the government and the joint sponsors fund the plan equally but where the government retains the full risk of the accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.*

It should be noted that the definition of a Joint Defined Benefit Plan under Section 3250 is not the same as the definition of a JSPP under the PBA, although there are some overlapping concepts between the two. A JDBP is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. The Province has concluded that OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. The OTPP is a contractual arrangement between the Province and OTF in which:

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

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 10(1)3 of the TPA for example).

The TPA, the Partners' Agreement and the plan text collectively set out this shared control and that the Province of Ontario has an equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a joint defined benefit plan.

The classification of OTPP as a JDBP for accounting purposes [and a JSPP under the PBA] by the Office of the Provincial Controller has been consistent since 2001 and had been consistently accepted without question by the Office of the Auditor General, including throughout the 2015/16 Public Accounts.

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Question 2 – Recognition of a pension asset for a JDBP

RETIREMENT BENEFITS, Section PS 3250 paragraphs .081 to .082 provide guidance on the accounting for a JDBP in the financial statements of the government sponsor. As OTPP meets the definition of a JDBP for the reasons noted above, the relevant guidance for the Province for purposes of reporting retirement benefits in the Public Accounts includes:

> *.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]*
>
> *.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.*

Section PS 3250.81 clearly states that "The government should account for its portion of the plan in accordance with the standards for defined benefit plans". It is clear from this that only the government's portion of the plan is included in the government's financial statements consistent with the requirements of Section PS 3250 (recognition) and the measurement of that portion is based on the requirements of Section PS 3250 (measurement). It is also then clear that the requirements of the standard for recognition and measurement, including the Limit of the Carrying Amount of an Accrued Benefit Asset guidance, are designed to be applied to a shared control situation and not only to situations where there is unilateral control. If it was intended that no pension asset could be recognized because the asset was subject to shared control and not unilateral control Section 3250 paragraph .081 would have made this clear. This paper discusses the question of measurement separately in Question 3.

The balance sheet recognition guidance for retirement benefits is stated in Section PS 3250 paragraphs .016 to .017:

> *.016 The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date. [SEPT. 2001]*
>
> *.017 The components of the retirement benefit liability are:*
>
> > *(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;*
> >
> > *(b) plan assets, if any; and*

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(c) unamortized actuarial gains and losses.

As the OTPP is a funded plan there are plan assets that are recognized as part of the retirement benefit liability. When plan assets and the net impact of unamortized actuarial gains and losses exceed the accrued benefit obligation then there is an "Accrued benefit asset" (ABA). An ABA is defined in Section PS 3250 as follows:

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

Accordingly, the portion of the government's plan to be recognized includes their share of the accrued benefit obligation and also their share of the plan assets. In the case of the Province's portion of OTPP there is no uncertainty regarding the *existence* of an ABA for the government's portion of the plan; the ABA is calculated by reference to accrued benefit obligation and plan assets, both determined based on the best estimate assumptions and the methodologies required by with Section PS 3250 for these items. As noted above an ABA is defined as the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance). For a jointly sponsored plan, this is the government's accumulated cash contributions less the government's share of the current and prior years' benefit expenses that are attributable to the government under the joint defined benefit plan. The Province's portion of OTPP resulted in an ABA of $10.1 billion as at March 31, 2016. There is no uncertainty regarding the occurrence of the cash contributions made (and the interest earned thereon) measured in accordance with Section PS 3250 and the existence of the government's obligation. As Section 3250.80 *requires* a government to account for its portion of the plan in accordance with the standards for defined benefit plans, this would include the recognition of any asset that meets the definition of an ABA under the standard.

Further, Section PS 3250.50 refers to the presentation of the ABA; this amount is presented in the financial statements, net of any valuation allowance. This indicates that an ABA should be recognized in the financial statements, but measured in reference to the limit on the carrying amount of the asset - essentially a measurement requirement rather than a recognition requirement, as the limit could result in an ABA being measured at anything from $nil to its full amount. Note that the *measurement* of any net asset is subject to guidance in Section PS 3250 paragraphs .50-.59 and is discussed later in this paper.

To recognize only their share of the liability and not their share of the plan assets, or to recognize only a net liability (accrued benefit obligation exceeds plan assets) but never a net asset (when plan assets exceeds the accrued benefit obligation, subject to the valuation allowance guidance discussed in the Measurement section below), would indicate that the Province does not share equitably in the risks and rewards of the OTPP because they bear only the risk of increased liabilities without being able to bear

any rewards of investment returns on the plan assets and under this interpretation the plan would not therefore be a joint defined benefit plan.

Concept of Shared Control and Asset Recognition

Included in the definition of a JDBP is the concept of shared control. Points (b) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of shared control resulting in a recognition of an asset could on the surface appear to conflict with the definition of an asset under FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210, as part of the definition of an asset under PS 1000 would suggest that the government must control the economic resource and access to the future economic benefits. Since shared control does not equate to control, there is a need to consider whether the recognition of any asset under PS 3250 is appropriate where there is only shared control.

The Province's position is that PSAS does not preclude asset recognition for assets under shared control and specifically for plan assets of joint defined benefit plans for the following reasons:

- As discussed above GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity. Section PS 3250 is a primary source of GAAP for dealing specifically with joint defined benefit plans and, as noted above, requires the government to account for their portion of the plan – both the accrued benefit obligation and plan assets in accordance with Section PS 3250. As such, reference to Section PS 3250 is sufficient to indicate that the recognition criteria are met for joint defined benefit plan assets, no further source of PSAS guidance need be considered.
- Similarly, if other primary sources of GAAP are considered then it is relevant to consider GOVERNMENT PARTNERSHIPS, Section PS 3060 which also includes the concept of shared control. Under Section PS 3060, shared control is sufficient for asset recognition.
- The concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. With the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that PSAB did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

- The Province's reporting of a pension asset for the JDBP is therefore consistent with these primary sources of GAAP, subject to measurement guidance including impairment considerations.

The similarities between the definitions of a JDBP and a government partnership under PSAS are demonstrated in Appendix F to this paper, and further support PS 3060 as being a relevant primary source of GAAP dealing with similar circumstances, should it be considered necessary to go outside of the requirements of Section PS 3250 to look for further clarification and guidance on recognition.

Under Section PS 3060 a critical condition for a Government partnership is shared control. Section PS 3060 explicitly acknowledges that under shared control "none of the partners is in a position to exercise unilateral control over the government partnership" (PS 3060.20), yet the accounting model required by Section PS 3060 for non- GBPs[9] is that of proportionate consolidation which is the recognition of a pro rata share of assets, liabilities, revenues and expenses of the partnership. Joint defined benefit plans are excluded from the scope of Section PS 3060 on the basis that control is shared with employees rather than with a party outside of the reporting entity (Section PS 3060 paragraph .06 footnote 3). This reason indicates that such plans are excluded because of a closer relationship between the government and the other party than normally exists for government partnerships. Even when an independent third party shares control, Section PS 3060 still requires the recognition of a share in an asset subject to shared control, indicating that the PSAS framework does not require unilateral control in order to support asset recognition when there is shared control. It would not be appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3060 for proportionate consolidation, and similarly it is not appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3250 to account for the government's portion of a joint defined benefit plan. In other words, PS 3250 is a primary source of GAAP and provides sufficient and complete guidance on how to account for assets related to joint defined benefit plans.

Concept of Contingent Asset

CONTINGENT ASSETS, Section PS 3320, provides guidance on the disclosure of contingent assets in a government's financial statements. It characterizes a contingent asset as one where there is uncertainty as to the existence of an asset (Section PS 3320 paragraph .04). It is the Province's position that the existence of the pension asset is not uncertain – there is an accrued benefit asset calculated in accordance with Section PS 3250 as noted above that is based on past transactions, being the impact of cumulative contributions and benefit expense. The fact that shared control exists with regards to access to the assets of the plan does not create additional uncertainty that would impact asset recognition under PSAS. The Province anticipates that in a broad sense, s any OTPP surplus would be shared in an "equitable manner" under the terms of the arrangement, and this is enabled through the ability to

[9] Government business partnerships (GBPs) are accounted for under the modified equity method rather than proportionate consolidation.

negotiate the utilization of the surplus including the ability to prevent the utilization of the surplus in a manner that does not benefit the Province. This expectation is further supported by past history of surplus utilization (see Appendix G). The method, extent and timing of which the Province will obtain the expected future benefits (contributions reductions vs increase in benefits) is not certain. However Section PS 3320 also states "The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset. For example, even though there may be measurement uncertainty related to income tax receivable, there is nothing uncertain about the fact that this asset exists. Any uncertainty is related solely to the amount thereof" (Section PS 3320 paragraph .07). Based on past history of surplus utilization for OTPP and based on the constating documents, expected future benefits for the Government are present. The uncertainty as with many types of assets relates to measurement uncertainty which will be discussed below.

Conclusion on recognition

Therefore the Province has concluded that PSAS permits the recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets must be subject to unilateral control. The Province's share of OTPP's pension surplus meets the definition of an Accrued Benefit Asset under Section PS 3250. The measurement of that accrued benefit asset is determined by reference to the guidance in Section PS 3250 regarding the Limit on the Carrying Amount of an Accrued Benefit Asset, which is discussed in Question 2 of this position paper.

Question 3 – Measurement of a pension asset

For an asset to be recognized it must be reliably measureable (Section PS 1000.55). Section PS 3250 paragraphs .050 to .059 address how to measure a pension asset. This is a two-step process. Firstly the accrued plan obligation (a Credit) and the plan assets (a Debit) are measured in accordance with the standard, and adjusted for any unamortized actuarial gains or losses (a Debit for gains not yet realized, a Credit for losses not yet realized). This measurement results in a retirement benefit liability when it is a net liability (a Credit) amount or an accrued benefit asset when it is a net asset (a Debit) amount. When the resulting amount is an asset, the standard requires a second step to test that the asset is not impaired. It should be noted that impairment testing in some form is required for all assets recognized under PSAS standards except those carried at fair value, although the methodology of impairment tests will vary depending on the nature of the asset. The amount that is tested is the "adjusted benefit asset". When there are net unamortized gains the ABA is equal to the adjusted benefit asset. When there are net unamortized losses the ABA is reduced by those net unamortized losses to calculate the adjusted benefit asset. A graphical illustration of the calculation of the Accrued Benefit Asset (AcBA) and the Adjusted Benefit Asset (AdBA) are shown in appendix C. Section PS 3250 paragraphs .052 to .059 go on to explain what the standard means by expected future benefit and how a government may benefit from the ABA or adjusted benefit asset. Note that for OTPP the accrued benefit asset equals the adjusted benefit asset as there are net unamortized actuarial gains.

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Section PS 3250.50-.59 are included here for completeness and ease of reference:

Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)

.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]

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

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

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

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

.055 The objective of the standard in Section PS 3250 paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

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

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

Section 3250 paragraph .052 states that a government may benefit from an ABA by either i) withdrawing surplus assets from the plan or ii) by taking a contribution holiday or receiving a refund of contributions. This is an explanatory paragraph on how a government may benefit from an ABA and why a valuation allowance may be needed, rather than detailing the test to be applied. Part of this justification is to note that that an ABA may be impaired when "the government is not entitled to benefit from [the ABA] fully". Examples of when a government may not be entitled to benefit from the ABA fully are given, such as a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

Section PS 3250 paragraph .059 gives additional guidance to apply when an entity contemplates realizing future benefits through a surplus withdrawal: "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the

ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal". This introduces the concept of a legally enforceable right but only in the context of a government's withdrawal of surplus and not in the context of contribution holidays. If the standard setters had intended legal enforceability to be the test throughout the standard, they would not have raised it only in the context of a withdrawal of surplus, but as a more fundamental notion in the guidance on expected future benefit.

It is acknowledged that the Province does not have a unilateral legal right to reduce its contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to shared control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Section 3250 paragraph .052 does not state that being "entitled to benefit" means having a legally enforceable right as at the reporting date to take contribution holidays. When considering the ability to realize expected future benefits under Section PS 3250 paragraph .052, the Province's legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability which is not explicitly required by the standard to support recognition and measurement of JDBP pension assets. Specifically, the amount of pension asset that gets recorded needs to take into account considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a pension asset in the Public Accounts. Pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". Expected does not equate to certainty (Section PS 1000.056).

Under the Plan and Partners' Agreement, if funding surpluses occur the partners are required to negotiate the use of the funding surplus (at least once every three years) and the Province is entitled to negotiate a reduction in contributions in respect of its share of the surplus. Under the Partners' Agreement any funding surplus must be dealt with so that the funding valuation becomes actuarially balanced*. In other words when there is a funding surplus over a certain range the "status quo" cannot be maintained, the surplus must be reduced by a combination of reductions in contributions, increases in benefits or withdrawals of surplus*. This is confirmed by the Partners' Agreement Section 57 that requires an actuarially balanced valuation to be prepared at least once every three years, allowing for a contingency reserve, combined with the FMP which sets out the framework for determining when a surplus or deficit outside of agreed upon ranges are met and action must be taken. While the Province might choose to accept an increase in member benefits rather than to reduce funding, any such decision is at the Province's discretion since the OTF cannot force the Province to increase benefits instead of

reducing contributions. In other words it is at the Province's discretion whether to address the actuarial balancing requirements by allowing its portion of the surplus to be utilized through increased benefits. The OTF equally has the right to not agree to reduced contributions from the Province, but they do not have the right to force an inequitable sharing of the surplus. Therefore, the Province is entitled to negotiate their share of the JDBP which may include taking contribution holidays in future negotiations and can effectively use their power in negotiations to benefit from the ABA. The joint partners do have the ability to renegotiate all aspects of the partners' agreement including the FMP. However all changes require the agreement of both parties and as such the Province can veto any changes to the agreement. Note that while the negotiations are based on funding surplus amounts rather than accounting surplus amounts, any differences would be captured in the mechanics of the calculation of the expected future benefit rather than precluding an ability to benefit from any of the accounting surplus.

Further, Section PS 3250 paragraph .055 indicates "The objective of the standard in Section PS 3250 paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Many generally accepted accounting frameworks use "expected" in a number of principles and is typically used in the probabilistic sense – something is expected when it is probable at some level, it does not equate to certainty. The Province has an expectation that they will benefit fully from the ABA by exercising their current rights under the plan arrangements to negotiate the use of current and future surpluses in the form of contribution holidays. This position is supported by the review of the constating documents and past history of negotiations that indicate:

1. The TPA 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). 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.
2. 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 (refer to Appendix G for a history of surplus utilization for OTPP). 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.

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3. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right[10]), 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.
4. 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. Under the plan, contributions are generally borne equally by the Province and the employees. Employees benefit economically from both an increase in benefits and from a reduction of contributions. The Province benefits economically directly from a reduction in contributions. This makes it reasonable that at least some contribution reductions would be agreed to by the joint sponsors as a highly unequal weighting towards increases in benefits would not balance the interests of taxpayers and teachers therefore may be unlikely to be a reasonable outcome of "good faith" negotiations between the Province and the OTF.

   This is further supported by the historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses, should also be considered. As previously discussed in respect of conditional indexing, a decrease in benefits by the employees were offset by an increase in payments by the Province. Similarly as the sponsors agreed to restore indexation, this increase in benefits resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.98B for the 2015 change, and $1.68B for the 2014 change). This demonstrates that historically and over the long term an equitable sharing of the deficits and surpluses has resulted in changes in the Province's contributions, even when there are decreases or increases to benefits for employees.

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, a mediator may be chosen by agreement of the sponsors (section 77 of the Partners' Agreement). If the sponsors do not accept the report of the mediator, an arbitration board will be appointed (section 84 of the Partners' Agreement). The arbitration board would consist 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

[10] The OTF Call Right is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising the government initiated Freeze period. Part of a previously agreed upon arrangement to ensure equitable sharing of the risks and rewards over the long term of the plan, it is not a general unilateral right to utilize future surpluses beyond the recovery of the specific funding shortfalls.

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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).

Based on the above analysis, the Province believes that the uncertainties around how and when to utilize a surplus in the OTPP do not result in an inability or lack of entitlement to utilize the surplus in accordance with Section 3250.52.

Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250.53 to .58 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where actual realization of the benefit would be reflected in a reduction in future contributions. A valuation allowance is recorded against the pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province calculated the expected future benefit as the sum of:

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

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

Each of these is discussed separately.

Through withdrawal of the surplus (Section PS 3250.056 (b))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph .059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

The TPA for OTPP does not specify a method for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution. The Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example

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at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

The Province's position is that there is no amount of expected future benefit included in respect of withdrawable plan surplus.

Through reducing future contributions (Section PS 3250 paragraph .056 (a))

PS 3250.56(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per PS 3250 paragraph.81 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

PS 3250.55 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the pension asset value to be recorded in the accounts. For example, if the pension asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the pension asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. It is therefore relatively straightforward and is typically calculated based on the Province's share of the current service cost reported in the actuarial valuation taken into perpetuity unless there is evidence to indicate the workforce will significant diminish over time (for example a closed plan).

The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for judgment in the above calculation is in this second part of the calculation. Note that consistent with the calculation of the expected future accruals for service, no amounts are considered for employee contributions as these relate to the OTF's portion of the plan. The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (3250.56(a)). There is no further guidance in S 3250 as to how the calculation of minimum required contributions should be performed and what restrictions or parameters should be factored into this calculation. Typically for defined benefit plans minimum contributions include those that are required by the pension regulator to be made for funding.

However, minimum contributions regardless of any surplus, may be required by plan text, legislation or other agreements with employees. For OTPP a key element of judgment is determining what contributions are required by the current plan arrangements "regardless of any surplus". The constating agreements for OTPP require that the parties negotiate every 3 years as a minimum, and when there is a funding surplus.

Determining the number of years of contributions to include should involve an assessment of the facts and circumstances of the plan and should consider uncertainty. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the contractual agreements between the Sponsors that provide for the sharing of risks and benefits and specifically in respect of assessing the minimum contributions required by the plan agreements the following:

- One view of minimum contributions might be that the agreed upon level of contributions are the minimum contributions until they are altered in the plan text. As this can only happen with agreement from OTF it cannot be assumed that changes will be made and therefore that the contribution formula as stated in the current agreements will continue in perpetuity. This view provides the most conservative view of minimum payments. However as the current contribution amounts are greater than the government's share of the annual current service cost for the existing workforce this indicates that continued contributions at this rate will result in ever increasing surpluses. Extrapolating the surpluses, at a certain point other requirements that are currently incorporated into the plan text, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan will apply to reduce the contributions. The effect of these caps on contributions would have to be estimated but cannot be ignored as they form part of the current contribution arrangements. Modelling could be performed to develop expectations as to when these CRA limits could be expected to be reached assuming no changes in the contribution levels. As is the most conservative view (highest minimum contributions) the impact of this has been considered, as discussed below.
- An alternative view of the minimum contributions required by the plan is that there is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'. On this basis it could be argued that any agreed upon contribution levels are mandatory for only a three year period, after which the contributions must be renegotiated to stay the same, increase or decrease, such that the stated contribution level in the plan text constitute minimum payments for only three years. It should be noted that the plan text requires an actuarially balanced funding valuation, so to the extent that a funding deficit currently existed a contribution holiday (contributions lower than the annual cost of the plan) could not be negotiated. However because the funding situation at the time of future negotiations is not known it could be argued that no amount is a fixed "minimum contribution" in this context, because all of the contribution amount is subject to future changes in funding and negotiation by the joint sponsors.

- Other views of what the minimum contributions are would fall between these two views, such as that the current funding level is set to ensure that there is no funding deficit over a 11 year period and after that changes in contributions would be negotiated. This view has been used in calculating the actuarial calculation of the asset ceiling as noted in the table below.
- Another consideration might be the specific framework within the Funding Management Plan for OTPP which contemplates specified funding zones and expectations regarding possible contribution reductions by the sponsors. Informed stochastic modelling would be necessary to estimate when the different funding zones will be reached and probability of contribution reductions may be increased.
- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to use some of the funding surplus to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change, $1.98B for the 2015 change, and $1.68B for the 2014 change).

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (PS 2130 paragraph .03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in Section PS 2130 paragraph .13, “As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.”

As part of the 2015/16 Public Accounts audit, the Office of the Provincial Controller engaged external consultants to conduct asset ceiling tests to assess the requirement for a valuation allowance against the $10.1 billion of net pension assets reported by the Province for OTPP . The results of those reports are summarized in Table 1 below.

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Table 1: Summary of Asset Ceiling Models performed for OTPP

Model Assumptions	Expected Future Benefit or Asset Ceiling ($ Billions)	Results
1. There is no minimum employer contribution under the plan/legislation that is required even if a surplus is present.	$44.6	There is no reduction in the expected future benefit (EFB) as at March 31, 2016.
2. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of the current funding report. Contribution requirements are $1.7B per year for 2015, 2016 and 2017.	$41.2	The minimum contribution requirement applies to the current period of the funding report and until a new report is completed. EFB is reduced for 2 years by $1.7B at March 31, 2016.
3. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of contribution requirement (i.e. 11 years through 2026) not just for the period of the current funding report.	$29.3	Uses a period to 2026 (11 year period) based on the funding report special contribution requirement. The EFB at March 31, 2016 is reduced by $15.3B.
4. The surplus is never used until the time it reaches the Income Tax Act (ITA) threshold. Once attained, the excess surplus is used at 50% for employees and 50% for the Province to reduce contributions in the following years.	$23.2	The ITA surplus limit is reached at the end of 2025, leading to forced contribution reductions from 2026. EFB is reduced by $21.4B at March 31, 2016
5. Every year, 50% of current year surplus is applied to	$12.9	The ITA surplus limit is reached at the end of 2041 leading to forced

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improve member benefits and the remaining 50% of the current year surplus is retained and continues to accrue. Once the ITA threshold is attained, the excess surplus is used 50%-50% to reduce contributions by employees and the Province.		contribution reductions from 2042. EFB is reduced by minimum $37.7B at March 31, 2016.

Note: Models above made no assumption on any value of the surplus withdrawal.

Under the Partners' Agreement, the parties are mandated to negotiate benefits and contributions every three years as a minimum and if agreement is not reached, it is reasonable to expect that a change in contributions might occur rather than the 'status quo' being retained.

For purposes of the OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

In addition to the above calculations, the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan should also be considered. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that no valuation allowance is required.

The determination of the minimum contribution levels required as input to the calculation of the expected future benefit involves significant judgements, estimation and assumptions about future funding surplus levels. These judgements, estimates and assumptions should be made on a consistent basis with best estimates used in developing the accrued benefit obligations and plan asset amounts. Regardless of the need to apply judgements, estimates and assumptions for the calculation, this does not imply that no asset can be recognized or that it cannot be reliably measured. In fact, pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions

will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". From the Province's perspective, 'expected' does not equate to 'certainty'.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (3250.42) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (3250.41). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. 3250.57 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on Plan Assets, which is one of the acceptable references suggested on PS 3250.44.

The OAG and the Government differ regarding whether it needs to be "expected" that the Government will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in Section PS3250 paragraph .059. The Government considers that it needs to be expected that future economic benefits are to be obtained as reflected in the definition of an asset in Section PS 1000 and as reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to use a plan surplus.

Other guidance in the PSA Handbook on measurement

MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe would be a useful addition to the current year financial statements. Section PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.*

> *.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.*

The estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is an acceptable alternative under PSAB and consistent with rates followed by other senior Canadian governments. Historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets reported in the Public Accounts.

Impact of valuation allowance

The current AG's view challenges previous interpretations of the Provincial Controller and former Auditor Generals regarding the interpretation and application of PS 3250 to those JDBPs where the government is a joint sponsor. The impact of the OAG's view is that no pension accounting surplus should be recognized in the Province's Public Accounts for JDBPs until the joint sponsor agrees to a change in the plan text for the Province to provide for unilateral authority to access surplus or reduce future contributions to enters into an agreement by year-end enabling the government to take a contribution holiday. In the absence of meeting either the criteria set out by the AG, any ABA would therefore be fully provided for through a valuation allowance, impacting each year's statement of operations by the amount by which the asset would otherwise increase in value. These results are counterintuitive with pension expense being higher in years in which increased funding is made and also higher when poor investment returns create actuarial losses that have not yet been amortized into the statement of operations. These examples are illustrated in Appendix C.

For information purposes, refer to Appendix H for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS. Of particular note is the impact in 2008 when the deficit would have be lower by $3 billion in a year when pension asset values fell significantly because of the financial crisis.

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Comparability of Ontario accounting for JDBPs to other Provinces

Commented [NP2]: Section should focus on JDBPs in other jurisdictions. Pauline/Jim to update.

Included in Appendix I is a legal opinion prepared by lawyers, Koskie Minsky, comparing access to the pension surplus of OTPP relative to JDBPs in British Columbia. The Province of British Columbia does not report a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

Quebec, Nova Scotia, Manitoba and New Brunswick also have pension plans that are in a net accrued benefit asset position before valuation allowance.

Commented [NP3]: Not JDBPs?

In New Brunswick, the target benefit pension plans are governed by an Agreement and Declaration of Trust which restricts the Province's access to the plan assets. These target benefit plans targets retirement benefits as opposed to guaranteeing it. Two of the four target benefit plans are in net asset position, where a full allowance is taken against the net pension asset.

Conclusion on measurement

As discussed, there is significant professional judgement and estimation in determining how to measure the valuation allowance under Section PS 3250, including the determination of the minimum contributions required by the current plan arrangements. It is the Province's position that the attributes of the joint defined benefit plan arrangements for the OTPP entitle the Province to access its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surplus through reduced contributions.

The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of those models to date no valuation allowance appears to be required and the OTPP pension assets should continue to be recorded on the books of the Province.

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Appendix A– Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the Sponsors to the OTPP have the authority to utilize ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years to comply with the PBA.

Commented [LD4]: JIM Can you also insert references to Sections 10 and section 57.
Also to Section 58 to 60 that are relevant.
Section 19 requires a valuation to be prepared every three years. This is also important.

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The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

In addition to the clauses identified above, the Partners' Agreement has an appendix called the Funding Management Policy which sets out the Sponsors' responsibilities in making funding decisions and

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surplus allocation regarding the Plan.

Funding Management Policy (FMP)

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

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

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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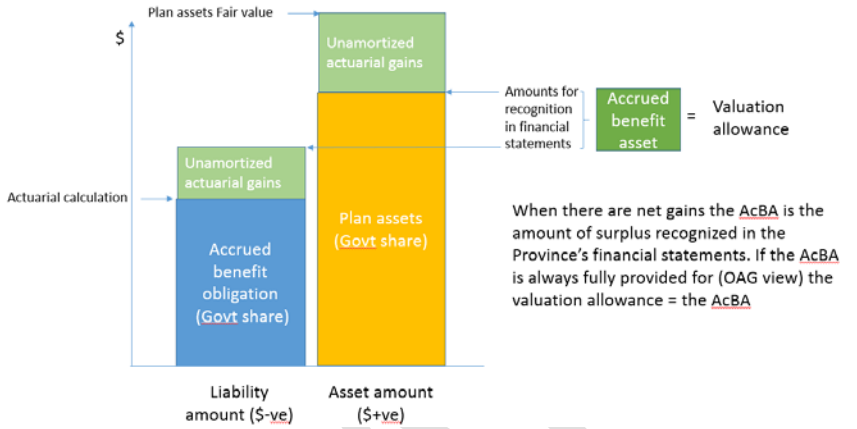
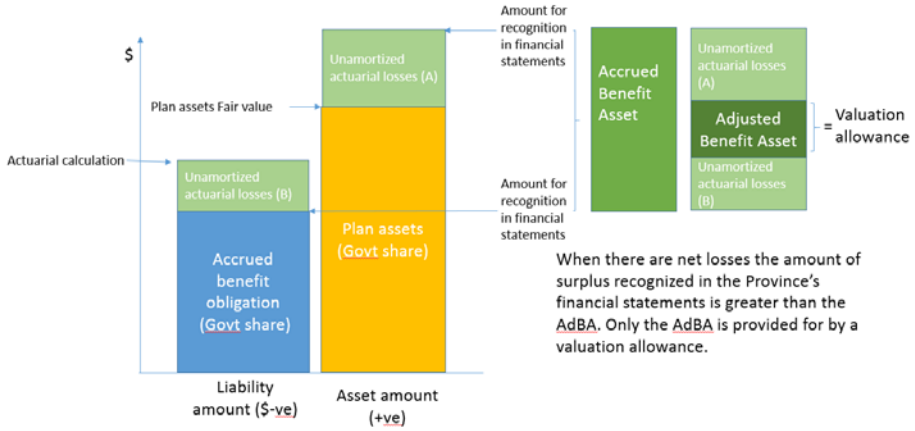
Appendix- C– Impact of a Valuation Allowance on Pension Assets

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



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

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

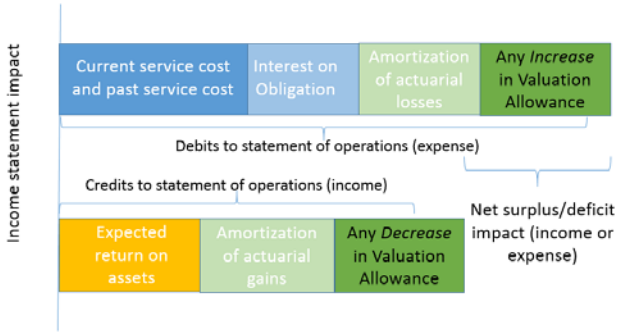


When there are net losses the amount of surplus recognized in the Province's financial statements is greater than the AdBA. Only the AdBA is provided for by a valuation allowance.

Components of Expense

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

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



Changes in the Accrued Benefit Asset

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

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

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

Appendix D - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, Section PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the definition of a JDBP

			focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership.	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former Section PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

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Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario				
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	5.95%	LT return on plan assets
Alberta				
Teachers' Post-1992 Pension Plan	7.00%	LT return on plan assets	7.25%	LT return on plan assets
Universities Academic Pension Plan	6.10%	LT return on plan assets	6.25%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)				
Local Authorities Pension Plan	5.80%	LT return on plan assets	5.80%	LT return on plan assets
Public Service Pension Plan	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Management Employees Pension Plan	6.40%	LT return on plan assets	6.40%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.75%	LT return on plan assets	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.20%	LT return on plan assets	6.20%	LT return on plan assets
Special Forces Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan				
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.80%	LT return on plan assets	6.80%	LT return on plan assets
British Columbia				
Public Service Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec				
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	6.40%	LT return on plan assets less inflation
Newfoundland				
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	6.30%	LT return on plan assets
Nova Scotia				
Nova Scotia Public Service Superannuation Plan (PSSP)	6.75%	LT return on plan assets	6.35%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	6.40%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba				
Civil Service Superannuation Plan	6.00%	LT return on plan assets	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.50%	LT return on plan assets	6.25%	LT return on plan assets

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Appendix ~~C~~F – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

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In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[11] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[11] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

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to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

We trust that these comments have been of assistance to you. Should you have any questions in regard to them, please do not hesitate to contact the undersigned.

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Appendix ~~D~~ G- Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.

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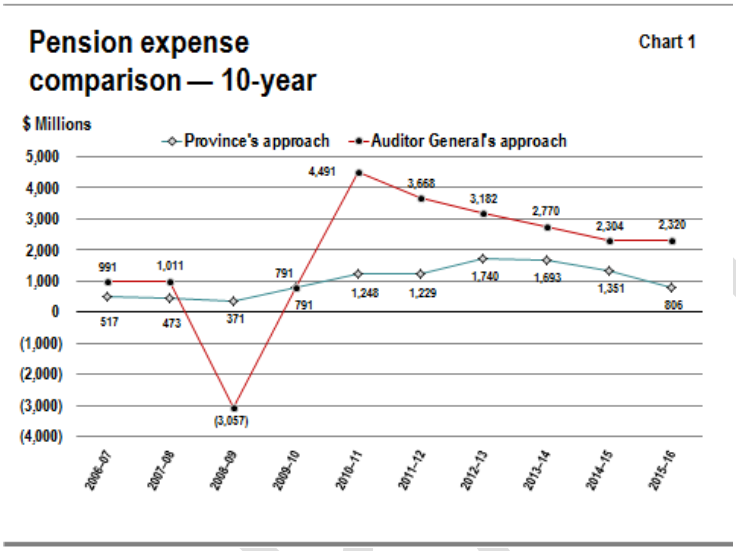
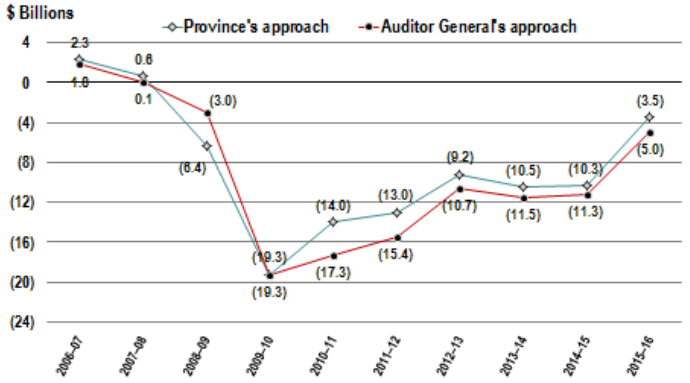


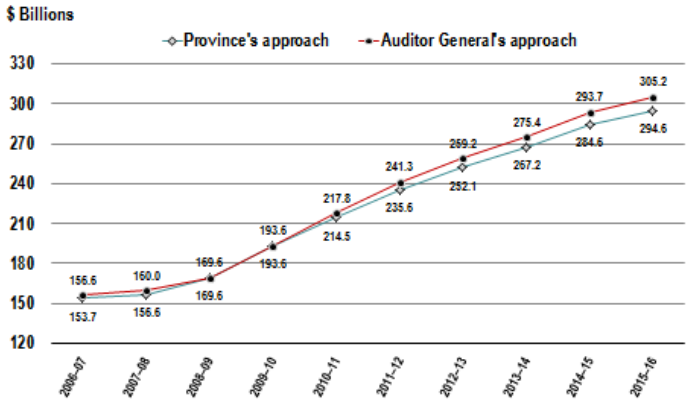
Surplus/(deficit) comparison — 10-year

Chart 2

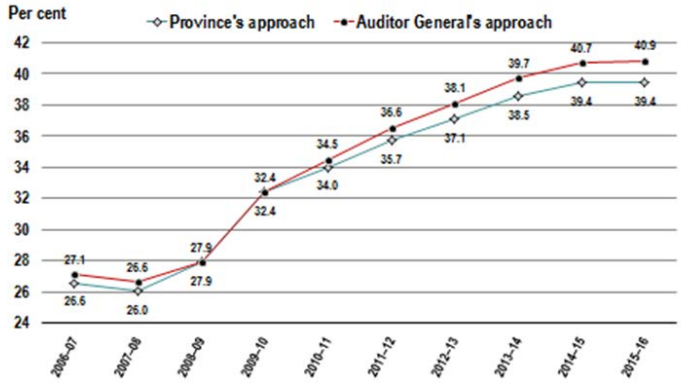


Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year Chart 4



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Appendix H – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			reduce the value of remaining special payments	
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		

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).

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Appendix I – Summary of different valuation methodologies for pension valuations

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The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits and pension obligations.	Measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered.
Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market -related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate.	In measuring a pension obligation amount, the defined benefit obligation amount determined by the	Not specified. However two methods are specifically acknowledged – a)

	For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.[12] The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

[12] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

Appendix A – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2011-12	2012-13	2013-14	2014-15	2015-16
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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.
Teachers' Pension Act (TPA)
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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the Sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the Pension Benefits Act, appointing the OTTP Board, and defining the role of the Board. Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the Sponsors to the OTPP have the authority to utilize ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years to comply with the PBA.

Commented [NP8]: JIM - please insert references to Sections 10 and section 57.
Also to Section 58 to 60 that are relevant.
Section 19 requires a valuation to be prepared every three years. This is also important.

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The process governing the use of ongoing surpluses by the Sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the Sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

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

We 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.

In addition to the clauses identified above, the Partners' Agreement has an appendix called the Funding Management Policy which sets out the Sponsors' responsibilities in making funding decisions and

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surplus allocation regarding the Plan.

Funding Management Policy (FMP)

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

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

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the Sponsors are unable to agree the mediation process set out in the Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both Sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the Sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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

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escalated adjustments for members).

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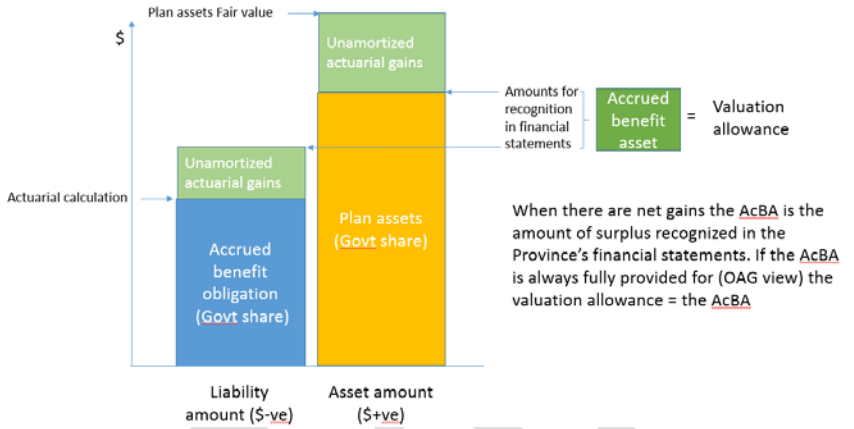
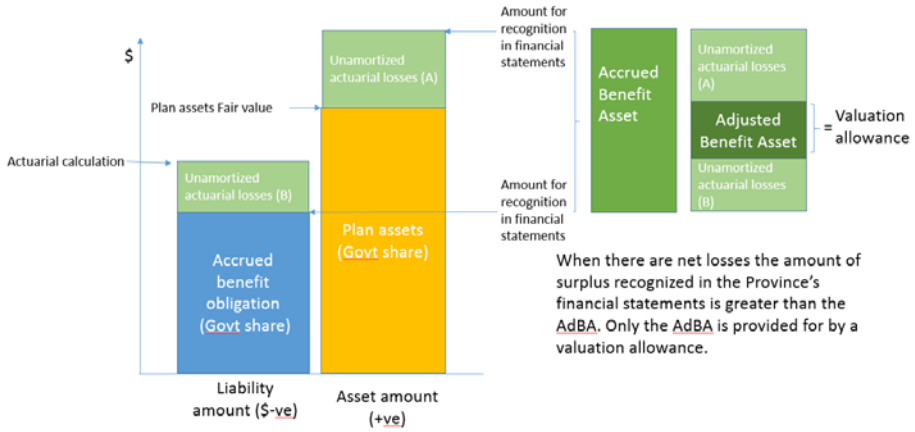
Appendix C – Impact of a Valuation Allowance on Pension Assets

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



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

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

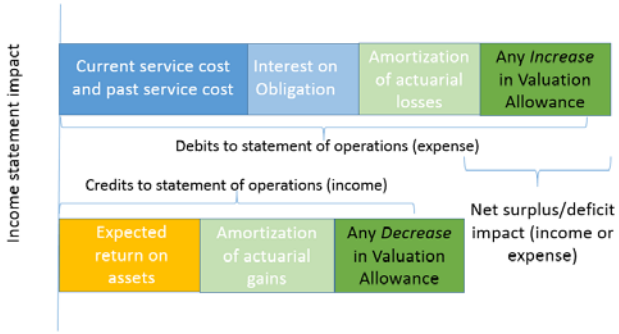


When there are net losses the amount of surplus recognized in the Province's financial statements is greater than the AdBA. Only the AdBA is provided for by a valuation allowance.

Components of Expense

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

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



Changes in the Accrued Benefit Asset

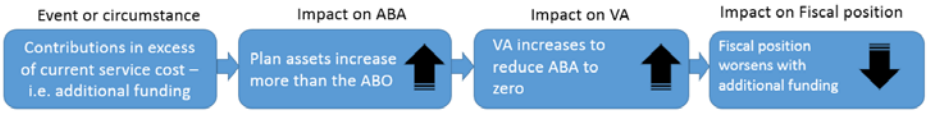
Continuing from the previous slide, where valuation allowances are taken to effectively reduce the value of the AcBA to zero, in the year of a reduction in the value of the AcBA or AdBA, where an economic downturn occurs for example, the following impacts on the statement of operations would be noted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

Event or circumstance	Impact on AcBA/AdBA	Impact on VA	Impact on Fiscal Position
Investment returns worse than expected e.g. economic downturn	The AcBA does not decrease significantly. The Adjusted Benefit Asset does.	VA decreases – lower allowance than prior year required	Fiscal position improves in an economic downturn
Plan assets fair values significantly lower in one year. Assuming no net amortized gains/losses in prior year this would create net *unamortized losses* as the use of market related values means the changes in plan assets are smoothed over 5 years.	The AcBA is based on the higher, smoothed value of plan assets and does not change significantly. However the actuarial losses are subtracted from the AcBA to calculate an AdBA, which is smaller than the AcBA.	Prior year allowance was based on AcBA (no net amortized actuarial losses). Current year is based on AdBA because there are unamortized actuarial losses. The AdBA is smaller than the AcBA because of the increase in unamortized losses. Therefore the VA is reduced correspondingly.	Fiscal position will be improved as a reduction in the VA results in a gain in the income statement in that year. The increased actuarial losses would only impact the statement of operations in future years. A similar impact would have been noted in 2008 if the OAG's position was reflected in the financial statements for that year.

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

Changes in the Accrued Benefit Asset

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



2015-2016 example:
Contributions of $1,812M exceeded other elements of pension expense by $1,514M

2015-2016 example:
Additional contributions increase plan assets. AcBA increases by $1,514M

2015-2016 example:
AcBA increase of $1,514M results in an increase to the VA of $1,514M

2015-2016 example:
Deficit increases by $1,514M.

The cash paid for contributions has not resulted in an asset and so is an expense, despite the funding position of the Province's share of the plan has been improved by the additional contributions.

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

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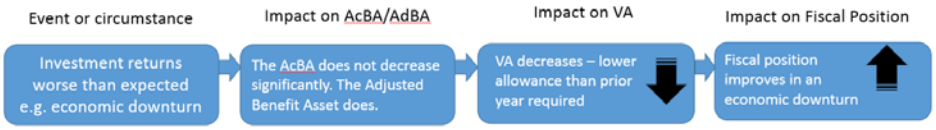
Changes in the Accrued Benefit Asset

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



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

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

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

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

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

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

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Appendix D – Summary of different valuation methodologies for pension valuations

Commented [NP9]: Request sent Oct 28 to ISPPD requesting to review details and confirm.

The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
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Actuarial cost method	*[To confirm – not clear from the valuation report]*	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values [To confirm the approach taken in OTPP funding valuation]	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	Market -related values, which are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied consistently. The Province uses adjusted market values for some classes of assets in certain plans.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate.	In measuring a pension obligation amount, the defined benefit obligation amount determined by the	Not specified. However two methods are specifically acknowledged – a)

	For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR Reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work To confirm the approach taken in OTPP funding valuation]	plan's sponsor may be (but is not required to be) used. Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. Part I (IAS 19) requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on bonds issued by the Province of Ontario.	discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing.[13] The Province of Ontario uses a discount rate for OTPP determined by reference to plan asset earnings.
Underlying population data	All valuation methodologies should use consistent underlying data of the population covered by the plan		
Inflation rate	All valuation methodologies should treat inflation in a consistent manner and use a consistent inflation assumption (best estimate). [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Demographic assumptions	All valuation methodologies should use a consistent demographic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		
Other economic assumptions	All valuation methodologies should use a consistent other economic assumptions (best estimate) in similar ways [To confirm this is actually the case – does the Province rely on the OTPP's Board's judgement or make their own estimates?]		

[13] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP [Tables are to be updated]

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	ON 1	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	ON 2	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	ON 3	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	ON 4	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	ON 5	5.95%	LT return on plan assets
Alberta					
Teachers' Post-1992 Pension Plan	6.80%	LT return on plan assets	AB 1	7.00%	LT return on plan assets
Universities Academic Pension Plan	6.00%	LT return on plan assets	AB 2	5.95%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)					
Local Authorities Pension Plan	5.60%	LT return on plan assets	AB 3	5.60%	LT return on plan assets
Public Service Pension Plan	6.00%	LT return on plan assets	AB 4	6.00%	LT return on plan assets
Management Employees Pension Plan	6.10%	LT return on plan assets	AB 5	6.10%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.40%	LT return on plan assets	AB 6	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.00%	LT return on plan assets	AB 7	6.00%	LT return on plan assets
Special Forces Pension Plan	5.90%	LT return on plan assets	AB 8	5.90%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan					
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.50%	LT return on plan assets	SK 1	6.50%	LT return on plan assets
British Columbia					
Public Service Pension Plan	6.50%	LT return on plan assets	BC 1	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	BC 2	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	BC 3	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	BC 4	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec					
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	QC 1	6.40%	LT return on plan assets less inflation
Newfoundland					
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	NF 1	5.80%	LT return on plan assets
Nova Scotia					
Nova Scotia Public Service Superannuation Plan (PSSP)	6.70%	LT return on plan assets	NS 1	6.15%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	NS 2	6.25%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba					
Civil Service Superannuation Plan	6.00%	LT return on plan assets	MB 1	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.25%	LT return on plan assets	MB 2	6.00%	LT return on plan assets

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Appendix F - Definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the definition of a JDBP

			focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership.	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from the time the OTPP became a jointly sponsored pension plans 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	$0

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			of remaining special payments	
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		

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).

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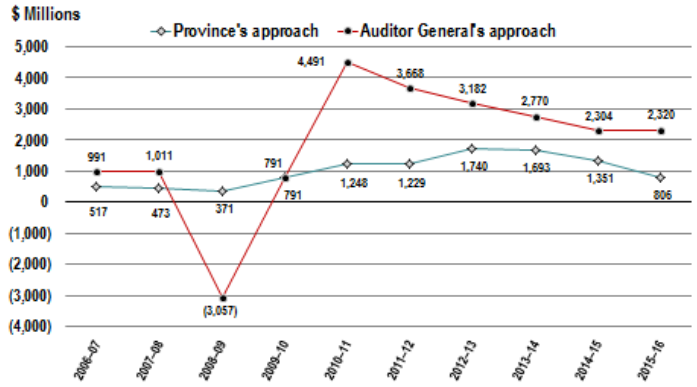
Appendix H - Comparison of key measurements of the Province over the prior 10 years following the Auditor General's approach to pension accounting compared with following the Province's interpretation of the PSAS.

Commented [NP10]: APFR to insert for OTPP details only (Pauline/Patricia)

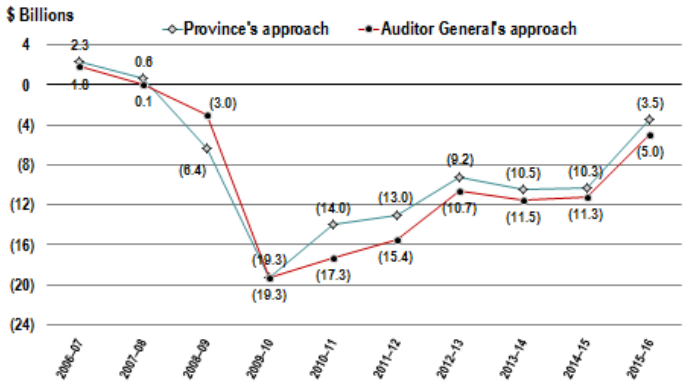
Pension expense comparison — 10-year

Chart 1



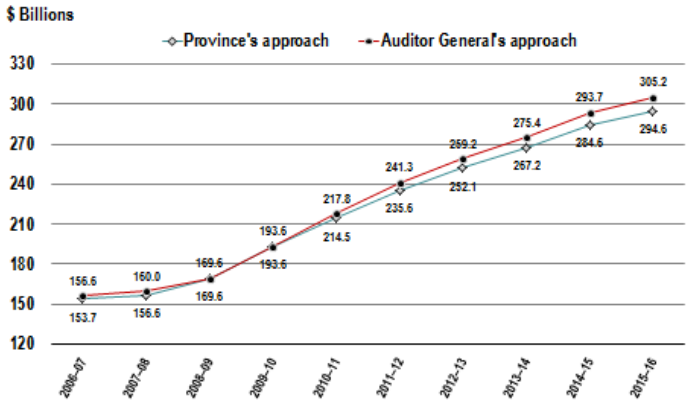
Surplus/(deficit) comparison — 10-year

Chart 2



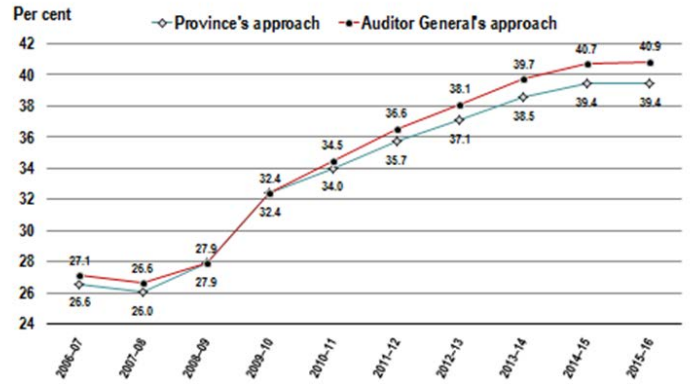
Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year

Chart 4



Appendix I – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners'

Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

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In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[14] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[14] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

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to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

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FW_ TBS question re ITA Excess Surplus.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]; Danyluk, Kerry (CA - Toronto) [kdanyluk@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: TBS question re ITA Excess Surplus
Date: Saturday, September 24, 2016 23:00:43

FYI. n

From: Hatzis, Len (TBS)
Sent: September-24-16 10:58 PM
To: Veinot, Cindy (TBS); Petsche, Nadine (TBS)
Cc: Kaufman, Paul (TBS); Kearney, Sean (TBS)
Subject: Fw: TBS question re ITA Excess Surplus

Cindy /nadine

Let me know if this addresses what you required. Thanks

Sent from my BlackBerry 10 smartphone on the Rogers network.

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

Sent: Saturday, September 24, 2016 6:00 PM

To: Hatzis, Len (TBS)

Cc: Carson, Brenda

Subject: TBS question re ITA Excess Surplus

Hi Len:

Further to our discussion and your emails, we have reviewed the emails you provided. The following is a brief overview of the excess surplus rule under the ITA:

Under the ITA, all pension plans that have a defined benefit provision (including JSPPs)

are prohibited from receiving further employer contributions while the plan holds an "excess surplus". The rules in the ITA operate such that essentially if an actuarial valuation illustrates that a pension plan's assets are greater than 125% of the plan's liabilities, the plan is considered to have an excess surplus and employer contributions are prohibited until such time as the excess surplus can be eliminated (or, alternatively, benefit improvements are provided – in this case the actuarial valuation has to include the improvements). The prohibition of ongoing contributions under the ITA rules generally applies to the employer. However, depending on the contractual terms, the prohibition could apply to both members and the employer.

Please let us know if you have any further questions or if we may be of further assistance.

Best regards,

Jana Steele

****

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****

FW_ Treasury Board Secretariat of Ontario - Invoice #36180604, October 11, 2016.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: nicole.smellie@ca.pwc.com [nicole.smellie@ca.pwc.com]
Subject: FW: Treasury Board Secretariat of Ontario - Invoice #36180604, October 11, 2016
Date: Tuesday, October 11, 2016 17:45:12
Attachment 1: Treasury Board.pdf

Shyrose,

FYI. Nadine

From: nicole.smellie@ca.pwc.com [mailto:nicole.smellie@ca.pwc.com]
Sent: October-11-16 5:29 PM
To: Shyrose.birani@ontario.ca
Cc: lucy.durocher@ca.pwc.com; Petsche, Nadine (TBS)
Subject: Treasury Board Secretariat of Ontario - Invoice #36180604, October 11, 2016

Good Afternoon,

Please find attached a PDF copy of our **October** invoice. Unless specified by you, we will not be forwarding a hard copy by mail.

For your convenience we accept the following payment methods:

Wire Transfer

Cheque

Credit Card

Please Remit Payment Referencing Invoice Number To:

Please remit Payment and Invoice Copy To:

Please contact Nicole Smellie:

CIBC, 199 Bay St., CCW, Concourse Level, Toronto, Ontario Canada M5L 1G9
Account Name: PricewaterhouseCoopers LLP **Transit No:** 010:00002 Swift Code: CIBCCATT

PwC Central Accounting Centre, PwC

Centre, 354 Davis Rd.,
Suite 600
Oakville, ON
L6J 0C5

nicole.smellie@ca.pwc.com to receive secure link or by phone 416-941-8383 ext. 14070

CAD Account: 63-55412
USD Account: 04-77419

Amex, MasterCard, and Visa Accepted

*Email payment details, including invoice number and amount paid to:
accounts.receivable@ca.pwc.com

Please note that an invoice number **must be included** for all payments. **For credit card transactions Foreign Currency exchange rate charges, and foreign transaction fees may apply for invoices issued in currency other than Canadian dollars.**

If you have any questions regarding this invoice please do not hesitate to contact myself or Lucy Durocher.

Kind Regards,

Nicole Smellie
PwC | Billing Administrator, Assurance
T: +1 416 941 8383 ext. 14070
Email: nicole.smellie@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Treasury Board.pdf

Invoice

Ms. Nadine Patsche
Director, Accounting Policy and Financial Reportin
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Lucy Durocher
Telephone: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com

Invoice number:	TR136180604	Account number:	60144520
Invoice date:	October 11, 2016	Payment requested by:	October 26, 2016

Fees for Professional Services: Interim billing for Pension Accounting advice of 39.3 hours to October 3, 2016.	**CAD**
Fees	**15,327.00**
HST	**1,992.51**
Total due	**17,319.51**

Remittance information

Electronic wire or EFT (not e-Transfer): CIBC, 199 Bay Street, CCW Concourse Level, Toronto, Ontario, M5L 1G9
Account name: PricewaterhouseCoopers LLP
Transit no.: 010:00002 Swift code: CIBCCATT CAD account: 63-55412 USD account: 04-77419
Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Invoice *Remittance copy*

Ms. Nadine Patsche
Director, Accounting Policy and Financial Reportin
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Lucy Durocher
Telephone: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com

Invoice number:	TR136180604	Account number:	60144520
Invoice date:	October 11, 2016	Payment requested by:	October 26, 2016

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Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

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

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
Subject: FW: URGENT: Statement of Facts and Assumptions Sept 19.docx
Date: Monday, September 19, 2016 14:45:59
Attachment 1: image001.gif
Attachment 2: image002.gif
Attachment 3: image003.jpg
Attachment 4: Statement of Facts and Assumptions Sept 19 (3).docx

---

Matt,

Please see additional feedback from legal (internal and external). Please share revised version when ready. N

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

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2016
CANADA'S BEST
DIVERSITY EMPLOYERS

Statement of Facts and Assumptions Sept 19 (3).pdf

Statement of Facts and Assumptions

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

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

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

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

(Source: OTPP.com)

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

- Teacher's Pension Act (TPA)
- Partners Agreement
- ~~Financial~~ Funding Management Policy (FMP)

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

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

Relevant Extracts from the TPA

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

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

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

Actuarial Valuation of the OTPP for accounting and funding purposes

[1] Partners Agreement, section 110.

Commented [HL1]: Is this accurate – nothing in the TPA says we represent employers.

Commented [RD2R1]: Agree.

Commented [RD3]: Not sure what this means; it would be more helpful to quote directly from the TPA or other sources (it seems to be more of a conclusion than a statement of fact)

Commented [RD4]: I believe there is matching in practice but I don't think it is mandated

Commented [RD5]: Not verified by us either

Commented [RD6]: Not sure they can say these are the *only* ways contributions would not be equal; and note that 5(1.1) does not technically say they must be equal.

Commented [RD7]: It provides a framework, but is by no means 100% prescriptive. Also the partners can deviate from the FMP by agreement.

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

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

According to the OTPP website, the most recent funding valuation reported a preliminary funding surplus of $13.2 billion on March 31, 2016.

Relevant Extracts from the Partners' Agreement

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

The Partner's agreement requires that when changes to the plan are required that the Partners negotiate how those changes are made in good faith (Paragraph ~~75~~74)

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

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

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

Relevant Extracts from the FMP

Commented [RD8]: We have not checked these figures.

Commented [RD9]: Note that this provision relates to changes flowing from a valuation that is to be filed with the regulators.

Commented [HL10]: Inaccurate: This applies to arbitration NOT mediation

The FMP is an appendix to the ~~partnership~~ partners' agreement that speaks to how the plan should be funded by both parties. The protocol for the use of surplus under the OTPP is detailed in the Funding Management Policy ("FMP") adopted by the Ontario Government and Ontario Teachers Federation as sponsors of the OTPP.

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

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

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

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

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

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

History of Surplus

The FMP was not established until 2003. The following is a summary of the history of how surpluses we treated before the FMP and post the FMP. The following is a summary of deficits over the year.

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	$4.6 billion to reduce the value of remaining special	$0

Commented [RD11]: I'd say it's broader than that; e.g. also deals with surplus utilization.

Commented [RD12]: 3.06(e) is not quite so prescriptive; e.g. it only speaks of "a reduction in contribution rates" but doesn't expressly say only down to the basic rate.

Commented [RD13]: Is that correct, or is it only the amount in excess of the 10% cushion?

Commented [RD14]: For a filing valuation, this is true – the parties must agree or go to mediation/arbitration. Arguably for any valuation that isn't being filed, either party can decide not to negotiate any changes and it would end there (that is our understanding).

Commented [Deloitte15]: Can this be confirmed as to whether the parties need to agree in order to reduce this cotnribution? Our understanding is that both parties do need to agree.

Commented [RD16R15]: We also interpret the FMP as requiring agreement to eliminate this special contribution.

Commented [RD17]: We didn't check this; we assume it was simply copied from the source.

		improvements	payments	
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 contributions	any changes to benefits or	$1.9 billion
Total		**$9.3 Billion**	**$9.3 Billion**	

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

Year	Valuation Status and Key Decisions
2003	$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary $6.1 billion shortfall was resolved, leaving plan with a $0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary $12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary $2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary $17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.
2012	$9.6 billion preliminary shortfall adjusted to reflect changes in mortality assumptions and impact of two-year freeze on teachers' salaries. 2012 shortfall resolved by making inflation protection for pension credit earned after 2013 fully conditional on plan's funded status and providing slightly smaller pension increases, beginning in 2014, for members who retired after 2009. These changes enabled the plan to assume a slightly higher discount rate. The changes left the plan with a $200 million surplus at Jan. 1, 2012.
2014	$5.1 billion preliminary funding surplus used to boost pensions of members who retired after 2009 to the level they would have been at if full inflation protection had been provided each year since they retired. The surplus funds were also used to raise conditional inflation protection to 60% of the increase in the cost of living for the portion of retirees' pensions earned after 2009. Both changes are effective with January 2015 pension payments.

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

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

Impact of Restoring Inflation Indexation

As noted above, a preliminary $12.7 billion plan shortfall in 2008 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 agreed to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation. In other words, employers and members shared in the outcome since the members would forego some benefits and the employers would also bear the cost to the extent of 50% of the missed inflation. These additional payments are often referred to as the "share the pain" payments. Despite the fact that the inflation protection was reduced, the cost of this protection has been fully reflected in the measurement of the accrued benefit obligation associated with the plan on the grounds that either the benefits would be restored and provided to pensioners or the "share the pain" payments would continue.

As also noted in the table above, plan surpluses arising in 2014-2016 are being used to restore some of the inflation protection that was reduced in 2008. This restoration of inflation protection is fully contemplated in the FMP under Section 3 describing the Restoration Zone. The direct impact of this action is that a portion of the "share the pain" payments that would otherwise be required have been eliminated. The estimated value of this reduction in contributions is $4.3 billion related to the 2016 action ($1.85 billion for 2015, and XX for 2014).

Commented [DK(-T18]: OPCD to make sure you agree with how I've worded this.

Commented [DK(-T19]: Amount outstanding

Commented [RD20]: We didn't verify this; we assume it all comes from the information cited above.

FW_ Update.rtf

From: Veinot, Cindy (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Update
Date: Thursday, November 03, 2016 18:03:55

-----Original Appointment-----
From: Colley, Matthew (CA - Toronto) [mailto:mcolley@deloitte.ca]
Sent: November-03-16 2:59 PM
To: Colley, Matthew (CA - Toronto); Danyluk, Kerry (CA - Toronto); Veinot, Cindy (TBS)
Subject: Update
When: November-04-16 10:30 AM-11:00 AM (UTC-05:00) Eastern Time (US & Canada).
Where: Skype Meeting

Hi everyone,

The purpose of the call is to connect on:

1. Summary of the opinion for communications
2. Release of the opinion to the panel.

Thanks

Matt

.....

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This is an online meeting for Skype for Business, the professional meetings and communications app formerly known as Lync.

Join by phone

+1-416-643-3390 (CANADA, Toronto) English (United States)
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+1-877-393-7360 Sans frais (CANADA, Toronto) French (Canada)
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[!OC([1033])!]

.....

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FW_ CSRA Number Pensions PWC - Security Clearance.rtf

From: Bernard, Dena (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: CSRA Number Pensions PWC - Security Clearance
Date: Friday, September 23, 2016 09:56:02
Attachment 1: image001.jpg

Hi Shyrose, Do we have the email addresses for the following people?

· Lucy Durocher- No record can be found of CSS having conducted a screening check for the individual.

· Martin Boucher- C-0035796, Clearance Expired 2016-04-14

· Sean Cable- No record can be found of CSS having conducted a screening check for the individual.

· Michael Walke- No record can be found of CSS having conducted a screening check for the individual.

Thanks

Dena

From: Bernard, Dena (TBS)
Sent: September 23, 2016 9:25 AM
To: Askcontractorscreening (TBS)
Subject: RE: CSRA Number Pensions PWC - Security Clearance

Thank you so much Thanusha. I really appreciate it.

Dena

From: Askcontractorscreening (TBS)
Sent: September 23, 2016 9:23 AM
To: Bernard, Dena (TBS)
Cc: Askcontractorscreening (TBS)
Subject: RE: CSRA Number Pensions PWC - Security Clearance

Hello Dena,

Please find the requested information below.

· Lucy Durocher- No record can be found of CSS having conducted a screening check for the individual.

· Martin Boucher- C-0035796, Clearance Expired 2016-04-14

· Sean Cable- No record can be found of CSS having conducted a screening check for the individual.

· Michael Walke- No record can be found of CSS having conducted a screening check for the individual.

Thank you,

Thanusha Gopalapillai
Program Analyst
Program and Policy Enablement Branch
Supply Chain Ontario | Ministry of Government and Consumer Services
222 Jarvis St., 7th Floor, Section A, Toronto M7A 0B6
416-212-4319

thanusha.gopalapillai@ontario.ca

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From: Bernard, Dena (TBS)
Sent: September 22, 2016 9:16 PM
To: Askcontractorscreening (TBS)
Subject: FW: CSRA Number Pensions PWC - Security Clearance

CSRA – 4oiope

Title – Pensions – PWC

Can you please tell me if the following people have clearance?

PWC

Lucy Durocher

Martin Boucher

Sean Cable

Michael Walke

I apologise in advance but hoping you can let me know as soon as possible. Can I call someone in the morning?

Thanks

Dena

From: Contractor Security Screening [mailto:AskContractorScreening@Ontario.ca]
Sent: September 22, 2016 9:06 PM
To: Bernard, Dena (TBS)
Subject: CSRA Number

Your CSRA number for the procurement, Complex Accounting - Pensions Asset Ceiling PWC, is: 4oiope. Please retain this number for your records. You will need to reference this number when submitting new Contractor Security Screening checks.

image001.pdf

M
G
C
S

FW_ CSRA Number Pensions PWC - Security Clearance.rtf

From: Bernard, Dena (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: CSRA Number Pensions PWC - Security Clearance
Date: Friday, September 23, 2016 09:24:17
Attachment 1: image001.jpg

FYI – for the file. We have to get clearance for 3 people

Lucy Durocher

Sean Cable

Michael Walke

Dena

From: Askcontractorscreening (TBS)
Sent: September 23, 2016 9:23 AM
To: Bernard, Dena (TBS)
Cc: Askcontractorscreening (TBS)
Subject: RE: CSRA Number Pensions PWC - Security Clearance

Hello Dena,

Please find the requested information below.

· Lucy Durocher- No record can be found of CSS having conducted a screening check for the individual.

· Martin Boucher- C-0035796, Clearance Expired 2016-04-14

· Sean Cable- No record can be found of CSS having conducted a screening

check for the individual.

· Michael Walke- No record can be found of CSS having conducted a screening check for the individual.

Thank you,

Thanusha Gopalapillai
Program Analyst
Program and Policy Enablement Branch
Supply Chain Ontario | Ministry of Government and Consumer Services
222 Jarvis St., 7th Floor, Section A, Toronto M7A 0B6
416-212-4319

thanusha.gopalapillai@ontario.ca

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From: Bernard, Dena (TBS)
Sent: September 22, 2016 9:16 PM
To: Askcontractorscreening (TBS)
Subject: FW: CSRA Number Pensions PWC - Security Clearance

CSRA – 4oiope

Title – Pensions – PWC

Can you please tell me if the following people have clearance?

PWC

Lucy Durocher

Martin Boucher

Sean Cable

Michael Walke

I apologise in advance but hoping you can let me know as soon as possible. Can I call someone in the morning?

Thanks

Dena

From: Contractor Security Screening [mailto:AskContractorScreening@Ontario.ca]
Sent: September 22, 2016 9:06 PM
To: Bernard, Dena (TBS)
Subject: CSRA Number

Your CSRA number for the procurement, Complex Accounting - Pensions Asset Ceiling PWC, is: 4oiope. Please retain this number for your records. You will need to reference this number when submitting new Contractor Security Screening checks.

image001.pdf

M
G
C
S

FW_ Call on cap and trade tomorrow.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Call on cap and trade tomorrow
Date: Monday, September 19, 2016 11:49:02

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: September 19, 2016 11:47 AM
To: Provis, Ian (TBS)
Cc: Virani, Shyrose (TBS); michael.hawtin@ca.pwc.com
Subject: Call on cap and trade tomorrow

Hi Ian,

We have a call on cap and trade scheduled for tomorrow at 10am. The call would be most effective if you and Nadine have had a chance to read the memo in detail and, in light of the timing of the Public accounts and the issues that I have been discussing with Nadine, I would understand if you have not yet had this chance.

Please let me know if you would like to reschedule this call for another time, we would be happy to accomodate.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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FW_ Call re_ Next Steps on Cap and Trade.rtf

From: Virani, Shyrose (TBS) []
To: Jack, Shannon (TBS) [Shannon.Jack@ontario.ca]
Subject: FW: Call re: Next Steps on Cap and Trade
Date: Tuesday, January 24, 2017 09:22:06

Hi Shannon

Pls. advise Cindy's availability.

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: January 24, 2017 8:09 AM
To: Petsche, Nadine (TBS)
Cc: Virani, Shyrose (TBS)
Subject: Re: Call re: Next Steps on Cap and Trade

Hi Nadine,

I am available at the following time - a call would be preferable.

This afternoon - Between 1pm-5pm

Tomorrow morning - Between 9:30am - 12:30pm

Thursday - between 11am and 2pm, or 3:30pm-4:30pm

Please let me know what works best.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2

http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
Date: 01/23/2017 09:09 PM
Subject: Call re: Next Steps on Cap and Trade

Hi Lucy.
We were wondering about your availability for a brief call to discuss the direction and next steps on the Cap and Trade accounting analysis. Please advise on your availability over the next couple of days to discuss with Cindy and myself. If more convenient, we can plan to meet via teleconference instead of in-person.
Thanks.
Nadine

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FW_ Cap and Trade.rtf

From: Virani, Shyrose (TBS) []
To: Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: FW: Cap and Trade
Date: Friday, September 30, 2016 09:35:26

From: david.c.greenall@ca.pwc.com [mailto:david.c.greenall@ca.pwc.com]
Sent: September 30, 2016 9:34 AM
To: Virani, Shyrose (TBS)
Cc: lucy.durocher@ca.pwc.com; michael.hawtin@ca.pwc.com
Subject: Re: Cap and Trade

Hi Shyrose - the invoice for effort spent since the last bill is in preparation and will be sent to you next week. As for level of effort forecast, I am not sure - suggest that we discuss this with Nadine and Ian on our next status call to get a sense as to their anticipated needs.

Thanks

David

David C. Greenall
PwC | Director, Sustainable Business Solutions
T: +1 613 782 2982
Email: david.c.greenall@ca.pwc.com
PricewaterhouseCoopers LLP
99 Bank Street, Suite 800, Ottawa ON K1P 1E4
http://www.pwc.com/ca

From: "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA, Michael Hawtin/CA/ABAS/PwC@Americas-CA, David C. Greenall/CA/ABAS/PwC@Americas-CA
Date: 09/30/2016 09:22 AM
Subject: Cap and Trade

Hello

We are in the process of preparing our budget and would like to know when your next billing on the above will arrive. So far you have billed us for $9129.27. I would really appreciate if you could provide me with the breakdown on how much you are planning to work on the above project for this fiscal which is ending on March 2017 and the next fiscal which starts from April 1, 2017 till your contract ends which would be in September 2017.

Your assistance would be greatly appreciate.

Thanks
Shyrose Virani

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FW_ _Confidential_ Re_ OSS-00426611-AppG-ConfidentialityAgreement-October2014.rtf

From: Virani, Shyrose (TBS) []
To: Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: FW: *Confidential: Re: OSS-00426611-AppG-ConfidentialityAgreement-October2014
Date: Friday, September 23, 2016 12:36:48

Lucy will send me confidentiality forms for all her staff

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: September 23, 2016 12:29 PM
To: Virani, Shyrose (TBS)
Cc: Bernard, Dena (TBS)
Subject: *Confidential: Re: OSS-00426611-AppG-ConfidentialityAgreement-October2014

Hi Shyrose,

I signed a confidentiality agreement for the cap and trade SOW and don't believe that I would need to sign another one, as the confidentiality agreement covers "each statement of work" pursuant to the agreement (the master agreement and SOWs) and already covers confidentiality for "any" services under the agreements.
Please advise if my interpretation of the wording in the confidentiality agreement is not correct.

I will ask Martin and Michael to sign the confidentiality agreement.

Sean Cable was listed on the SOW in the case that an accounting opinion was to be provided as a concurring reviewer. To date Sean has not been involved in any of the work and currently is not expected to be. Does this mean he should still sign a confidentiality agreement? Please confirm and I will arrange accordingly.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Bernard, Dena (TBS)" <Dena.Bernard@ontario.ca>
Date: 09/23/2016 09:34 AM
Subject: OSS-00426611-AppG-ConfidentialityAgreement-October2014

Hi Lucy

Can you please sign the attached Confidentiality Agreement and return it to me asap. Please back date it to when the contract was signed. Also, if you can please have Martin, Sean and Michael sign as well.

Thanks
Shyrose[attachment "OSS-00426611-AppG-ConfidentialityAgreement-October2014.docx" deleted by Lucy Durocher/CA/ABAS/PwC]

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FW_ Contact details.rtf

From: Virani, Shyrose (TBS) []
To: Jack, Shannon (TBS) [Shannon.Jack@ontario.ca]
Subject: FW: Contact details
Date: Thursday, June 08, 2017 09:38:32
Attachment 1: image001.gif

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: June 8, 2017 8:55 AM
To: Virani, Shyrose (TBS)
Cc: Sarah Anderton
Subject: Contact details

Hi Shyrose,

I'm preparing a document that needs to be addressed to Cindy and cc: Karen Hughes (Associate DM), Helen Angus (DM) and Nadine.

Could you please provide me full titles/mailing details/email addresses for everyone?

Many thanks,

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

FW_ EY Proposal - Public Sector Pension and Non-Pension Benefit Advice (TBS-OTB-OPCD-22).rtf

From: Donaldson, Mark (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: EY Proposal - Public Sector Pension and Non-Pension Benefit Advice (TBS-OTB-OPCD-22)
Date: Thursday, November 02, 2017 18:18:49
Attachment 1: image001.gif
Attachment 2: EY Proposal_TBS Pension and Non Pension Benefit Advice - Pricing (Schedule A).pdf
Attachment 3: EY Proposal_TBS Pension and Non Pension Benefit Advice - Technical.pdf

---

From: Mehnaz Thawer [mailto:Mehnaz.Thawer@ca.ey.com]
Sent: November 2, 2017 4:17 PM
To: Donaldson, Mark (TBS)
Cc: Uros Karadzic; Christina Chan
Subject: EY Proposal - Public Sector Pension and Non-Pension Benefit Advice (TBS-OTB-OPCD-22)

Good afternoon, Mark.

On behalf of EY please see the attached proposal for the above-noted RFS. Should you have any questions or concerns, please don't hesitate to contact Uros or Christina (cc'd on this email).

We would very much appreciate a **confirmation of receipt** at your earliest convenience.

We look forward to hearing from you.

Thank you kindly.

Mehnaz

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-

Mehnaz Thawer | Communications and Pursuits Strategist - Supervising Associate | Business Development

Ernst & Young LLP

Pacific Centre, 700 West Georgia Street, P.O. Box 10101, Vancouver , BC V7Y 1C7, Canada

Direct: +1 604 891 8308 | Mehnaz.Thawer@ca.ey.com

1668429

Website: http://www.ey.com

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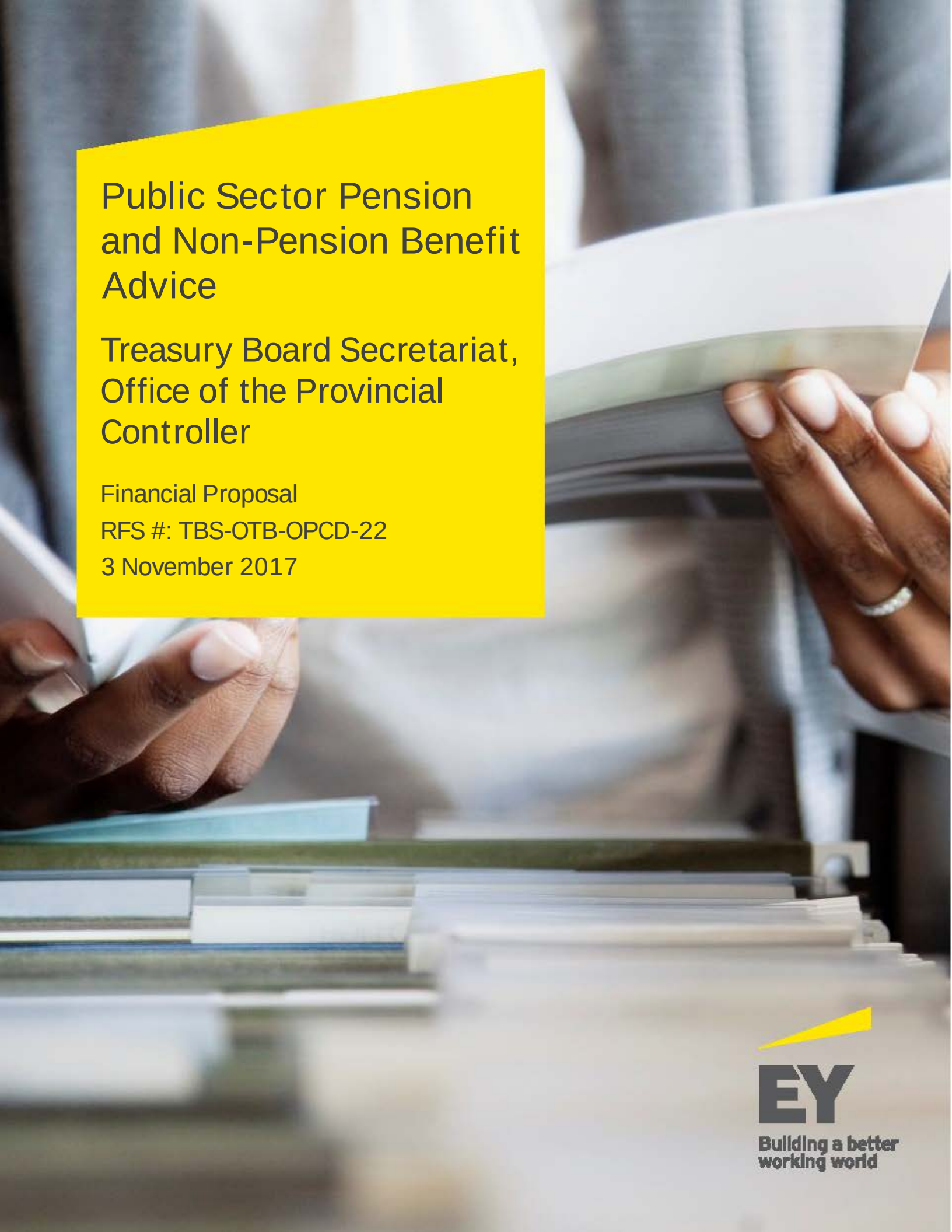
image001.pdf

EY Proposal_TBS Pension and Non Pension Benefit Advice - Pricing (Schedule A).pdf



Public Sector Pension and Non-Pension Benefit Advice

Treasury Board Secretariat, Office of the Provincial Controller

Financial Proposal

RFS #: TBS-OTB-OPCD-22

3 November 2017

EY

Building a better working world

Schedule A - Pricing Schedule

Please provide the following information in accordance with Sections 2.2.1 and 2.2.2 of this Request for Services:

Legal Name of Vendor: Ernst & Young LLP

Part A – Vendor Personnel

Complete the following table in respect of all proposed Vendor Personnel that will perform the Services and/or provide the Deliverables. Vendors should not include proposed Subcontractors in this Part A of Schedule A.

List the names of Consultants who will be assigned to the Project	Role and Experience Level
Uros Karadzic	Senior Consultant/ Project Lead
Christina Chan	Intermediate Consultant/ Project Analyst

Will Subcontractors be used for this Project? Yes [ ] No [X] If "Yes", complete Part B.

Part B – Vendor Subcontractors

Complete the following table in respect of the proposed Vendor Subcontractors at any tier of subcontracting, including any Vendor contractors that will perform the Services and/or provide the Deliverables.

Legal Name of Subcontractor	List the names of Consultants who will be assigned to the Project	Role and Experience Level
N/A	N/A	N/A
N/A	N/A	N/A

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Part C – Fixed Price

In the following table, enter the Fixed Price in respect of each role to be performed and the particular Deliverables to be provided, which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

For the purposes of bidding, the Ministry has estimated that 75 hours of effort is required for each role totalling 150 hours over the term of the Agreement. The Ministry reserves the right to alter the number of working days for each role as the project unfolds. The Ministry reserves the right to alter the number of working days at the time of award.

Fixed Price for each Core Deliverable	**Amount**
· One (1) Senior Consultant / Project Lead shall provide **75 hours** of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements.	$ 42,825 ($571/hour X 75 hours)
· One (1) Intermediate Consultant / Sr. Analyst shall provide **75 hours** of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements.	$ 25,875 ($345/hour X 75 hours)
Total Fixed Price:	$68,700

Part D – Other Expenses

In the following table, Vendors should list all expenses applicable to the Project that have not been included in the Total Fixed Price amount as stated in Part C of this Schedule A. Vendors should review the Travel, Meal and Accommodation Expenses section of the RFS prior to completing this table.

Expenses by Type *(List each item below):*	**Proposed Amount**
	$
	$
Total Other Expenses:	$

Part E – Maximum Price

In the following table, Vendors shall calculate Subtotal Price by adding Total Fixed Price, as stated in Part C of this Schedule A, to Total Other Expenses, as stated in Part D of this Schedule A.

Vendors shall calculate Maximum Price by adding the Subtotal Price to the applicable HST.

Subtotal Price (Part C + Part D):	$68,700
HST (if applicable):	$8,931
Maximum Price (Subtotal Price + HST):	**$77,631**

Part F – Follow-on Work Rates

In the following table, enter the **Hourly Rates** in respect of each particular Role to be performed which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

In the event that Follow-on work is requested, the Ministry will prepare a contract amendment to engage the consultant(s) for a specified duration and hours worked. Details on deliverables will be disclosed in the amendment as well.

Fixed Price for each Core Deliverable	Hourly Amount
· One (1) Senior Consultant / Project Lead	$571
· One (1) Intermediate Consultant / Sr. Analyst	$345

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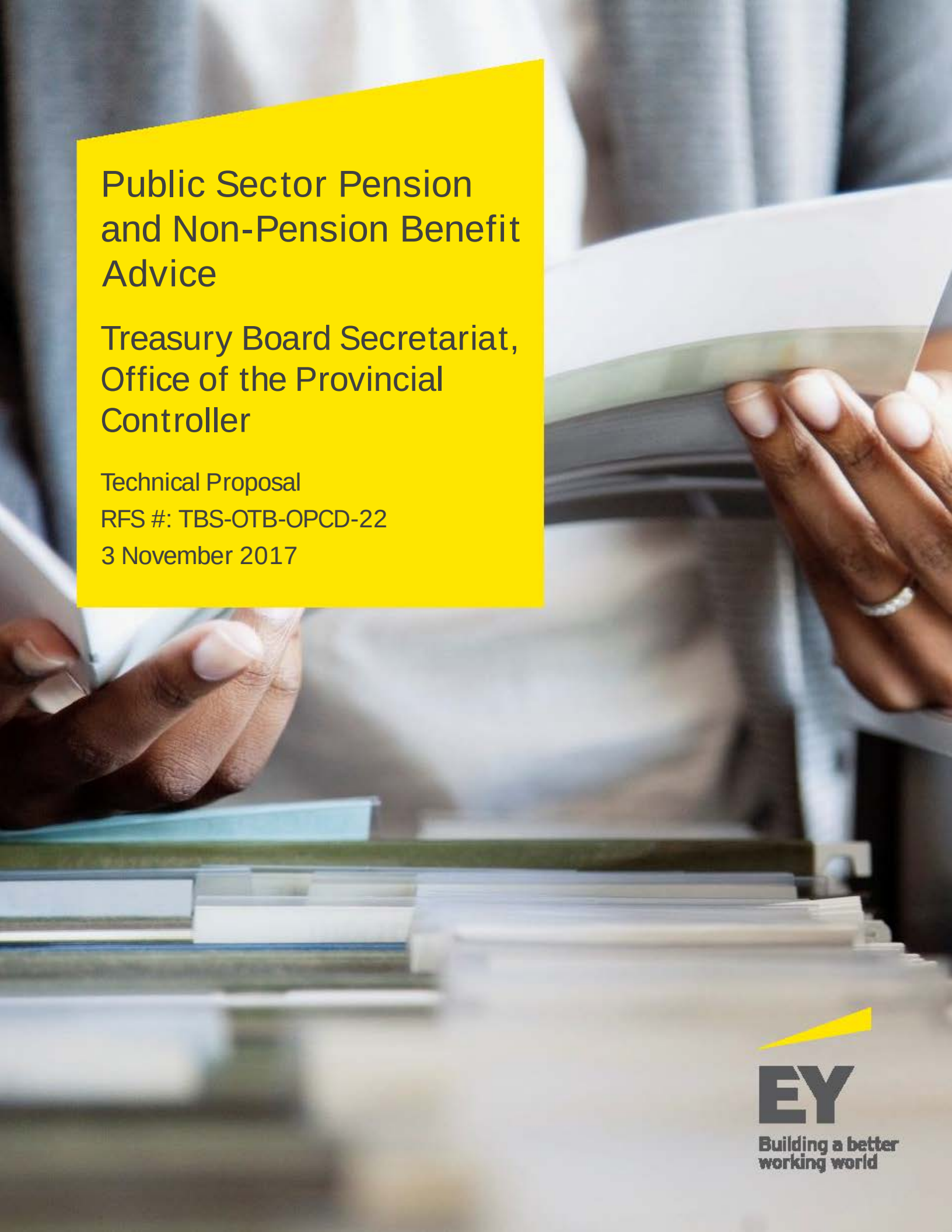
EY Proposal_TBS Pension and Non Pension Benefit Advice - Technical.pdf



Public Sector Pension and Non-Pension Benefit Advice

Treasury Board Secretariat, Office of the Provincial Controller

Technical Proposal

RFS #: TBS-OTB-OPCD-22

3 November 2017

EY

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Ernst & Young LLP
EY Tower
100 Adelaide Street West, PO Box 1
Toronto, ON M5H 0B3

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Mr. Mark Donaldson
Director
Treasury Board Secretariat, Office of the Provincial Controller
mark.donaldson@ontario.ca

3 November 2017

Request for Proposal for Public Sector Pension and Non-Pension Benefit Advice,
RFS# TBS-OTB-OPCD-22

Dear Mr. Donaldson,

Please find enclosed our technical proposal to provide services to the Treasury Board Secretariat, Office of the Provincial Controller related to Public Sector Pension and Non-Pension Benefit plans.

We look forward to continuing to work with you and welcome the opportunity to discuss our proposal and address any questions or concerns you may have. Please don't hesitate to contact us.

Best regards,

Ernst & Young LLP

Uros Karadzic, FSA, FCIA
Partner
416 943 2087
uros.karadzic@ca.ey.com

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In the event you receive an access to information or freedom of information request that could require disclosure of our proposal (or any other information provided by us in this context) please immediately notify us so that we may avail ourselves of any available protections or exemptions under the applicable legislation. Our proposal is being provided to you in confidence and includes commercially sensitive information, the disclosure of which, among other things, may significantly prejudice the competitive position of EY or be otherwise harmful to our business interests.

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"EY" as used in this proposal means the Canadian firm of Ernst & Young LLP or, as the context requires, other member firms of the global Ernst & Young network, each of which is a separate and independent legal entity.

Executive summary

We are pleased to put forward our proposal for actuarial services to the Treasury Board Secretariat (TBS), Office of the Provincial Controller Division (OPCD). We will support you in the preparation and review of pension and non-pension benefit expenses and liabilities of various benefit plans for which the Province is either a sole sponsor or a joint sponsor. These expenses and liabilities, determined by OPCD in accordance with Public Sector Accounting Standards (PSAS), are important for inputs reporting in various public documents.

EY has unparalleled knowledge and experience in the most important areas related to this project. Specifically, we bring:

- Deep and up-to-date understanding of PSAS as they relate to single and jointly sponsored public sector pension and non-pension plans
- Top-notch actuarial expertise and experience, with two of the most recognized and respected Canadian actuaries available to you as part of our team
- Familiarity and hands-on working experience with TBS and the OPCD team. This enables us to communicate our findings clearly, and assist TBS in interpreting and using the outcome of our work
- Ability to fine-tune our reporting and documentation approach for TBS in a way that is recognized by your stakeholders
- In-depth understanding of the key issues at hand, including asset ceiling interpretation, the importance of working with a variety of public sector stakeholders, the government financial reporting objectives of transparency and accountability, and the Ontario government's confidentiality requirements
- Provide directly applicable, useable and practical recommendations to TBS building off our familiarity with the reporting process at TBS

EY actuarial team

Your core EY resources for this project are Uros Karadzic as the project lead and Christina Chan as the intermediate consultant for this engagement. Both Uros and Christina have first-hand experience working with the TBS and OPCD.

Uros Karadzic is one of the most respected Canadian actuaries with deep knowledge and involvement in Canadian public sector pension accounting matters. He is a member of the PSAB's Employment Benefit Taskforce leading the review and revision of public sector accounting standards for pension plans in Canada. This means that he is both well-versed in the details of PSAS, and also aware of the key challenges with the standard that may be revised. He was a member of the Ontario Pension Asset Expert Panel in 2017.

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Both Uros and Christina have provided actuarial services to TBS previously, most recently supporting the team on the process related to compilation of inputs to the 2017/2018 Provincial Budget and the preparation of the 2016/2017 consolidated financial statements of the Province related to the pension plans in accordance with PSAS. They are cleared through the security requirements at TBS and their prior knowledge and experience allows them to initiate the project at full speed.

We recognize the needs of an engagement sometimes evolve and may require additional resources. Should there be additional service requests, need for an additional professional perspective, a change or extension in scope or urgent needs, we have the in-house capability to staff additional experienced resources as necessary to best serve TBS throughout this engagement:

Faisal Siddiqi: Faisal is a well-known and senior Canadian actuary who is joining our team on 13 November 2017 as an Associate Partner. He is an actuary with over 25 years of experience. Currently, Faisal is the Chair of Canadian Institute of Actuaries' Practice Council, member of the Financial Services Tribunal of Ontario, and member of Financial Services Commission of Ontario's (FSCO) actuarial advisory panel. He has provided actuarial advisory services related to many aspects of multi-employer, public sector and private sector benefit plans.

Gregory Winston: Greg is a Senior Manager at EY and an actuary with over ten years of experience. His primary focus includes actuarial audit support, due diligence and integration support on M&A transaction, and ongoing advisory services for both private and public sector clients. Greg has deep knowledge and experience with pension actuarial and accounting issues under PSAS and other accounting standards. He is a leading pension audit practitioner with many years of experience in reviewing actuarial assumptions, pension forecasts, accounting models and various specific issues including those related to asset ceiling calculations.

Our experience

Each year, our EY actuarial team provides actuarial services and audit support to over 250 audit entities with employee benefits programs. In addition to audit support, we provide actuarial services directly as the plan actuary. For most of our projects, our work includes developing reports with an executive summary, our findings and analysis both from the qualitative and quantitative perspective, and our recommendations, when applicable.

Our experience is demonstrated through our recent work in providing services for the following engagements:

- Treasury Board of Secretariat, Office of the Provincial Controller Division: Provided actuarial services to support the process related to compilation of input for the 2017/18 Provincial Budget and the preparation of the 2016/17 consolidated financial statements of the Province for its pension plans. In particular, we have reviewed the calculations prepared by TBS, clarifying information relied on by TBS, provided recommendations to improve the quality, usability, and consistency of the various calculation models used by TBS, advised on the interpretation of PS 3250 for both sole and jointly sponsored pension plans. We have also independently performed asset ceiling test analysis for two pension plans based on our interpretation and provided documentation on our procedure and recommendation. To conclude our prior engagement, we transferred knowledge by conducting three training sessions.

- Ontario Pension Asset Expert Panel: As a member, Uros's role included providing advice on the appropriate application of PSAS regarding pension accounting for the Province's jointly-sponsored pension plans, specifically with respect to asset ceiling and asset recognition.
- Federal Office of the Auditor General (OAG): Actuarial support to OAG as they audit federal Public Service Pension Plan (PSPP) liabilities. Uros has led this engagement for the past five audits, working closely with OAG and also the Office of the Chief Actuary (OCA) and the Office of the Superintendent of Financial Institutions (OSFI).
- Federal OAG and Provincial OAGs: Actuarial support for similar public sector audit related projects, such as OAG (Federal) – Canada Post Corporation; OAG (PEI) – Public Accounts; OAG (NL) – Public Accounts; OAG (NB) – Public Accounts; and OAG (Federal) – Via Rail, to name a few. The work often involved both actuarial and PSAS interpretation matters.
- OAG National Professional Practice Group: Provided on-call advisory services to the Federal OAG's Professional Practice on some of the most challenging actuarial and PSAS interpretation issues over the last five years.
- Treasury Board of Canada Secretariat: Provided assistance in the development of a funding policy proposal for the Public Service Pension Plan, including researching governance best practices relating to establishing funding policies in Canada and globally.
- Ontario Pension Board (OPB): Actuarial support for more than five years on the audit of the Public Service Pension Plan of the OPB. In particular, the work involves re-calculating the detailed actuarial calculations made by the OPB's actuary, to review methodology and valuation used to derive the employee benefit costs and balances.
- Ontario Pension Reform: by invitation, informed David Marshall's group on pension accounting impacts of pension reform alternatives, including how solvency and other funding requirements may impact pension accounting and asset ceiling calculations. Further, advised on possible changes to Pension Benefit Guarantee Fund (PBGF) in Ontario.
- Public Education Benefits Trust Fund (PEBT): Ongoing annual audit services for the review of the Core LTD Benefit Plan, including the review of the key economic and demographic assumptions, assessing the documentation of the assumption-setting process, and testing the actuary's valuation of the benefit obligations in accordance with the Canadian Institute of Actuaries (CIA) guidance.
- Canada Post Corporation Parliamentary Committee Testimony: Uros testified in front of a Parliamentary Committee on pension issues faced by Canada Post. The testimony was based on the EY report and analysis that looked at Canada Post's pension obligations and alternatives.
- Workplace Safety and Insurance Board (WSIB): Provided actuarial support, including the review of the benefits liabilities and funding status, the claims experience, the assumptions, sensitivity disclosed in the financial statement, and the methodology and the calculation of the benefits liabilities.

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- Ontario Hospitals: Provided audit support for the review of the non-pension post-retirement benefits (unfunded Plans) under PS 3250/3255 for a number of Ontario hospitals, such as Baycrest Centre for Geriatric Care, London Health Sciences, Woodstock General Hospital, Huron Perth Healthcare, and St. Joseph's Health Care London. Our audit review procedure includes assessing the appropriateness of accounting disclosures and assumptions under PS 3250/3255, discussions and review of the various methods used to determine each entity's cost of borrowing used as the basis for determining the discount rate assumption for unfunded plans.
- Newfoundland and Labrador English and French School Districts: Provided audit services for the review of the Sick Leave and Severance Plans, including the review of key economic assumptions, testing the actuary's valuation of benefit obligations under PS 3255 to confirm that the plan provisions are interpreted correctly, the actuarial assumptions are applied as disclosed, and the actuarial calculations have been carried out correctly.
- Canadian Institute of Actuaries taskforce on accounting discount rates: Uros has been a member of this taskforce since the financial crisis, setting and monitoring CIA's guidance on this important pension accounting topic.
- Directors College: Uros sits on the Advisory Board of Directors College and has taught a Pension Governance course to current and future corporate directors.

EY's Advisory Partners Council: bringing value to the TBS

In addition to the knowledge and experience of our actuarial team, we have selected senior EY partners to be part of our Advisory Partners Council for this engagement. The Advisory Partners Council brings together a diverse but complementary set of skills and experiences that, together with our actuarial team, will enable TBS to best benefit from the work undertaken through this project. By engaging the Advisory Partners Council at key times during the engagement, we will be able to ask key questions that help to strengthen the final results. Advice from the Advisory Partners Council members is a value-added service and will be included in the proposed fee for this engagement.

- Blake Langill: A senior Assurance Partner with more than 20 years of experience providing audit and advisory services to many of Canada's leading organizations. He was a part of our Professional Practice group, where he provided technical accounting and regulatory advice to audit and non-audit clients. Blake has experience in advising clients across various industries on the transition to US GAAP and/or IFRS and routinely deals with advising clients with complex accounting matters. His public sector experience includes an accounting advisory engagement with Infrastructure Ontario, as well as a current on-going engagement with TBS. *Blake brings specialist accounting and auditing knowledge and the current working experience with TBS.*
- Suzie Gignac: A senior Assurance Partner with over 20 years of experience providing assurance and advisory services to private and public sector clients. She participates on the Assets Task Force for the Public Sector Accounting Board of Canada which independently sets financial reporting standards critical to promoting confidence in public sector entities. Suzie is also a member of the Standards Council of Canada's (SCC) Governing Council, which is appointed by the federal government, and is Chair of the Audit Committee. *Suzie brings deep knowledge of public sector financial reporting and can help identify particular areas of focus that are relevant to accounting standards within the public sector.*

- Mark MacDonald: An experienced leader in public sector reform for dozens of governments worldwide in every major policy sector including health, human services, justice and security, finance and treasury, transportation and infrastructure, agriculture, trade and economic development, education and government services. *Mark brings a global view on some of the key questions that might need to be addressed, as well as a comparative perspective on best practices.*

We have the expertise both from accounting as well as advisory perspectives in the public sector and have many years of experience providing actuarial services relating to pension and other post-retirement benefits. We trust that our experience demonstrate our capability to carry out the services outlined in the RFS. We hope to be given the opportunity to apply those skills, as well as our knowledge of the issues at hand, to this engagement.

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About EY

EY is a global leader in assurance, tax, transaction and advisory services. We are 250,000 colleagues serving clients in the public and private sectors worldwide. EY Canada has 16 offices across the country with approximately 5,000 professionals.

We take great pride in the long-standing working relationships we have developed with our government clients, and have earned an excellent reputation through demonstrated commitment to understanding their business needs and delivering high quality services.

EY has invested in knowledge, resources, and technologies to help support both our clients and our professionals worldwide, bringing broad and deep understanding of actuarial services similar to those required by TBS. We have decades of experience providing actuarial services including employee benefits actuarial valuations. Our actuarial practice has more than 1,200 professionals globally with 25 located across Canada and ready to serve TBS.

Submission requirements

Experience and qualifications

Previous experience

As a global firm, we are able to leverage the knowledge, qualifications and experience from our professionals across the country and around the globe. For ease of evaluation, we have provided a project grid demonstrating the Team Leads' cumulative work experience in all the elements identified by TBS.

Experience	Treasury Board Secretariat, OPCD	Ontario Pension Asset Expert Panel	PSAB Taskforce	Ontario Pension Board	EY PPG/ OAG NPPG	Audit Support/ OAG PSPP	Treasury Board of Canada Secretariat	Canada Post Corporation
A) Current or past experience with similar projects, with examples of successful outcomes, anticipated challenges, and corresponding mitigation strategies	ü	ü	ü	ü	ü	ü		
B) Pension actuarial experience with the Ontario Government or other senior Canadian Governments	ü	ü	ü	ü	ü	ü	ü	ü

Experience	Treasury Board Secretariat, OPCD	Ontario Pension Asset Expert Panel	PSAB Taskforce	Ontario Pension Board	EY PPG/ OAG NPPG	Audit Support/ OAG PSPP	Treasury Board of Canada Secretariat	Canada Post Corporation
C) Demonstrated knowledge, skills, experience and expertise with developing reports with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative of a public pension related initiative and any recommendation made as part of the report	ü	ü		ü		ü	ü	ü
D) Demonstrated knowledge, skills, experience and expertise with running different ceiling tests and sensitivity analysis scenarios including providing ceiling tests and sensitivity analysis advice	ü	ü	ü		ü	ü		

The following detailed project summaries demonstrate our current and past experience with the Ontario Government, the government of Canada and other provincial governments, in performing actuarial activities as outlined in the RFS for projects that are similar in size, nature and scope.

For each project, we have also included description of the type of reports delivered. Generally, our reports include an executive summary, an overview of our methodology, analyses, recommendations, and information we relied on.

Project #1: Ontario Treasury Board Secretariat, Office of the Provincial Controller	
Brief project description	EY provided actuarial services to support the process related to compilation of inputs for the 2017/18 Provincial Budget and the preparation of the 2016/17 consolidated financial statements of the Province for its pension plans, including asset ceiling test analysis.
Successful outcomes	By assessing the reasonability and providing recommendations on enhancements to the calculations, the EY actuarial team provided additional quality control for TBS prior to signing off the accounting reporting for the Province's pension plans. We independently performed analysis on asset ceiling test for the two pension plans in an accrued asset position based on our interpretation of PSAB 3250. Our independent analysis is considered and referenced by TBS in confirming their interpretation of the standard.

Anticipated challenges and mitigation strategies	Key challenges include the complexity of the models used by TBS, the potential misinterpretation of information received from different data source and/or inappropriately applied to the models, the various plan provisions and plan-specific considerations, and the lack of clarity regarding asset ceiling requirements under the PSAS. These risks are mitigated by detailed review of the models, discussions with project staff and developed thorough understanding of the plans, including requesting additional information from third-parties as necessary (e.g. plan actuaries, pension board, etc.).
Type of reports delivered	Asset ceiling test: report with an executive summary and detail outlining the calculation of the asset ceiling determined under PSAS per our interpretation. Summary description of our work related to the models used by OPCD to prepare the pension accounting results.
Relevance to TBS project deliverables	We believe the RFS is partly a continuation of work performed. Our prior engagement allows us to start the project immediately with minimal transition or kick-off effort. Building off our familiarity of stakeholders' priorities, the extensive knowledge of the plans and models, as well as our understanding of TBS' working preference, we are equipped to carry out the project effectively and seamlessly.

Project #2: Ontario Pension Asset Expert Panel	
Brief project description	As a member of the Ontario Pension Asset Expert Panel, Uros' role included providing advice on the appropriate application of PSAS regarding pension accounting for the Province's jointly-sponsored pension plans, specifically with respect to asset ceiling and asset recognition.
Successful outcomes	A report on the Panel's recommendations and reasoning.
Anticipated challenges and mitigation strategies	There are a number of challenges, including the lack of clarity regarding asset ceiling requirements under the PSAS, managing differing viewpoints among various stakeholders, and interpreting accounting rules in the context of the actuarial valuations and asset ceiling calculations. These challenges are mitigated by careful thought, analysis and broad consultations.
Type of reports delivered	Report with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative sources. The report is related to a public pension related initiative and the Panel's recommendations are part of the report. The report provides analysis and advice related to ceiling tests and sensitivity analysis.

Relevance to TBS project deliverables	The work of the Expert Panel deals directly with the subject matter of the RFS. The participation on the Expert Panel will allow Uros and the team to hit the ground running as they will be familiar with the issues and the context of the work.

Project #3: PSAB's Employment Benefit Taskforce	
Brief project description	Uros is a member of the PSAB's Employment Benefit Taskforce leading the review and revision of public sector accounting standards for pension plans in Canada.
Successful outcomes	Participation on the PSAB Taskforce means that our team is both well-versed in the details of PSAS, and also aware of the key challenges with the standard that may be revised.
Anticipated challenges and mitigation strategies	Reviewing and revising the accounting standards is a significant and complex undertaking. The Taskforce therefore brings together senior professionals from different areas of practice. Uros contributes his actuarial and pension accounting knowledge and experience in the complex and challenging task.
Type of reports delivered	The PSAB Taskforce report and recommendation will deal with many aspects of pension accounting in the public sector, including pension asset ceiling issues and calculations.
Relevance to TBS project deliverables	Participation in the PSAB Employment Benefit Taskforce provides our team with deep and cutting-edge understanding of PSAS as they related to pension assets and liabilities. This includes the issues with asset and liability measurement, as well as asset ceiling calculations.

Project #4: Ontario Pension Board	
Brief project description	EY has provided actuarial audit services for more than five years on the audit of the Public Service Pension Plan (PSPP) of the OPB. In particular, we re-perform the detailed actuarial calculations made by the OPB's own actuary, to review methodology and calculations used to derive the employee benefit costs and liabilities.
Successful outcomes	The EY actuarial team provides the OPB's auditors with actuarial analysis and advice needed to sign off on OPB's actuarial liabilities. We identify actuarial valuation issues and provide recommendations on improvements to OPB.
Anticipated challenges and mitigation strategies	Key challenges include the complexity of the PSPP plan provisions and data, the appropriate interpretation of plan rules, and the correct application of actuarial assumptions and valuation methods to arrive at the actuarial liability. These risks are mitigated by application of EY's actuarial valuation tools, our professional knowledge and experience, and coordination with the various stakeholders (including auditors, plan actuaries and the OPB management) to resolve any differences.

Type of reports delivered	We provide a formal report to document our findings. This report presents a summary of key findings, analysis of the information collected from the qualitative and quantitative aspects of a public pension related initiative, narrative of the testing procedures, and any recommendation made as part of the report.
Relevance to TBS project deliverables	The work we perform for OPB involves design and execution of actuarial valuation models. The work is done in a context of a large and complex public service pension plan, and it requires both the actuarial knowledge and the experience in interpreting and applying accounting standards to pension plans. This experience enables us to assist TBS with the review of APFR's calculation of estimated accounting valuations based on actuarial input for pension plans reflected on the Province's various reporting.

Project #5: EY Professional Practice Group (EY PPG)/OAG National Professional Practice Group (NPPG)	
Brief project description	The EY team provides the Federal OAG's National Professional Practice Group with on-call advisory services on employee benefits actuarial and accounting issues under PSAS and IFRS. Issues discussed included actuarial valuation, discount rates, mortality assumptions, accounting for shared risk plans, asset ceiling and IFRIC 14 interpretation, asset and liability recognition and measurement, etc. The questions addressed are usually of a highly complex nature. Our team also provides the same type of advice to EY's own Professional Practice Group as well as individual audit teams.
Successful outcomes	EY provides resolution of the most complex accounting and actuarial questions, related to a wide range of PSAS and other standard interpretation issues. We provide technical and practical advice on actuarial matters, including issues related to valuations, asset and obligation measurement, and asset ceiling computations.
Anticipated challenges and mitigation strategies	Key challenges relate to the highly complex nature of the issues encountered, including issues with no practice or precedent. The resolution of these issues is sought through careful analysis, deep understanding of the standards, and diligent care taken to understand and agree on the facts and circumstances of each situation.
Type of reports delivered	The results of our analysis are provided through the means that best meet the clients' needs. The actuarial support and the accounting advice we provide, including the advice related to asset ceiling calculations and sensitivity analysis scenarios, is provided in formal reports, memos, or email and telephone calls.
Relevance to TBS project deliverables	Our team can provide high quality advice and subject matter expertise to APFR as our experience with this type of actuarial and pension accounting work is extensive. We routinely engage in complex discussions with many internal and external stakeholders, often with differing views. Our team has extensive experience of

	working with the Federal OAG and Provincial OAGs, as well as EY Professional Practice, experience that would directly benefit TBS on this project.

Project #6: Audit Support/OAG Public Service Pension Plan (PSPP)	
Brief project description	EY provides actuarial assistance to the federal OAG as they audit federal PSPP liabilities. In particular, we assess the appropriateness of actuarial assumptions and methods, accounting treatment and disclosure of PSPP's obligations and costs, assess the reasonableness of the sensitivity analysis. EY has provided these actuarial expertise to OAG for the past five audits, working closely with OAG and also the Office of the Chief Actuary (OCA) and the Office of the Superintendent of Financial Institutions (OSFI). In addition, our team provides actuarial services and audit support to over 250 audit entities including many with significant pension liabilities both in the public and private sector. In this context, we routinely interpret and apply asset ceiling tests under both PSAS and IFRIC 14.
Successful outcomes	The EY actuarial team provides the necessary actuarial analysis and advice needed for the auditors (EY and OAG) to sign off on the significant pension and post-retirement benefit liabilities under both PSAS and other accounting standards. Our work routinely addresses issues related to asset ceiling interpretation and calculation.
Anticipated challenges and mitigation strategies	Challenges involve the lack of clarity (PSAS) or the complexity (IFRS) in the interpretation of asset ceiling rules as they relate to the limit on a defined benefit asset under the applicable standards. Mitigation strategies involve a comprehensive analysis of the relevant accounting standards, plans facts and circumstances, discussions with knowledge experts from diverse backgrounds and their interpretations to address issues related to these large, complex plans that are of interest to many stakeholders.
Type of reports delivered	We provide a formal report to document our findings. This report presents a summary of key findings, analysis of the information collected from the qualitative and quantitative aspects of a public pension related initiative, narrative of the testing procedures, and any recommendation made as part of the report.
Relevance to TBS project deliverables	The work we perform for the federal OAG in respect of PSPP and on numerous EY audit client enables us to develop and execute various actuarial valuation models quickly. Our approach is tailored to purpose. We do not approach these actuarial valuations in the same manner that the plan actuary would, but rather develop models that are suitable to the analysis, scenarios or sensitivity modelling required. This often means that we exercise our judgement and experience to focus the analysis on the key elements enabling decision making, in the context that is similar to the development of the Province's Budget and the consolidated financial statements.

	The large number of clients we serve in this capacity puts us in a position to see many more different plans, valuations, and asset ceiling issues than a typical plan actuary.

Project #7: Treasury Board of Canada Secretariat /Public Service Pension Plan	
Brief project description	EY assisted TBS of Canada in the development of a Funding Policy including performing pension industry research on funding policy trends and commentary and advice on funding policy proposals. We prepared a research report outlining funding policy examples, elements and approaches; consideration of rules/limits-based versus risk-based funding policy; trends related to funding policies; impact of legislative environment; and considerations of provisions, demographics and actuarial methods applied in funding policies.
Successful outcomes	We have assisted TBS of Canada in successful development of a funding policy proposal that balanced many competing priorities and had to take into account varying views of many different stakeholders. Federal PSPP is a large pension plan sponsored by a senior Canadian government. Our work demonstrated our ability to be responsive and respectful of these differing perspective, while supporting the client in achieving their strategic objective.
Type of reports delivered	Our research report noted the key funding policy insights and themes based on Canadian and international best practices, pension industry regulatory guidelines and the review of approaches taken by other Canadian sponsors of significant pension plans. The findings of our report were considered and incorporated into the Final Policy Statement in all material respects. Further, our written comments, provided based on our review of the three draft funding policy statements, were considered and included in the Final Policy Statement, where appropriate. Overall, our assistance in preparing the Final Policy Statement presents a comprehensive and well-drafted funding policy that can help meet the governance objectives of the public sector pension plans. The Final Policy Statement, in its level of detail and sophistication provides a relevant and robust governance framework for these large, complex plans that are of interest to many stakeholders.
Relevance to TBS project deliverables	We can utilize our prior experience of assisting TBS of Canada on the development of the Funding Policy. Our report on that project demonstrated knowledge, skills, experience and expertise with developing reports with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative aspects of a public pension related initiative, similar to the services requested by TBS.

Project #8: Canada Post Corporation Parliamentary Committee Testimony	
Brief project description	Uros testified in front of a Parliamentary Committee on pension issues faced by Canada Post, more specifically highlighting the factors that led to the large pension liability issues faced by Canada Post.
Successful outcomes	EY assisted the Parliamentary Committee to understand the issues facing Canada Post, including significant issues related to pension liabilities.
Type of reports delivered	EY assisted an independent taskforce appointed by the Minister of Public Services and Procurement in their responsibility of the review of the Canada Post Corporation. EY provided this taskforce with a report containing independent analysis of Canada Post's financial position and projections on pension related matters. As part of this mandate, our report presented as a discussion paper that outlined viable options for the future of Canada Post Corporation.
Relevance to TBS project deliverables	Our team can provide skills, experience and expertise with developing reports with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative aspects of a public pension related initiative and any recommendation made as part of the report. We routinely engage in complex discussion with many internal and external stakeholders, often with differing views, bringing unparalleled experience in providing services similar to the services required by TBS.

Methodology and implementation plan

Our approach and methodology will be flexible and geared toward meeting your objectives and timelines. As a general principle, we will work with you to understand your requirements and validate our methodology and understanding of the deliverables. We will then work with you to meet those requirements under the timelines laid out in the engagement.

The following outlines our key project management elements and approach taken by the actuarial team in delivering our services to the TBS, based on the requirements of the RFS.

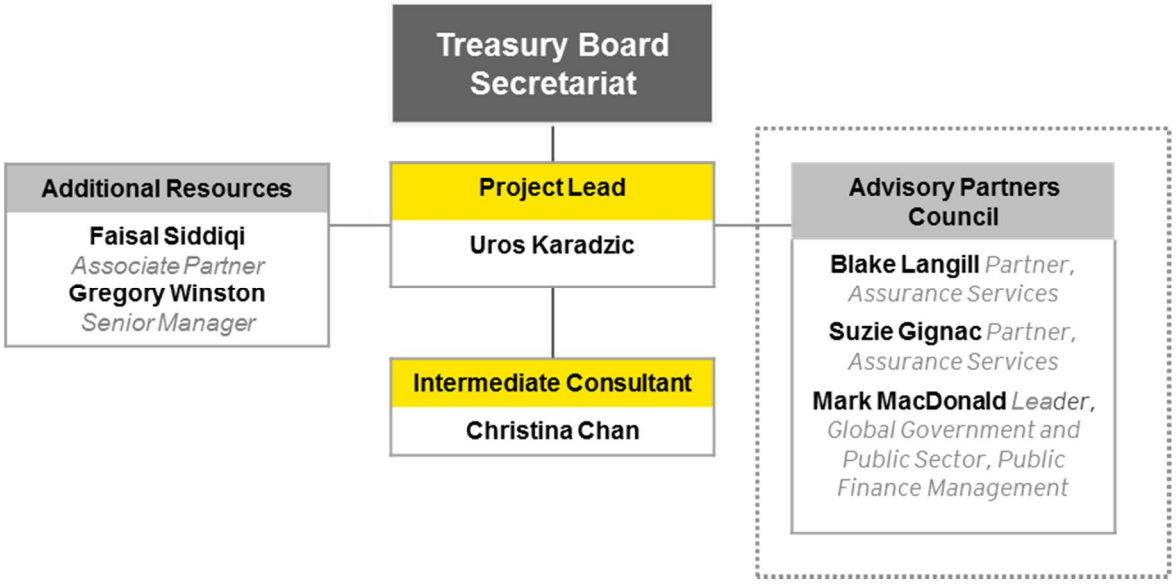
1.	Define expectations of the services required, including scope of work, timing, and expected effort required with a timeline for specific deliverables and milestones over the course of the engagement
2.	Collect data, analysis and documentation as necessary to complete the deliverables in a timely manner, such as plan provisions, assumptions, details of existing calculations and analysis, and any other documentation and data
3.	Review the economic assumptions used for accounting valuations, actual and forecast numbers prepared by APFR's staff for the Province's various pension and non-pension plans.
4.	Perform asset ceiling test in accordance with requirements under PSAS and any sensitivity analysis as required
5.	Identify and recommend potential improvements based on our review and analysis
6.	Participate in discussions and meetings with internal and external stakeholders as required
7.	Advise on any accounting issues related to pension and non-pension benefits as required
8.	Report our findings, analysis and recommendations in a document
9.	Transfer knowledge to the OPCD staff in an agreed upon and effective approach

In addition to the knowledge and experience of our actuarial team, we have selected senior EY partners to be part of our Advisory Partners Council for this engagement. This Advisory Partners Council would assist you and our actuarial team in matters related to PSAS interpretation, the review of the work product, and assisting with the interpretation and application of the work product to best support TBS throughout the engagement. The Council will help ensure that strategic issues are considered accordingly, including but not limited to stakeholder impacts, public policy implications and the Province's fiscal priorities.

Proposed resources

Core team

We selected team members that fulfil the necessary skills, qualifications and experience as described in the RFS. A diagram of our team structure is depicted below, followed by a brief description of our proposed team resources. Additional information on our team is attached in Schedule B – Resumes and references.



Uros Karadzic, Project Lead/Senior Consultant: Uros is the national leader of EY's Reward practice, and is an actuary with more than 18 years of experience. He specializes in pension accounting and audit; pension and benefit issues in merger & acquisition transactions; and on-going advisory services on retirement benefit plans. Uros has advised clients (Canadian and multinational) on all aspects of their pension and benefit plans, including accounting, funding, design, implementation, management, risk and administration. He has assessed and developed strategies, policies, guidelines, cost models and processes to identify, manage and reduce costs and risks to organizations related to these issues. Uros' responsibilities throughout the engagement will include direct engagement and oversight of all aspects of work, including the review of final deliverables before submission.

Christina Chan, Intermediate Consultant: Christina is an actuary with over nine years of experience. Her primary focus is on providing advice on pension and benefit plans, funding and accounting valuations and human resources transaction due diligence for employee benefit plans. During her last engagement with TBS, she provided substantial recommendations and assisted with the implementation process of improvements to the accounting reporting and forecasting models, which result in enhancements to both the usability and estimation approach of the models.

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Other actuarial resources

We recognize that needs of an engagement sometimes evolve and require additional input. This is why we have included our other actuarial resources below to demonstrate that we have the in-house capabilities necessary to perform the work and provide additional professional actuarial input and perspective:

- Faisal Siddiqi: Faisal is a well-known and senior Canadian actuary who is joining our team on 13 November 2017 as an Associate Partner. He is an actuary with over 25 years of experience. Currently, Faisal is the Chair of Canadian Institute of Actuaries' Practice Council, member of the Financial Services Tribunal of Ontario and a member of FSCO's actuarial advisory panel. He has provided actuarial advisory services related to many aspects of multi-employer, public sector and private sector benefit plans.

- Gregory Winston: Greg is a Senior Manager at EY and an actuary with over ten years of experience. His primary focus includes actuarial audit support, due diligence and integration support on M&A transaction, and on-going advisory services for both private and public sector clients. Greg has deep knowledge and experience with pension actuarial and accounting issues under PSAS and other accounting standards. He is a leading pension audit practitioner with many years of experience in reviewing actuarial assumptions, pension forecasts, accounting models and various specific issues including those related to asset ceiling calculations.

Advisory Partners Council

We have selected senior EY Partners to be part of our Advisory Partners Council for this engagement that will provide advice on a requested basis, based on their experience in Canada and across the globe in similar engagements. We have provided a brief overview of each council member's area of expertise. Advice from the Advisory Partners Council is a value-added service and will be included in the fee for this engagement:

- Blake Langill: a senior Assurance Partner with more than 20 years of experience providing audit and advisory services to many of Canada's leading organizations. He was a part of our Professional Practice group, where he provided technical accounting and regulatory advice to audit and non-audit clients. Blake has experience in advising clients across various industries on the transition to US GAAP and/or IFRS and routinely deals with advising clients with complex accounting matters. His public sector experience includes an accounting advisory engagement with Infrastructure Ontario, as well as a current engagement with TBS. *Blake brings specialist accounting and auditing knowledge and the current working experiences with TBS.*
- Suzie Gignac: a senior Assurance Partner with over 20 years of experience providing assurance and advisory services to private and public sector clients. She participates on the Assets Task Force for the Public Sector Accounting Board of Canada which independently sets financial reporting standards critical to promoting confidence in public sector entities. Suzie is also a member of the Standards Council of Canada's (SCC) Governing Council, which is appointed by the federal government, and is Chair of the Audit Committee. *Suzie brings deep knowledge of public sector financial reporting and can help identify particular areas of focus that are relevant to accounting standards within the public sector.*

- Mark MacDonald: an experienced leader in public sector reform for dozens of governments worldwide in every major policy sector including health, human services, justice and security, finance and treasury, transportation and infrastructure, agriculture, trade and economic development, education and government services. *Mark brings a global view on some of the key questions that might need to be addressed, as well as a comparative perspective on best practices.*

Communications and reporting

Ongoing communications with stakeholders and regular status updates are critical to project success. Based on our prior experience with TBS, we have incorporated weekly project status update emails (or meetings as appropriate) into our implementation plan and will confirm timing and content for written updates with the TBS project manager at the beginning of the project.

Status reports, which are used to report on performance, will help facilitate regular communications between team leads, the project manager, leadership and stakeholders. They will detail activity status, including risks, assumptions, issues and dependencies. Their goals will be to provide the following:

- Serve as an early warning system to team members which would allow them to adjust their work effort accordingly
- Provide an assessment of project performance on an ongoing basis relative to plans, objectives, and staffing
- Support the identification of corrective strategies to deal with issues identified during the assessment which may impact project timelines or performance

The common elements of status reports are:

- Project health: Summary of the project's health status (e.g., cost, schedule, scope, resource); this is derived from the individual status reports submitted by the team members to the team lead, including feedback from full-time ministry staff working in an integrated fashion with EY
- Individual project progress assessments: Narrative overview of project status including work completed; work in progress; planned key milestones, activities and/or events (e.g., the executive summary)
- Issues: Summary of major events that may impact the delivery of the project
- Risks: Summary of major, uncertain events or circumstances which, should they occur, will impact the project
- Project change requests: Summary of modifications that were identified, resolved or rejected
- Project milestones: Summary of progress based on significant points or events with information on description and due date
- Deliverables: Summary of completed client work products

The engagement lead will consolidate and summarize status information for scheduled status meetings, other leadership meetings and stakeholder reports, as required.

Contingency plan

We recognize that during the course of an engagement, unforeseen circumstances can have significant effects on the project timeline or resources. As a large, multinational firm that provides advisory services for assignments of all sizes, we are experienced at identifying, mitigating and correcting a host of scenarios that may impact a project.

To account for these factors, we build flexibility in our work plans. This can include, for instance, accelerating certain components of the work to balance the delay in others, with the overall goal of staying on track. More critically, we communicate with you regularly so that you are made aware of any delays and we work with you to find the best solution to mitigate.

Based on our experience the following are some of the risks associated with a project of this nature. We have identified the respective mitigation/management strategy for each risk. Working with the TBS team, we will validate these risks and identify and manage others throughout the lifecycle of the engagement.

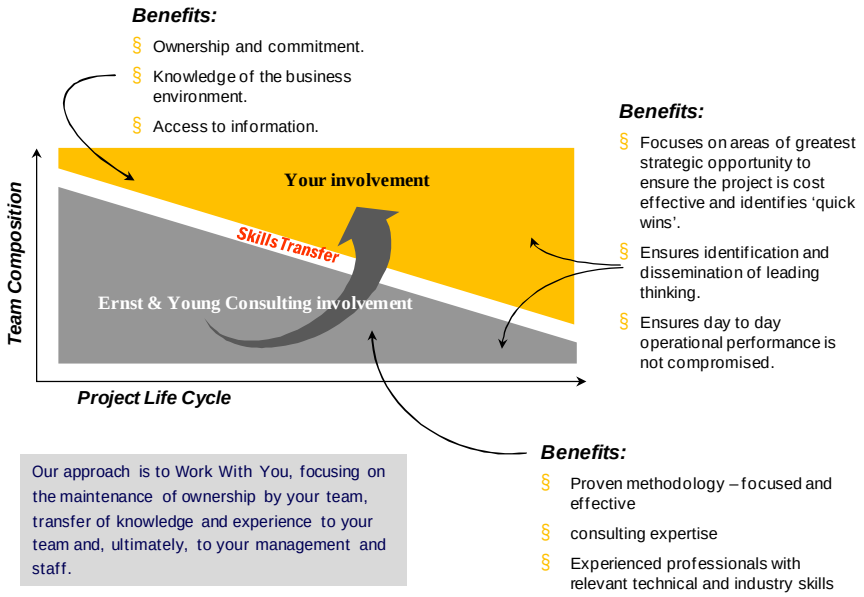
Risks	Mitigation/management
Access to necessary documentation and data in a timely manner	► During launch phase, we will create an inventory of documents and data that will be required as part of the engagement ► Where documentation does not exist or data is not currently housed, we will deploy other methods to collect the information required
Access to key stakeholders in a timely manner	► During the initiation phase, we will identify the stakeholders who we will need to meet with as part of the engagement ► We will arrange our activities based on availability of stakeholders
Changes to scope of the project	► Develop a change management process and incorporate the protocol for identifying, managing and approving any possible changes to the original scope
Communications and disclosure	► Provide clear documentation and appropriate disclosures to ensure our deliverables will not be misinterpreted ► Identify any limitation or additional advice from other sources (e.g. legal advice) may be required ► All actuarial opinions and advice will be in writing and signed by a Fellow of the Canadian Institute of Actuaries ► All accounting opinions and advice will be in writing and signed by a Chartered Professional Accountant
Availability of team resources	► Develop a detailed project plan outlining team resources and manage the resource schedule to identify any potential staffing conflicts ► Should any changes be required, we will propose a replacement staff ahead of time with similar of better qualifications for your approval and at no cost to you

Knowledge transfer

We understand that various stakeholders will have different roles and levels of responsibility and will require different types of knowledge, modes for delivery, and availability to gain such knowledge. EY is committed to delivering the full benefits of knowledge-sharing with our clients. Our strong commitment to collaborating with clients helps facilitate the transfer of knowledge in an effective way. In transferring knowledge to project resources we use a structured approach that includes:

- Working with project team members to define knowledge transfer plans
- Providing hands on training and walk-through sessions on any proposed improvements to existing tools
- Providing overviews of methodologies and approaches
- Reviewing progress against knowledge transfer plans

During the project, it is important that the knowledge, techniques and processes employed in the analysis and review are adequately transferred to the client to ensure that you have future continuity of the improvement process and allow for continued momentum. Below is a diagrammatic representation of our knowledge transfer approach.



Based on our understanding of your situation, our knowledge of the TBS objectives and our experience in providing actuarial support services, we will tailor an approach that aims to maximize all efforts, manage cost and achieve multiple objectives in parallel. The best way for this transfer to happen is to create a structured process. Accordingly, we will work with your project team members to develop knowledge transfer plans that outline the specific skills and capabilities to be transferred and the activities required to close the knowledge gap. Specific elements of the plan include:

- Knowledge transfer action plan
- Evidence of successful knowledge transfer – Identifies performance criteria that indicate development of specific knowledge/skills
- Assessment rating – Identifies the target assessment "rating" for identified knowledge/skills to be transferred

Performance management process

The methodology for maintaining overall engagement quality is EY's Quality Assurance approach. The foundation of all of EY's engagements is built on delivering a high quality engagement experience to our clients. We have built in checks and balances throughout our work plan and the EY core delivery team will work collaboratively with OPCD's project leadership team to ensure all deliverables are completed in agreed upon timeframes.

EY's quality process requires our partners and senior management to participate directly on a timely basis in the performance of our work and the supervision of our professionals. As the project lead, Uros will serve as the final quality check and will sign off on all deliverables to the TBS.

Direct participation of EY management means involvement in the actual performance of the work relating to a particular area. This may range from effective direction and supervision, usually on-site, of team members performing the tasks and generally will involve direct contact with key client personnel. Normally, the time spent by EY management in directly participating in the project will be offset by reduced time spent in the creation and review of working papers, including the time-consuming process of writing and clearing review comments.

The primary objectives of these reviews and supervision procedures, from a quality assurance perspective, are to determine the following:

- Project has been planned appropriately
- Scope of the project is sufficient to support our report
- Work has been performed in accordance with the standards of our firm and the profession
- Significant judgments made and conclusions reached throughout the project were appropriate work performed and the results and conclusions are adequately documented

Our previous work with the TBS and other government bodies has given us a continuous improvement process that takes into account the MGCS and client standards, processes and policies. EY will put in place the required management procedures to confirm that quality is embedded into all deliverables in compliance with the expectations put forth in the Statement of Work based on this RFS.

Additional submission requirements

Deliverables and milestones

As majority of Client Requirements described in the RFS refer to working with management to provide various aspects of actuarial support services as required, the deliverables and milestones will be dictated by management as required. We will be available to commence work on December 4, 2017 as required, and complete the work by March 2018.

We anticipate that, subject to management's request, we will be preparing a report, with an executive summary, to present the findings of our work. This report would be reviewed by our Advisory Partners Council, who along with our actuarial team would also be available to answer any questions you may have, and assist in interpretation and application of the report findings. This report will be the key deliverable for this project. However, we anticipate that other deliverables may be requested by management (e.g. shorter memos, email summaries, conference calls etc.) that we will provide as requested.

Level of effort to complete the project

We anticipate that we will be able to complete the work within the allotted 150 hours as described in the RFS. The hours will not exceed the total 150 hours as stated within the RFS over the term of the agreement without prior mutual written agreement.

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Supplement B - Submission

SUPPLEMENT B - SUBMISSION FORM

Request for Services Number: TBS-OTB-OPCD-22

To: HER MAJESTY THE QUEEN in right of Ontario as represented by President of Treasury Board

1. Vendor Information

(a) The full legal name of the Vendor is: _Ernst & Young LLP_____

(b) Please identify any other relevant name under which the Vendor conducts business:

__EY_____

(c) The Vendor's address, telephone and facsimile numbers are:

100 Adelaide Street W., Toronto, Ontario M5H 1S3, Canada, Telephone: 416 864 1234; Fax: 416 864 1174_____

(d) The name and title of the Vendor's Representative:

_Uros Karadzic, Partner_____

(e) The mailing address, phone number and e-mail address of the Vendor's Representative:

100 Adelaide Street W., Toronto, Ontario M5H 1S3, Canada, Telephone: 416 943 2087, uros.karadzic@ca.ey.com_____

(f) State the name, address, telephone and facsimile numbers and e-mail address of the Company Security Officer (CSO) for the Vendor:

Laarni Tansingco 100 Adelaide Street W., Toronto, Ontario M5H 1S3, Canada, Telephone: 416 932 5822, laarni.tansingco@ca.ey.com_____

(g) State the name and title of each of the individuals that the Vendor is proposing for this Project:

Uros Karadzic, Partner, People Advisory Services – Reward

Christina Chan, Manager, People Advisory Services – Reward

[Instructions: Please add additional lines as required to accommodate each of the proposed Personnel]

2. Submission Requirements and Accuracy of Information

The Vendor accepts the terms and conditions set out in the RFS. While this submission is provided for evaluation purposes only and is not legally binding before the execution of a SOW, I confirm that the information provided is accurate.

3. Certificate(s) of Insurance

As required in Article 32.4 – Proof of Insurance in the Master Agreement, please identify the status of the Vendor's Certificate(s) of Insurance by placing a check mark (√) in one (1) of the following three (3) boxes:

☒ a) the Vendor has previously submitted a Certificate of Insurance to MGCS, which has been approved

☐ b) the Vendor has included its Certificate of Insurance with this RFS submission (that will be subject to approval by MGCS) prior to the Client issuing a SOW

☐ c) the Vendor agrees to submit a Certificate of Insurance (that will be subject to approval by MGCS) prior to the Client issuing a SOW

As required in the Request for Services, the Vendor agrees to submit a Certificate of Insurance (that will be subject to approval by the Client) prior to the Client issuing the SOW to evidence the additional insurance and/or the additional coverage required by the Client.**]**

4. Conflict of Interest

The Vendor must complete the following:

(a) If the box below is left blank, the Vendor will be deemed to declare that: (1) there was no Conflict of Interest in preparing its submission; and (2) there is no foreseeable Conflict of Interest in the Vendor or any of its Personnel performing the contractual obligations contemplated in the Request for Services.

(b) Otherwise, if the statement below applies, check the box.

☐ **The Vendor declares that there is an actual or potential Conflict of Interest relating to the preparation of its submission, and/or the Vendor foresees an actual or potential Conflict of Interest in it and/or its Personnel performing the contractual obligations contemplated in the Request for Services.**

(c) If the Vendor declares an actual or potential Conflict of Interest by marking the box above, the Vendor must set out below details of the actual or potential Conflict of Interest:

_____
_____
_____

(d) The following individuals, as employees, advisors, or in any other capacity (i) participated in the preparation of our submission; **AND** (ii were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:

Job Classification (of last position with OPS):

Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):

Last Date of Employment with OPS:

Name of Last Supervisor with OPS:

Brief Description of Individual's Job Functions (at last position with OPS):

Brief Description of Nature of Individual's Participation in Preparation of Submission:

(Repeat above boxed information for each identified individual)

(e) The following are individuals that: (i) are proposed to be assigned by the Vendor to perform work under the SOW; **AND** (ii) were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:

Job Classification (of last position with OPS):

Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):

Last Date of Employment with OPS:

Name of Last Supervisor with OPS:

Brief Description of Individual's Job Functions (at last position with OPS):

(Repeat above boxed information for each identified individual)

(f) We agree that, upon request, we shall provide the Client with a Conflict of Interest Declaration from each individual identified above in the form prescribed by the Client.

5. Schedules

This submission includes the following Schedules:

Schedule A (Pricing Schedule)
Schedule B (Resumes)
[Instructions to Vendor: List all other schedules.]

[Ernst & Young LLP]
I acknowledge that providing my name on the line below in electronic form will constitute a signature for the purposes of the *Electronic Commerce Act, 2000*, S.O. 2000, c. 17.
I have authority to bind the Vendor.

Per: Ernst & Young LLP

Signature:

Name: Uros Karadzic

Title: Partner

Date: 3 November 2017

Schedule B – Resumes and references

Uros Karadzic, FSA, FCIA
Partner, People Advisory Services - Reward
416 943 2087
uros.karadzic@ca.ey.com

Role – Project Lead

Background

- Uros Karadzic is a partner and the national leader of the Reward practice. He is a pension actuary located in Toronto, Canada.
- His primary focus is in the following areas:
  - Pension audit and internal audit
  - Pension and benefit issues in Merger & Acquisition transactions
  - On-going advisory services on retirement benefit plans
- Advised clients (Canadian and multinational) on all aspects of their pension and benefit plans, including accounting, funding, design, implementation, management, risk and administration.
- Extensive experience in accounting for benefit plan obligations. He works with numerous EY audit teams, the EY Professional Practice (Canadian and Global) and industry bodies on benefit accounting issues.
- M&A transaction and integration, supporting clients by clearly identifying and measuring risks and costs. He also advised on appropriate measures to reduce those costs, focusing on post-acquisition funding requirements.

Pension Industry Leadership

The following projects are either currently ongoing or have been completed within the last 12 months:

- Member of the Ontario Pension Asset Expert panel in 2017, advised on the appropriate application of PSAS regarding pension accounting for the Province's sponsored pension plans with respect to asset ceiling and asset recognition.
- Member of the Public Sector Accounting Board's task force on Employment Benefits, working on improving the current pension accounting standards, and developing the new standards.
- As the leader of EY's pension practice, Uros has advised companies, governments and professional bodies on a diverse and broad range of pension issues. This included advising the federal government on a new funding policy for PSPP, as well as plan sponsors (corporate and government) on funding issues related to the adoption of Shared Risk Plans.

- Works closely with EY's Professional Practice (Canadian and Global) in setting audit rules for pension plans. He has also consulted to the Federal Office of the Auditor General on pension issues, as well as to the AGs of NS, NB, PEI and NL.
- Helped to establish EY's global position on various emerging issues (e.g. Shared Risk Plans, mortality, discount rates, transition to new accounting standards, asset ceiling, IFRIC 14, etc.).
- Member of the Canadian Institute of Actuaries taskforce for setting accounting discount rates, and the Society of Actuaries Project Oversight Group for the Pension Assumption and Methods.
- Presented to various industry and accounting bodies (Canadian and global) on pension accounting issues in Canada, including:
  - Canadian Council of Legislative Auditors (CCOLA) on accounting for Shared Risk Plans
  - Presentation to International Accounting Standards Board (IASB) staff on the impact of IFRS conversion on Canadian pension plan sponsors
  - Presentation to the CPA Canada on various pension accounting topics

Education and professional qualification and accreditation

- Hon. BSc. (High Distinction) in Actuarial Science from University of Toronto.
- Fellow of the Canadian Institute of Actuaries and a Fellow of the Society of Actuaries.

References

Patricia O'Malley
Pension Asset Expert Advisory Panel Chair
Ontario Pension Expert Panel
416-570-1924
plomalley@outlook.com

Cindy Veinot
Assistant Deputy Minister and Provincial Controller
Treasury Board Secretariat, Office of the Provincial Controller Division
416-323-8017
cindy.veinot@ontario.ca

Renée Pichard, CPA, CA
Principal, Professional Practices
Office of the Auditor General of Canada
613-952-0213 (5489)
renee.pichard@oag-bvg.gc.ca

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Christina Chan, FSA, ACIA
Manager, People Advisory Services - Reward
416 943 3121
christina.chan@ca.ey.com

Role – Intermediate Consultant

Background

- Christina Chan is an actuarial manager in the Reward practice in Toronto, Canada with over 9 years of experience. Her primary focus is in the following areas:
  - Pension and non-pension benefit plans audit and internal audit
  - Funding and accounting valuations of private and public sector pension plans
  - On-going advisory services on retirement benefit plans
  - HR transaction due diligence of pension and non-pension employee benefit programs
- Provided advisory services to plan sponsors on special non-routine projects, including plan design, plan wind-up, plant closure with union members, and asset transfer. All these projects involved valuation and projections, cost and benefit analysis, member communications, and assistance for the administration practice.

Audit and advisory experience

The following projects are either currently ongoing or have been completed within the last 12 months:

- Treasury Board of Secretariat (OPCD): Supported and provided advisory services on the process of compilation of input for the 2017/18 Provincial Budget and the preparation of the 2016/17 consolidated financial statements of the Province of its pension plans.
- Treasury Board of Secretariat (OPCD): Conducted three pension training sessions and transferred knowledge to the OPCD staff at the end of engagement.
- Ontario Power Generation: Supports and advises EY audit teams in the areas of auditing pension disclosure in financial statements, including assessment of actuarial assumptions, accounting methodology, plan provision interpretation and valuation, and assessment of the accounting for special events (example: Ontario Power Generation).
- Offers advanced knowledge of reporting prerequisites to assist in the preparation of accounting disclosures for pension and benefit plans under CPA Canada, US Financial Accounting Standards Board (FASB), Public Sector Accounting board (PSAB) and International Financial Reporting Standards (IFRS) guidelines.

Education and professional qualification and accreditation

- Bachelor of Mathematics in Actuarial Science with Finance Option from the University of Waterloo.
- Associate of the Canadian Institute of Actuaries.
- Fellow of the Society of Actuaries.

References

Cindy Veinot
Assistant Deputy Minister and Provincial Controller
Treasury Board Secretariat, Office of the Provincial Controller Division
416-323-8017
cindy.veinot@ontario.ca

Nadine Petsche
Director, Internal Audit
Ontario Power Generation (previously, TBS)
416-592-4240
Nadine.petsche@opg.com

Winnie Guo
Senior Manager, Actuarial and Financial Valuation
Ontario Power Generation
416-592-5702
Winnie.guo@opg.com

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FW_ Employee Life and Health Trusts (ELHTs) - accounting treatment.rtf

From: Petsche, Nadine (TBS) []
To: Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Employee Life and Health Trusts (ELHTs) - accounting treatment
Date: Friday, April 07, 2017 17:06:25
Attachment 1: ELHTs Accounting Treatment (EY 27 March 2017).pdf
Attachment 2: image001.jpg

Alicia,

I will request Shyrose set up a meeting for us to discuss next week. Thanks. Nadine

From: Christina Chan [mailto:Christina.Chan@ca.ey.com]
Sent: March-27-17 5:46 PM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani
Subject: Employee Life and Health Trusts (ELHTs) - accounting treatment

Hi Nadine,

As requested, we have prepared the attached document discussing the following topics:

1) Accounting treatment related to the provisions of the ELHTs under PSAB 3250/3255 (and the associated risks to the school boards)

2) Comparison of the ELHTs with Shared Risk Pension Plans

Both Shayan and I will be at Queen's Park tomorrow. Let us know if you have any comments. We are available if you would like to discuss prior to our meeting on Wednesday.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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ELHTs Accounting Treatment (EY 27 March 2017).pdf

Ernst & Young LLP
222 Bay Street, P.O. Box 251
Toronto, Ontario M5K 1J7

27 March 2017

Accounting Treatment - Employee Life and Health Trusts

OPCD has asked EY to comment on the accounting treatment related to the provisions of benefits from the Employee Life and Health Trusts ("ELHTs") under the Public Sector Accounting Standards.

Background

Historically, health, life and dental benefits were provided to employees in Ontario's educator sector through a multitude of individual plans administered separately by the Ontario school boards. To improve the cost-efficiency and delivery of benefits, all individual benefit plans are consolidated into six Employee Life and Health Trusts[1], each covering a certain group of employees. Each ELHT is established to meet the definition of an ELHT under the Income Tax Act Sc. 144.1. Benefits are provided through a joint governance structure between the bargaining/employee groups, school board trustees associations and the Government of Ontario under the ELHTs.

The ELHTs are intended to provide benefits to employees during their employment years. There are also separate retiree provisions intended to provide access to benefits for retirees.

Member groups

In order to determine the necessary accounting treatment, it is important to identify the different member groups and their respective benefit entitlements. Three groups of members with different benefit entitlements under the ELHTs are:

- "Active": approximately 211,000 members
- "Pre-August 2013 Retirees"[2]: approximately 5,700 members
- "Post-August 2013 Retirees"[3]: approximately: 1,400+ members

For current Active employees, the contributions by the boards to the ELHTs are fixed and negotiated during bargaining. Annual contribution amounts required from the boards per full-time employee are pre-determined for the period covered by collective bargaining agreements. Upon retirement, active members may be eligible for retiree benefits at full cost and they are not eligible for any cost subsidization (i.e. provisions for Post-August 2013 Retirees).

Certain members who retired prior to August 31, 2013 are eligible for a partial or full subsidization of benefit costs from the board, based on prior arrangements with their employer. The members are eligible to participate in the ELHTs until age 65 (with the exception of a small group who are eligible for lifetime coverage).

All members retiring after 31 August 2013 are eligible to participate in the ELHT through a Voluntary Plan and Separate Account. However, they are responsible for the entire cost of benefits. They are not eligible for any cost subsidization.

[1] OECTA, ETFO, AEFO, OSSTF Trust Agreements have been formally signed; CUPE and PVP/Non-union are to be finalized.
[2] Members retiring prior to 31 August 2013
[3] Members retiring after 31 August 2013

According to the ELHT Trust Agreements Article 6, "*the Trustees may establish any number of Separate Accounts within the Fund. The assets in each Separate Account shall be held as segregated funds and used for the provision of Benefits, in accordance with the terms of a Plan, to a discrete and identifiable group of Participating Employees*". Based on the benefit entitlements described above, presumably, a Separate Account is established for the Active members and a Separate Account is established for the Pre-August 2013 Retirees. Therefore, there is no cross-subsidy. For example, retiree costs are not cross-subsidized by premiums paid in respect of Active employees.

The Trust agreement state that any surpluses in a Separate Account may be used to increase Claims Fluctuations Reserve ("CFR"), enhance benefits, or reduce employee contributions. Conversely, any deficiencies in the trust may require the use of the CFR, amendment to benefit (reduction), or an increase to employee contribution levels.

For the Pre-August 2013 Retirees group, it is our understanding that if there is a funding deficiencies in the Separate Account for this group, the school board will be required to contribute and reimburse the Trust to make up the funding shortfall ("chargeback").

Accounting treatment

Paragraphs 011 – 012 of PSAB 3250 (see Appendix) discuss the classification of benefit plans as Defined Benefit ("DB") or Defined Contribution ("DC"). Further, in accordance with 3250.014, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan.

Considering the different provisions applicable to member groups and PSAB 3250.011 – 3250.012, the benefits provided through the ELHTs include DB provisions in respect of retiree groups, whereas Active member benefits do not fall in the scope of PSA 3250/3255. Specifically:

- *Active:* Benefits/costs relating to current active members does not fall under the scope of PS 3250 (Retirement Benefits) or PS 3255 Retirement Benefits (Post-employment benefits, compensated absences and termination benefits). The scope of these sections cover benefits payable in retirement, after employment but before retirement, or compensated absences or termination benefits. Costs relating to providing benefits to active members during employment would be expensed annually in amounts equal to the fixed contribution. Further, as current active members are not eligible for subsidized benefits upon retirement (i.e. they pay for the entire cost of the post-retirement coverage without any cost to the employer), there is also no post-retirement obligation. To the extent that members on long-term disability are also eligible to receive benefits from the ELHT, a defined benefit obligation may need to be recognized under PS3255 in respect of expected future contributions over the anticipated period of long-term disability in respect of disabled employees.

- *"Pre-August 2013 Retirees:* The provisions relating to certain members who retired prior to 31 August 2013 would be classified as DB provisions as the boards are at risk with respect to the amount of benefits these employees will receive. These risks include the possibility of higher/lower than expected claims, or greater/less than expected longevity. We understand that the school boards have historically reported defined benefit obligations in respect of the ongoing commitment to subsidize retiree benefits for members in this group and will continue to do so subsequent to the transition to the ELHTs. This is appropriate as the ELHTs would be reimbursed by the boards for any contribution requirement to make up for the deficit in providing the coverage for these members.

- *"Post-August 2013 Retirees:* By contrast, there is no cost to the school boards relating to members retiring after 31 August 2013. The entire cost is borne by retirees and the school boards are not required to make any additional contributions in the future in the event of any shortfall. School board contributions are not

subject to any actuarial risk. Rather, all risks are borne by the retirees. In the event that funds are insufficient to pay for benefits, the trust agreements outline measures to address those deficiencies. The measures include the application of reserves, increases to member contributions and a reduction in benefits. None of the measures require any additional contributions from the school boards.

Therefore, we understand there to be a defined benefit obligation only in relation to the benefit entitlement for the subsidies provided to certain members retired prior to 31 August 2013. In addition, there may be a defined benefit obligation in respect of members on long-term disability to the extent that the ELHT covers such members.

Comparison with Shared Risk Pension Plans

In recent years, a number of Canadian provinces have adopted "Shared Risk Pension Plan" legislation. Shared Risk Pension Plans (SRPPs) provide benefits under a defined benefit formula, while putting cost constraints on employer contributions. Employer and employee contributions are often restricted within a band and benefits may be subject to reductions depending on the funded level.

In general, Shared Risk Pension Plans have been viewed as defined benefit plans. Risks are shared by the employer and employees, with the employer usually being subject to some level of actuarial and market risks. There may, however, be instances where DC accounting could be possible. This would be the case when no risk is retained by the employer, i.e. contributions are fixed in all scenarios. As there are many variations of Shared Risk Pension Plans, careful judgment is required to determine the appropriate accounting treatment in each case.

At the request of OPCD, we have compared the key characteristics of the ELHTs established by the Ontario school boards to those of Shared Risk Pension Plans. We have not considered the provisions relating to Pre-August 2013 Retirees, as these are clearly DB provisions under PS 3250/3255.

When comparing the benefits for the Active members under the ELHT with the SRPPS, there are a number of important differences to be considered but the following two are most significant:

- As SRPPs provide post-retirement benefits, they are within the scope of PS3250; however, as demonstrated in the previous section, the benefits provided for the Active members under ELHTs do not fall under the scope of PS3250.
- For SRPPs, the employer is subject to some level of actuarial risks and market risk as future contributions may be increased to pay for past deficiencies. Under ELHTs, the school boards are not subject to any risks: (a) contributions are fixed (as required by a Central Collective Agreement or any applicable Participation Agreement); (b) no additional contributions will be required for the related past service regardless of future actuarial or market experience; (c) the contributions required by the school boards are not dependent on the funding position of the Separate Account. Rather, employee's contributions (or benefits paid) may increase or decrease based on the surpluses/deficiencies of the Separate Accounts.

Further, there is no cost (and therefore, no post-retirement benefits) for members retiring after 31 August 2013 under the ELHTs. For these reasons, we would not expect the same accounting treatment to be applied for the SRPPs and ELHTs.

Appendix – Public Sector Accounting Board ("PSAB") 3250 Retirement Benefits (applicable excerpts)

.011 Two types of benefit plans are addressed in this Section — defined benefit plans and defined contribution plans. A defined benefit plan is one that specifies either the benefits to be received by employees after retirement or the method for determining those benefits. Generally, the amount and value of the benefits to be paid depend on a number of factors and events. These include how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation and retirement age. When a government provides benefits under a defined benefit plan, it is at risk with respect to the amount of the benefit that each employee will receive (actuarial risk) and with respect to the investment returns on any assets set aside to pay for the cost of these benefits (investment risk).

.012 When a government provides benefits under a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. A defined contribution plan (or money purchase plan) is one in which a government's contributions in respect of services rendered by employees are specified. The government is required by the plan to make a specific fixed contribution each period. If that contribution is made, no additional government contributions are required now or in the future for the related service. The employees are at risk. This is generally because the amount of the benefit that will be payable to an employee is dependent upon the funds accumulated for each employee's account and the investment earnings on the accumulated funds.

.013 Because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of a particular plan makes it a defined benefit or a defined contribution plan.

. 014 In some circumstances, a benefit plan may include both defined benefit and defined contribution promises. The plan, for example, may guarantee a basic defined retirement benefit and state that additional benefits, such as inflation protection, will be provided on a defined contribution basis. In such circumstances, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan. Once the type(s) of promise is identified, the accounting and reporting principles in this Section would be followed accordingly.

Appendix – Public Sector Accounting Board ("PSAB") 3255 Post-Employment Benefits (applicable excerpts)

Purpose and scope

.01 This Section establishes standards on how to account for and report obligations for post-employment benefits, compensated absences and termination benefits in government financial statements.

.02 This Section applies to post-employment benefits, compensated absences and termination benefits earned by employees and expected to be provided to them when they are no longer providing active service either on a temporary or permanent basis. For the purposes of this Section:

- *(a) Post-employment benefits are expected to be provided after employment but before retirement to employees and their beneficiaries. These benefits include long- and short-term disability income benefits (including workers' compensation), severance benefits, salary continuation, supplemental unemployment benefits, job training and counselling, and continuation of benefits such as health care benefits and life insurance.*
- *(b) Compensated absences are benefits for employee absences for which employees will be paid. These benefits include parental leaves, accumulated sick days, and sabbaticals that provide compensated, unrestricted time off for past service.*
- *(c) Termination benefits include the following:*
  - *a. Contractual termination benefits are benefits required to be provided to employees under the existing terms of a benefit arrangement when a specific event occurs that results in the downsizing and termination of a group of employees.*
  - *b. Special termination benefits are benefits that are not contractual termination benefits and that are offered to employees for a short period of time, normally not exceeding twelve months, in exchange for employees' voluntary or involuntary termination of employment.*

.03 The glossary in RETIREMENT BENEFITS, Section PS 3250, provides definitions for other relevant terms.

.04 This Section does not apply to short-term employee benefits, which would be accounted for under the general provisions for accruing liabilities. This accounting is generally straightforward because no actuarial assumptions are required and the liabilities are measured on an undiscounted basis.

.05 Examples of such short-term employee benefits are:

- *(a) Salaries, wages, bonuses, fringe benefits and similar items a government provides in the current reporting period or within twelve months thereafter, in exchange for services rendered by employees in the current reporting period; and*
- *(b) Occasional sick days and vacation days that do not vest or accumulate beyond twelve months after the current reporting period.*

Post-employment benefits, compensated absences and termination benefits are liabilities of a government. Accounting for all benefit plans is important because many governments have accumulated significant related liabilities. The fundamental accounting task is to determine the amount of the liability for these benefits and to what periods to attribute the costs.

.07 These standards are consistent with those established in RETIREMENT BENEFITS, Section PS 3250. The standards set out in that Section are appropriate for accounting for and disclosing post-employment benefits, compensated absences and termination benefits of a government. For example, a government providing these types of benefits through a defined contribution plan, multiemployer plan or joint defined benefit plan would refer to the guidance set out in Section PS 3250. This Section sets out those areas where the accounting and reporting are different from Section PS 3250.

image001.pdf

EY

FW_ FW_ Cap and Trade.rtf

From: Provis, Ian (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: FW: Cap and Trade
Date: Wednesday, August 22, 2018 13:13:13
Attachment 1: ATT00001.png

For your file on information related to the Quebec interpretation on the certification date issue

Ian Provis, OPCD

' 416.327.2722 | ian.provis@ontario.ca

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: Friday, January 20, 2017 7:30 AM
To: Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>
Cc: Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca>; Provis, Ian (TBS) <Ian.Provis@ontario.ca>; michael.hawtin@ca.pwc.com
Subject: Re: FW: Cap and Trade

Hi Cindy,

The information below does help explain Quebec's position, and on consideration I do think it has merit and is an acceptable approach to the issue of how to account for cap and trade.
Given the existing definitions of exchange vs non-exchange transactions and the high level of the SOP I believe that both approaches (Exchange and non-exchange) to examining this program would be acceptable under existing PSAS.

Given this, I think the question you have to determine is whether it is worth pursuing the "exchange transaction" view as an accounting policy in light of the AGs views, or whether to go with another equally acceptable accounting policy that will align with the AGs views and ensure there are no differences of opinion should the auction timing result in certification on or before March 31, 2017.

If the latter, I am happy to update the paper to conclude in line with a non-exchange view. I don't think it will take much time as the bulk of the paper is regarding asset recognition and liability recognition, both of which are important sections and do not significantly change based on the revenue recognition aspects.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Provis, Ian (TBS)" <Ian.Provis@ontario.ca>
To: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>, "Keates, James (TBS)" <James.Keates@ontario.ca>, Michael Hawtin/CA/ABAS/PwC@Americas-CA, Lucy Durocher/CA/ABAS/PwC@Americas-CA, "Chen, Doris (MOECC)" <Doris.Chen@ontario.ca>, "Lau, Lucia (MOECC)" <Lucia.Lau@ontario.ca>
Cc: "Veinot, Cindy (TBS)" <Cindy.Veinot@ontario.ca>
Date: 01/18/2017 05:33 PM
Subject: FW: Cap and Trade

We received this from Quebec - it sounds a little like they didn't need to come to an agreement so it seems they didn't agree on the application but they did on the unilateral revenue.

Ian Provis
' 416.327.2722 | ian.provis@ontario.ca
From: Pageau, Lucie [mailto:Lucie.Pageau@cf.gouv.qc.ca]
Sent: Wednesday, January 18, 2017 1:26 PM
To: Provis, Ian (TBS)
Cc: Falardeau, Simon-Pierre
Subject: RE: Cap and Trade

Hello Ian,

Here are the information we can provide you, following your emails to Mr Falardeau and me :

- We didn't have an agreement with our AG about all the details of the basis of recognition. However, we know that the AG examined the accounting aspect of Cap and Trade since he had included this specific matter in his audit plan for the consolidated financial statement of the governement (march 31st, 2016). We assumed he agreed with our position because no comment were made about that aspect.

- For the accounting aspect, here are the foundations of the accounting for these revenues. They are recorded on an accrual basis, on the basis of the amounts collected during auctions or over-the-counter sells.
  - The revenues associated with the future units of vintage are recognized at the moment of their auction.
    - This treatment is in accordance with the government accounting policy on duties et permits, which stipulates that: "Revenue from duties and permits is recognized when receivable. Where duty or permit revenue is refundable on demand and is linked to clearly identifiable goods and services that the Government must supply to the holder of the duty or the permit, the revenue is recognized over the reference period of such duty or permit."
    - These revenues are earned from the moment they become receivable, which is to say from the moment a trader has to pay the selling price agreed upon for the units bought in auction. Also, these revenues are non-refundable.
  - This accounting treatment is analogous to the one recommended in the project Statement of principles on revenues issued by the Public Sector Accounting Board.
    - The statement suggests the following principle: "Unilateral revenues should be recognized by a public sector entity when there is:
(a) authority to claim economic resources from other parties; and
(b) a past event that gives rise to a claim of economic resources."
    - In the statement, we define unilateral revenues as "When there is no direct exchange for goods or services, as is the case when performance obligations arise directly from the consideration promised or received." The authority to these unilateral revenues " is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue."
    - Paragraph .113 of the statement specifies that "It is the occurrence of a past event together with the authority that gives the public sector entity a right to the revenue. Unilateral revenues are recognized when the public sector entity has an unconditional right to the revenue, regardless of when cash is received."
    - In this case, the past event is the acquisition of the rights during an auction. The government doesn't have any other obligation to fulfill towards the trader regarding the units he has acquired.

Hope this will be usefull,

Lucie

Lucie Pageau, CPA, auditrice CA

Directrice générale de la pratique professionnelle
Ministère des Finances - Contrôleur des finances
1058, rue Louis-Alexandre Taschereau
Québec (Québec) G1R 5T2
Téléphone : 418 643-0284
Courriel : lucie.pageau@cf.gouv.qc.ca

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détruire et nous en aviser. Merci!
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De : Pageau, Lucie
Envoyé : 17 janvier 2017 16:32
À : 'Provis, Ian (TBS)'
Objet : RE: Cap and Trade

Hello Ian,

I am trying to find as much information as I can. I should be able to send you someting tomorrow in early afternoon.
Our AG and I didn't have that much of discussion about this matter but the AG agrees with our accounting.

Lucie

De : Provis, Ian (TBS) [mailto:Ian.Provis@ontario.ca]
Envoyé : 17 janvier 2017 15:20
À : Pageau, Lucie
Objet : Cap and Trade

Bonjour Lucie

I am sorry to be a pest. Do you already have an accounting position paper that supports Quebec's booking of auction proceeds from WCI

If you don't have a written paper could we arrange a call to discuss.

Our Auditor General's office is saying the reasons for the accounting based on the certification date being of the basis of recognition from the view of the Quebec's auditor's office. Did you and your auditor agree to all the details (that it is a unilateral/

non-reciprocal transaction?

Thank you
I hope to see you again soon

Ian

Ian Provis, CPA C.A.
Manager
Office of the Provincial Controller Division
' 416.327.2722 | ian.provis@ontario.ca

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TBS

FW_ FW_ auction timing.rtf

From: Provis, Ian (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: FW: auction timing
Date: Wednesday, August 22, 2018 13:09:58
Attachment 1: ATT00001.png
Attachment 2: Cap and Trade accounting implications - memorandum to file v7 December 7 EPD comments addressed.docx
Attachment 3: Cap and Trade accounting implications - memorandum to file v7 to v6 Compare.docx

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Shyrose V7 was the last version I got from PWC directly. The previous e-mail is considered the OAG copy as the final I think.

Ian Provis, OPCD

' 416.327.2722 | ian.provis@ontario.ca

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: Wednesday, December 07, 2016 9:50 AM
To: Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca>
Cc: Provis, Ian (TBS) <Ian.Provis@ontario.ca>
Subject: Re: FW: auction timing

Hi Nadine,

Please see attached revised paper, clean, and tracked changes to version 6. I made all the MOECC changes and therefore removed the MOECC comments from this document to the extent I believe they have been appropriately addressed.
I also enhanced the discussion on revenue recognition for the points that Cindy was requesting and the point that Nadine and I discussed the other day regarding including a discussion of the alternative of not recognizing revenue until the end of the compliance period.
A key concern was over the use of the word "contract". I have removed all references to the EAs as contracts and replaced it with other terminology that is acceptable under the accounting standards that gets to the same accounting outcome without the legal characterization as a contract.

A few outstanding items were noted:

Issue 1 - ITEM TO RECONFIRM WITH MOECC

Termination of the program
Myra's comment - It's not clear what "arrangements with the WCI " is being referred to here. There are a number of agreements and they all include termination clauses, including Ontario's agreement with WCI, Inc. (the entity administering the program) and the linking agreement between Quebec and California provides for termination.

Response (included in document)
We had asked in an earlier meeting if there were specific termination provisions for withdrawal from the linked market.
To re-confirm whether the Quebec California agreement only provides for termination but the terms are to be negotiated, which was our understanding, or whether there are terms described in the agreement – in which case it would be beneficial to get an understanding of these. I have clarified the language, but want to make sure we have the right fact pattern. Note – that I don't think termination provisions with WCI Inc as a service provider is relevant to the broader question here.

New wording:

While we understand that the agreement between Quebec and California provides for termination of that agreement we are not aware of any specific terms in the arrangements with linked jurisdictions that would detail how a withdrawal from the linked jurisdictions might be undertaken, if and when such a link is made.

Issue 2 - ITEM TO CONFIRM WITH MOECC - possibly Adrienne Molnar is the best person

Issue: I would like to confirm that the decision as to exactly which EAs are transferred (by identifier) is only made upon transfer of EAs. For example, does the invoice to the participant list the EAs by serial identifier? Or would the participant only know exactly which EAs it owns after they are transferred. Another way of asking the question is does the algorithm allocate specific EAs to each successful participant as part of the auction certification process, or only allocate the number of EAs that the participant will receive.

New wording:

A Participant only knows which specific EAs it controls (by identifier) when they are credited to the CITSS account.

Issue 3 - ITEM FOR NADINE'S GROUP

Myra's comment See the legal advice above indicating identifying which of the sections in the document are subject to privilege (Cabinet or solicitor-client). This is a section that should be noted as solicitor-client privileged. Those sections that rely on

statements in the TB submission(s) or other Cabinet documents should be marked as Cabinet confidential.

Response (included in document)
Nadine/Ian – please can you ensure this is appropriately done?

(I would rather someone on staff determine what is the appropriate language to use here).

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 12/02/2016 04:56 PM
Subject: FW: auction timing

Lucy,
FYI. I haven't had a chance to review yet. Nadine

From: Chen, Doris (MOECC)
Sent: December-02-16 4:07 PM
To: Petsche, Nadine (TBS); Lau, Lucia (MOECC)
Cc: Provis, Ian (TBS); Graham, Helen (TBS)
Subject: RE: auction timing

Hi Nadine,

Please see attached for an updated copy of the PwC document with MOECC feedback as well as proposed wording (in track changes).

It includes edits from our program areas as well as MOECC Legal re: the legislation and auction processes.

I didn't want to remove/edit any of their comments on the legislations/auction since they are the subject matter experts – so there are quite a bit of comments. Please let me know if you have any questions and I can follow-up with them.

From the accounting perspective, as you mentioned below, the revenue recognition aspect will require further discussion. I would recommend internal OPS discussions prior to your meeting with OAG.

Please let us know once you've had a chance to take a look – we are happy to discuss.

Thanks, Doris

Doris Chen, CPA, CA
Controller
doris.chen@ontario.ca
416-212-4825
40 St.Clair Avenue West, 6th Floor
Toronto ON M4V1M2

From: Petsche, Nadine (TBS)
Sent: December 2, 2016 8:35 AM
To: Chen, Doris (MOECC); Lau, Lucia (MOECC)
Cc: Provis, Ian (TBS); Graham, Helen (TBS)
Subject: FW: auction timing
Importance: High

Good morning Doris/Lucia.
Hoping you can help me out here w.r.t. the discussion below on auction date and how it would relate to the most recent information received from Jim Whitestone (through Helen Graham) that the expected date for allowances to be in hands of auction participants is Apr 12.

In our recent discussions on timing of various auction process milestones, we did not envision such a late date for transfer of the allowances, nor did I understand that any physical delivery of allowances was part of the process. I've attached a copy of the accounting analysis paper previously circulated, which included the illustrative timeline chart below. As a reminder, the preliminary accounting analysis concluded that revenue could only be recognized once the performance obligation was met. If that milestone is accomplished post March 31st, then the revenue would be reported in 17/18.

As previously noted, we are scheduling discussions with the OAG for next week to review the accounting. We had expected to receive feedback on the last version of the document by Monday at the latest. Not sure if it was sent to Ian? In light of the most recent info related to delivery/release of EAs, the paper would benefit from your team's

input/update.

Thanks in advance for your clarification and input.
Nadine

p.s. In light of the recent discussion on EA delivery/release, I have asked that the OAG meeting be scheduled for next Thursday to buy us more time to assess the implications of the latest info.

From: Tiffin, Dave (MOECC)
Sent: December 1, 2016 12:35 PM
To: Graham, Helen (TBS)
Cc: Lau, Lucia (MOECC); Fung, Felix (TBS); Whitestone, Jim (MOECC)
Subject: Re: auction timing

Helen,

I spoke with Jim W. He will try call you today.

Thx
Dave

From: Graham, Helen (TBS)
Sent: Thursday, December 1, 2016 11:18 AM
To: Tiffin, Dave (MOECC)
Cc: Lau, Lucia (MOECC); Fung, Felix (TBS)
Subject: auction timing

Hi Dave

Would appreciate an update from you on possibility of achieving transfer of allowances to participants in the first auction before the end of the fiscal year? I understand you folks are working on whether the machinery can achieve that – whats your current view as to whether it can be done, whats your current estimate of how likely it is we will get there, any particular things that have to be solved to make that happen? Would appreciate at least an informal view today, please – happy to do a phone chat if that is best?

thanks

Helen[attachment "PWC Document - comments (part 1 - pages 1 - 12) EPD commentss nov 27 1....docx" deleted by Lucy Durocher/CA/ABAS/PwC] [attachment "PWC Document - comments (2 - pg 13 to end) EPD comments nov 27 16 Cap....docx" deleted by Lucy Durocher/CA/ABAS/PwC]

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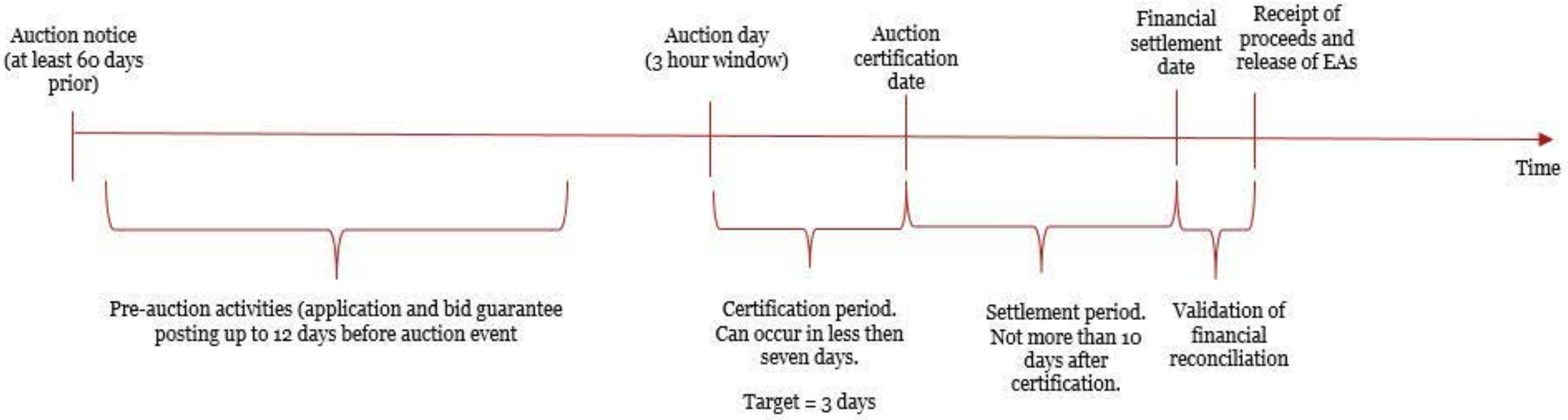

Auction notice (at least 60 days prior)
Auction day (3 hour window)
Auction certification date
Financial settlement date
Receipt of proceeds and release of EAs
Time
Pre-auction activities (application and bid guarantee posting up to 12 days before auction event
Certification period. Can occur in less then seven days.
Target = 3 days
Settlement period. Not more than 10 days after certification.
Validation of financial reconciliation

Cap and Trade accounting implications - memorandum to file v7 December 7 EPD comments addressed.pdf

Cap and trade accounting implications memorandum to file

1. Executive summary

2. Background and outline of cap and trade legislation and regulations

The *Climate Change Mitigation and Low-Carbon Economy Act, 2016* (the "Act") that was recently enacted establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario Regulation 144/16 and Ontario regulation 143/16 (together "the Regulations") have been made under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, sell, trade or otherwise deal with Ontario emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but whose greenhouse gas emissions ("emissions") meet the regulatory threshold and who choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the market so they can purchase, sell, trade or otherwise deal with EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Obtained free of charge from a distribution by the Minister of Environment and Climate Change ("the Minister") (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITSS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions, through sub-contractors. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as compliance within holding limits which limit the number of allowances participants can hold in these accounts. If holding limits are exceeded and not remedied within 5 days, the Minister has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, occurrences of this are expected to be rare as our understanding is that controls within the CITSS system should not generally allow individual limits to be exceeded except in very limited circumstances.

Auction process: In accordance with the Regulations there will be four auctions a year. EAs are sold at auction classified by "vintage". The Regulations provides for how many EAs are created of each vintage and how many EAs of each vintage will be available at auction, after the distribution of free EAs. The vintage of an EA affects which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held

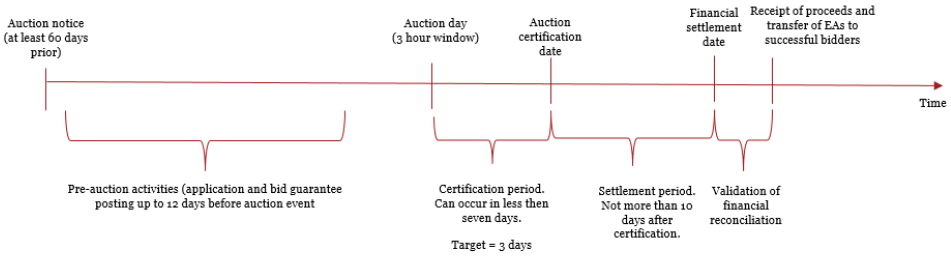
March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post financial assurance (a bid guarantee). This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash or a combination of these, and all bid guarantees are held in escrow by Deutsche Bank National Trust Company (DBNTC) in the auction participant's sub-account under the jurisdiction's escrow account. The jurisdiction's escrow account is opened by DBNTC in the name of WCI, Inc for the benefit of Her Majesty the Queen in Right of Ontario ("the Province's escrow settlement account"). The bid guarantee may be posted up to 60 days before the auction, and must be equal to or exceed the auction participants proposed maximum bid value for the auction (which is determined in accordance with the regulation).

At the auction the participants place bids for the number of EAs they will purchase at any price point at or above the auction minimum price. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results available on the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor of WCI, Inc. (currently Monitoring Analytics, LLC). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, notices (invoices) made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is given a notice by the Minister (invoiced) for the amounts due for the EAs resulting from a participant's successful bids. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's financial services sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay cash separately no later than 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC/LOG is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement account and Ontario's staff have confirmed that the amount in the escrow account match payments due from successful auction participants, then the escrowed amounts are transferred from Ontario's escrow account to Ontario's CRF bank account(s) and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas in the regulation that are applied to the entity specific situation of the participant (applicant). The distribution of allowances free of charge is expected to diminish over time as risk of leakage declines and other capped emitters are transitioned to the price of carbon from the cap and trade program (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). These EAs issued as free allowances are identical to those sold at auction and may be sold, traded or otherwise dealt with by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet the primary compliance obligation (submitting allowances or credits that match attributed emissions) under the program for the 2017-2020 compliance period except in limited circumstances (i.e., they were received as part of a participants free allocation or for meeting the additional compliance obligation for 3-to-1 if imposed). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Capped participants may acquire more allowances to meet their obligations if needed by purchasing EAs from other participants in market trades. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs created and distributed for the compliance period is capped by regulation. Unused EAs for the compliance period can be carried forward by the capped participant and used in future compliance periods. If the total emissions from all capped participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism creates an incentive for those capped participants who can most cheaply reduce their emissions to do so, in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

Mandatory and voluntary participants are required to report their greenhouse gas emissions annually (which must be quantified/calculated, reported and verified). The sum of the verified emission amounts over the course of the compliance period forms the total compliance obligation and capped participants must ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts by the deadline. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to meet the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to submit an additional 3 EAs (the "additional compliance obligation"). This additional compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the additional compliance obligation for the 2017-2020 period, however, they cannot be used to settle the primary compliance obligation or shortfall).

Due to the additional compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are submitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are submitted as part of the additional compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and submit sufficient EAs to meet their compliance obligation, including the number required by any additional compliance obligation (i.e. the additional 3). If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation (primary and additional) be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account does not give rise to compensation. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" (ERAs) or "offset credits"(OCs) in certain circumstances. Credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with OCs as opposed to EAs. As emissions can be settled by either EAs or credits, the creation of OCs essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link with California and Quebec and their linked market in 2018. When linked to that market, there will be one market for EAs – all participants from participating jurisdictions can purchase, sell trade or otherwise deal with EAs with other participants registered in the participating jurisdictions. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage for each year in the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs issued or created in one jurisdiction can be used to settle a compliance obligation in any of the participating jurisdictions, regardless of which jurisdiction created and issued/distributed them. The instruments are intended to be completely fungible. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation. It does not matter how the participant purchased the EA (auction or from another participant) or which jurisdiction originally issued the EA. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued/distributed.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. A change in the legislation would likely need to be made to terminate the program. While we understand that the agreement between Quebec and California provides for termination of that agreement we are not aware of any specific terms in the arrangements with linked jurisdictions that would detail how a withdrawal from the linked jurisdictions might be undertaken, if and when such a link is made.

Greenhouse Gas Reduction Account

The Act establishes an account in the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Proceeds from the distribution of EAs are credited to this account. Amounts of any fees, penalties and the settlement of additional compliance obligations in cash are also credited to the GGRA. The funds credited to the

Commented [HM(1]: It's not clear what "arrangements with the WCI " is being referred to here. There are a number of agreements and they all include termination clauses, including Ontario's agreement with WCI, Inc. (the entity administering the program) and the linking agreement between Quebec and California provides for termination.

Commented [LD2R1]: We had asked in an earlier meeting if there were specific termination provisions for withdrawal from the linked market.
To re-confirm whether the Quebec California agreement only provides for termination but the terms are to be negotiated, which was our understanding, or whether there are terms described in the agreement – in which case it would be beneficial to get an understanding of these.

I have clarified the language, but want to make sure we have the right fact pattern.

Note – that I don't think termination provisions with WCI Inc as a service provider is relevant to the broader question here.

GGRA may be used for initiatives set out in a Schedule to the Act and other initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include initiatives that include the following actions: the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts credited to the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will make a report available to the public about his evaluation of initiatives that are funded from amounts charged to the GGRA In addition an annual report will be prepared describing the credits and charges to the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from (charged to) the GGRA, even if these expenditures were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government proposed that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Based on the proposals, it is assumed that Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable (has a unique identifying number) and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. Market participants may also purchase or hold EAs without having a compliance obligation. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the legislation[1].

Is it a financial instrument?

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) defines financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument is by definition a contract, although PS 3450 does not define "contract" for its purposes.

It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is analogous to a contract between the holder and the Province insofar as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange a previously issued EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an additional compliance obligation at its discretion). Similarly, once a participant holds an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may have to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an additional compliance obligation (that may be converted to a cash payment requirement) but these are obligations arise through the act of directly or indirectly emitting greenhouse gas and not an obligation that is incurred through holding an EA. Rather an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs and credits). The creation and the maintenance of the Cap and Trade program, including the EAs in circulation, is due to legislation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand, although there are significant differences in the New Zealand program compared to the Ontario program (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. Further, once Ontario is linked to the California and Quebec market it will not be the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not completely control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it a charge (non-exchange transaction) on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce greenhouse gas emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation effectively requires capped participants to reduce emissions or to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed the number of allowances they have acquired (i.e., free-of-charge, at auction or by trading) EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be non-exchange transactions as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

Under this model, from an accounting perspective it is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that effectively requires a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the California and Quebec market (which is subject to government decisions and regulatory amendments that have not been made) capped participants will be able to meet their obligations by submitting EAs issued by California or Quebec. They will longer be required to effectively purchase EAs from the Province alone.

If the scheme is considered to be analogous to a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade legislation. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts:

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike capped participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Capped participants also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).

- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's receipt of payment from a participant arises from the auction process. If no EAs are purchased at auction the Province does not receive any payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario makes a decision to link, and has linked, with California and Quebec, then some or all of the EAs obtained by capped participants who emit greenhouse gas (or who are responsible for emissions) in Ontario could have been originally issued by other jurisdictions, as EAs can be purchased through auction or through the secondary market. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a non-exchange "charge" on emissions, for accounting purposes, does not hold as there is no consistent basis on which this charge is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions, the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was often limited direct costs to companies from emitting pollution - rather the costs were largely born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a "permit" to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not to provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a

participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of the nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for additional compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to additional compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has no material impact on the Public Accounts.

b) Escrow proceeds in the auction process: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the EAs are the transferred to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the auction certification date to the delivery date of the EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation in relation to emissions that have been produced by capped participants are not recognized as assets, whether sold at auction or distributed as free allowances.

e) Failure of participant to pay additional compliance obligation: The right to demand payment in lieu of EAs for an additional compliance obligation is recognized after the time period that a participant has to rectify the shortfall by submitting EAs has expired, e.g. on the deadline specified in a notice issued under subsection 14 (8) of the Act of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to Province's CRF account(s) (credited to GGRA) and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations and any additional compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying additional compliance shortfall by submitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) On creation of free and auctioned EAs:

EAs are "goods" created to be sold at auction to participants or by reserve sale or distributed free of charge to capped participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to additional compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account, as the Province is the sole beneficiary of this account and WCI, Inc does not have authority to

give instructions for the funds in this account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participants' sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DBNTC fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by various agreements between the entity administering the program on behalf of Ontario and its sub-contractors, including the agreed to terms and conditions governing the auction. The contractual arrangements are intended to protect the province from liability for errors by the financial services administrator (DBNTC).

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On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no mutual understanding of the agreed terms for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report submitted by Monitoring Analytics LLC. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements. Internal jurisdiction approvals must also be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred and notice provided to the successful participants there is a mutual understanding of the terms of sale and purchase between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own CRF account(s) (credited to the GGRA) until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been transferred to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While the terms of the transfer of EAs for consideration has been agreed upon between the participant and the province, neither party has executed on the arrangement prior to cash being received into Escrow, and therefore it remains an executory arrangement until one party performs by paying consideration or delivering the goods. As there is no

amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow, return of LOCs/LOGs by courier, or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to settlement.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as arrangement date: An alternative view is that the auction date, rather than the certification date is the date that the terms of the transfer of EAs is set between the Province and the participant for the sale of EAs. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, once the auction algorithm has been run the Province does know who the successful bidders are and at what price the EAs will be sold and therefore from the Province's perspective there is an agreed upon arrangement, as the purchaser stands ready to transact at the bid price and collection of consideration is reasonably assured through the financial assurance process. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed

Settlement period/financial settlement date as arrangement date: Legally there is no obligation of the Province to deliver EAs until cash has been received. Therefore it could be argued that there is no enforceable obligation of the Province to transfer EAs until the cash is received during the settlement period. It should be noted that the financial settlement date itself is merely the date by which all cash will be received under the escrow process. It is not substantive for accounting purposes in that it does not reflect when the cash is received into the Province's Escrow Settlement account, nor when it is transferred into the Province's CRF account(s) (credited to GGRA). This view was rejected for accounting purposes because both parties have an understanding of the auction processes and arrangements to be able to determine their respective rights and obligations and payments terms under the program prior to this point. The auction system is arranged such the financial assurance process ensures that a successful bidder will pay and the Province is legally obligated to transfer the EAs upon receipt of payment. Therefore both the rights and obligations of the parties are enforceable at the auction certification date. (Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) even if accepted, this view would not substantially change any of the accounting entries.)

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the arrangement that exists from the certification date to the settlement of the arrangement by delivery of EAs date. The arrangement is at a fixed price as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not a contractual right to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Successful auction bids to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the arrangement

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 additional compliance obligation. However, when the EAs are distributed the Province cannot expect that any participants will be subject to the 3 for 1 additional compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 additional compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there being no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of

goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 additional compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for additional compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay additional compliance obligation:

An additional compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EAs during the compliance period or else the participant must obtain a greater number of EAs, potentially at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for additional compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or additional compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction with whom Ontario links) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the additional compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an additional compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be submitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with California and Quebec it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all the three linked jurisdictions and once distributed all EAs are identical to each other in terms of rights and obligations relating to the EA (notwithstanding each EA does have an identifying number) and so there is no meaningful distinction between EA's that are "Ontario" EA's or those of another jurisdiction. If a capped participant has purchased an EA that was issued as an allocation from California or Quebec and submits it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the EAs distributed or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the

cap and trade program or bankruptcy of a participant. Based on the legislation there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of distribution.

In respect of the EAs that are given away for free, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the capped participant being registered and applying each year to be eligible to receive the EAs. To the extent that that a capped emitter has applied to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the distribution of EAs free of charge or by auction, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade program, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not

have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA distribution, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of participants' cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DBNTC or its parent company, DB. Based on legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's escrow accounts as there is recourse under both the indemnification clause of the DBNTC contract and required insurance (depending on the nature of the error). Further, if DBNTC fails to make payment to a participating jurisdiction because it or its parent company bank, DB, has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DBNTC or DB's errors.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DBNTC and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation for the sale of EAs? A performance obligation is defined in IFRS 15 as a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract or, in the case of the Revenue SOP, the terms of service set by legislation or regulation – both resulting in an arrangement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that the arrangement is considered to exist between a specific participant and the province to transfer a specified number of EAs.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the market or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to both capped participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a performance obligation is created when a participant successfully bids at auction and that bid is confirmed as successful in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under the auction arrangements.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the other jurisdictions, not all the participants will be located in Ontario. While the province has set targets for the reduction of greenhouse gas below the 1990 levels in Ontario and has represented that the cap and trade program will help them achieve these targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both an obligation to distribute the EA in the auction process and a stand-ready obligation to retire the EA in the future in settlement of a compliance obligation. In other words an EA is an intangible "right" that has been created and distributed by the Province that Province is obligated to retire. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province retires the EA's at the end of the compliance period. This view was rejected because the past event that gives rise to the obligation to retire the EA as settlement of a participant's compliance obligation occurs when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to retire all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to retire an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the other jurisdictions as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions and likewise there is an obligation to retire EAs submitted by Ontario participants, even when these were purchased from California or Quebec (if and when Ontario links) or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to submit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade ~~and~~or otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash

in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no creation of an does not have an alternative use. Therefore the performance obligation will be satisfied at a point in time.

   IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and transfer of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the auction process must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not apply to EAs and is never transferred. However, holding limits are applied. This indicates that EAs can be legally held (below holding limits) or not legally held (above holding limits) which forces a sale of the excess EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date. Holding limits are measured on what is in a participant's CITSS account.
The entity has transferred physical possession of the asset	While EAs do not have physical form, each EA has a unique identifier when created, and as such separately exists and can be identified as being in a specific CITSS account. Under the legislation, the Province has a legal obligation to transfer the EAs to participants once cash payment has been received. This indicates that there is still some action to be taken by the Province in respect of the transfer of control of the EAs that is not met until that transfer has occurred.			The record of a participant's EAs is maintained in the CITSS account and so the right to trade or use an EA is confirmed only upon this date. A Participant only knows which specific EAs it controls (by identifier) when they are

				credited to the CITSS account. Therefore prior to this point a participant cannot be said to control specific EAs. There is a process performed by jurisdiction staff to transfer EAs on this date. The timing of this transfer and the specific EAs transferred is not controlled by the Participant.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset. Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is determined by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

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Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily. Additionally, although the EAs are

intangible, they are uniquely identified meaning that the transfer to the participants CITSS account can be seen as substantive delivery of the EAs.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

A point after transfer date: As the EAs can only exist be held in a participant CITSS account within the cap and trade program and legal title never transfers as EAs are not "property" it could be argued that control never passes to the participant and therefore revenue would not be recognized until the retirement of the EA at the end of the compliance period. This view was rejected as legal title is only one indicator and the other indicators suggest that control has passed to the participant at the transfer date. Additionally, as discussed in Section 3 above, the nature of the EA is that it is a permit that the holder has to settle the legislative compliance obligation that arises from producing one ton of emissions. The ability of the participant to be able to exercise that permit is a key determinate of control and this is passed on the transfer date. This is further emphasized by the fact that participants would be expected to recognize EAs as assets under various frameworks such as IFRS or ASPE. Both IFRS and ASPE have a similar definition of an asset as PSAS does, which includes a requirement that an entity controls the asset before recognition. As the same asset cannot be controlled by two parties simultaneously, some symmetry would be reasonable to expect.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash (up to 7 calendar days after the notice), the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a

government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to credit the auction proceeds to a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purposes specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be recorded in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet

their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction (as defined by PS 3100) on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to California and Quebec, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[2] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[2] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For a grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[3]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[3] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are submitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs sold or distributed in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has a government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem (retire) the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Cap and Trade accounting implications - memorandum to file v7 to v6 Compare.pdf

Cap and trade accounting implications memorandum to file ~~– proposed outline~~

1. Executive summary

2. Background and outline of cap and trade legislation and regulations ~~[INTD – MOECC to provide comments on accuracy of background terminology]~~

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The *Climate Change Mitigation and Low-Carbon ~~Economic~~Economy Act, 2016* (the "Act") that was recently enacted ~~that~~ establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario ~~regulation~~Regulation 144~~.~~/16 and Ontario regulation 143~~.~~/16 (together "the Regulations") have been ~~passed~~made under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, ~~hold,~~ sell ~~or,~~ trade or otherwise deal with Ontario emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but whose greenhouse gas emissions ("emissions") meet the regulatory threshold and who choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the ~~program~~market so they can ~~hold~~purchase, sell ~~and,~~ trade or otherwise deal with EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- ~~Distribution as a free allowance~~Obtained free of charge from a distribution by the Minister of Environment and Climate Change ("the Minister") (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "~~CITTS~~CITSS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions~~.~~, through sub-contractors. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as ~~holding levels are~~compliance within holding limits~~.~~ which limit the number of allowances participants can hold in these accounts. If holding limits are exceeded and not remedied within 5 days, the Minister ~~of the Environment and Climate Change (the "Minister")~~ has the ability to remove the excess allowances~~. Currently proposed updates to the Regulations would require~~ for no compensation that ~~the amounts in excess of the holding limits~~could then be re-sold at ~~auction and the proceeds of that sale to be remitted back to the participant.~~future auctions. However, occurrences of this are expected to be rare as our understanding is that controls within the ~~systems~~CITSS system should not generally allow ~~sales over the~~ individual limits to be ~~processed so examples of this should be~~ exceeded except in very limited ~~in practice.~~circumstances.

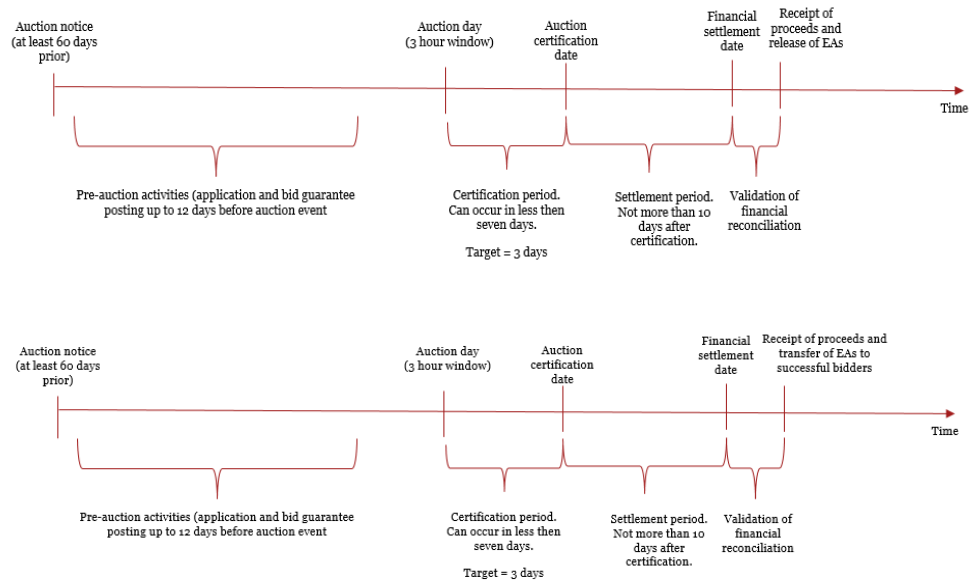
Auction process: In accordance with the Regulations there ~~are~~will be four auctions a year. EAs are sold at auction classified by "vintage". The Regulations ~~set out~~provides for how many EAs are created ~~for~~of each vintage and how many EAs of each vintage will be available at ~~each~~ auction, after the distribution of free EAs. The vintage of an EA ~~determines~~affects which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post financial assurance (a bid guarantee~~.~~). This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash~~, both~~ or a combination of ~~which~~ these, and all bid guarantees are held in escrow by Deutsche Bank ~~(DB~~National Trust Company (DBNTC) in the auction participant's sub-account under the jurisdiction's ~~Escrow~~escrow account. The ~~Province's~~jurisdiction's escrow account is opened by DBNTC in the name of WCI, Inc for the benefit of Her Majesty the Queen in Right of Ontario ~~Minister of~~ ("the ~~Environment and Climate Change.~~Province's escrow settlement account"). The bid guarantee may be posted up to 60 days before the auction, and must be equal to or exceed the ~~total amount of bids that will be submitted by~~ auction participants proposed maximum bid value for the ~~participant in~~ auction (which is determined in accordance with the ~~auction.~~regulation).

At the auction the participants place bids for the number of EAs they will purchase at any price point~~.~~ at or above the auction minimum price. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results ~~provided by~~available on the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor ~~called~~of WCI, Inc. (currently Monitoring Analytics, LLC). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, notices (invoices) made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is given a notice by the Minister (invoiced) for the amounts due for the EAs ~~purchased~~resulting from a participant's successful bids. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's financial services sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay cash separately ~~within~~no later than 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC/LOG is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement ~~accounting~~account and Ontario's staff have confirmed that the amount in the escrow account match payments due from successful auction participants, then the escrowed amounts are transferred ~~to the GGRA~~from Ontario's escrow account to Ontario's CRF bank account(s) and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas in the regulation that are applied to the entity specific situation of the participant ~~and are~~ (applicant). The distribution of allowances free of charge is expected to diminish over time as ~~transition~~risk of leakage declines and other capped emitters are transitioned to the price of carbon from the cap and trade program ~~is completed and inter-provincial "leakage" declines~~ (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). ~~Once~~These EAs issued~~, these EAs~~ as free allowances are identical to those sold at auction and may be ~~held or~~sold, traded or otherwise dealt with by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet ~~normal~~the primary compliance obligation (submitting allowances or credits that match attributed emissions ~~obligations~~) under the program for the 2017-2020 compliance period ~~(although~~except in limited circumstances (i.e., they ~~can be used~~ were received as part of a participants free allocation or for meeting the additional compliance obligation for 3-to ~~settle increased compliance obligations~~ 1 if imposed). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. ~~Participants~~ Capped participants may ~~purchase~~acquire more allowances to meet their obligations if needed by purchasing EAs from other participants in market trades ~~to be able to meet their obligations~~. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs

~~issued~~created and distributed for the compliance period is capped by regulation. ~~Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price.~~ Unused EAs for the compliance period can be carried forward by the capped participant and used in future compliance periods. If the total emissions from all capped participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism ~~allows~~creates an incentive for those capped participants who can most cheaply reduce their emissions ~~an incentive~~ to do so, in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

~~At the end of the compliance period mandatory~~Mandatory and voluntary participants are required to report their ~~attributed carbon emissions (~~greenhouse gas emissions annually (which must be quantified/calculated, reported and verified~~) for the~~). The sum of the verified emission amounts over the course of the compliance period forms the total compliance ~~period~~obligation and capped participants must ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts by the deadline. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to ~~fulfil~~meet the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to ~~acquire and~~ submit an additional 3 EAs (the "~~increased~~additional compliance obligation"). This ~~increased~~additional compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the ~~increased~~additional compliance obligation for the 2017-2020 period, however, they cannot be used to settle the ~~original~~primary compliance obligation or shortfall).

Due to the ~~increased~~additional compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are ~~remitted~~submitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are ~~remitted~~submitted as part of the ~~increased~~additional compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs ~~for future compliance periods~~ is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and ~~remit~~submit sufficient EAs to meet their compliance obligation, including the number required by any additional compliance ~~obligations for shortfalls.~~obligation (i.e. the additional 3). If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation (primary and additional) be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account ~~is without payment~~does not give rise to ~~the participant~~compensation. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" (ERAs) or "offset credits""(OCs) in certain circumstances. ~~These credits~~Credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with ~~credits~~OCs as opposed to EAs. As emissions can be settled by either EAs or credits ~~and offsets~~, the creation of ~~credits or offsets~~OCs essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link ~~to the WCI in 2018. The WCI currently includes~~ with California and Quebec and ~~California.~~ their linked market in 2018. When linked to ~~the WCI~~that market, there will be one market for EAs – all participants from participating jurisdictions can ~~buy~~purchase, sell~~, hold and~~ trade or otherwise deal with EAs with other participants registered in the participating jurisdictions. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage ~~based on their cap~~ for each year in the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs ~~are not attributed back to a~~issued or created in one jurisdiction ~~of issuance and~~ can be used to settle a compliance obligation in any of the participating jurisdictions, regardless of which jurisdiction created and issued/distributed them. The instruments are intended to be completely fungible. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation ~~based on their emissions.~~. It does not matter ~~whether they~~how the participant purchased the ~~EAs at~~ EA (auction or from ~~a California~~another participant) or ~~Quebec participant~~which jurisdiction originally issued the EA. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California ~~below their caps~~, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued/distributed.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. ~~The program could only be terminated through a~~ A change in the legislation~~. We~~ would likely need to be made to terminate the program. While we understand that the agreement between Quebec and California provides for termination of that agreement we are not aware of any specific terms in the arrangements with ~~the WCI~~linked jurisdictions that would ~~specify~~detail how a withdrawal from the ~~WCI~~linked jurisdictions might be undertaken~~.~~, if and when such a link is made.

Greenhouse Gas Reduction Account

The Act establishes an account ~~with~~in the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Other than limited exceptions, proceeds~~Proceeds from the distribution of EAs are ~~included in~~credited to this account. Amounts of any fees, penalties and the settlement of ~~increased~~additional compliance obligations in cash are also ~~included in~~credited to the GGRA. The funds ~~in~~credited to the GGRA may be used for initiatives set out in a Schedule to the Act and other initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include initiatives that include the following actions: the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts ~~in~~credited to the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will ~~issue~~make a report available to the public ~~notice regarding the~~ about his evaluation of initiatives that are funded ~~by~~from amounts charged to the GGRA~~.~~ In addition an annual report will be prepared describing the ~~activities of~~credits and charges to the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from (charged to) the GGRA, even if ~~they~~these expenditures were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government ~~announced~~proposed that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Based on the proposals, it is assumed that Ontario's cap and trade program means that it will not be subject to the federal carbon floor price

Commented [HM(1]: It's not clear what "arrangements with the WCI " is being referred to here. There are a number of agreements and they all include termination clauses, including Ontario's agreement with WCI, Inc. (the entity administering the program) and the linking agreement between Quebec and California provides for termination.

Commented [LD2R1]: We had asked in an earlier meeting if there were specific termination provisions for withdrawal from the linked market.
To re-confirm whether the Quebec California agreement only provides for termination but the terms are to be negotiated, which was our understanding, or whether there are terms described in the agreement – in which case it would be beneficial to get an understanding of these.

I have clarified the language, but want to make sure we have the right fact pattern.

Note – that I don't think termination provisions with WCI Inc as a service provider is relevant to the broader question here.

as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable (has a unique identifying number) and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. Market participants may also purchase or hold EAs without having a compliance obligation. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the ~~Act~~legislation[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) ~~define~~defines financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument is by definition a contract, although PS 3450 does not define "contract" for its purposes.

It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA ~~could be considered~~is analogous to ~~be~~ a contract ~~in the broadest sense~~ between the holder and the Province insofar as both parties know their respective rights and obligations that arise from holding and issuing EAs ~~as these are laid out by legislation and enforceable under it.~~.

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[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange ~~an~~a previously issued EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an ~~increased~~additional compliance obligation at its discretion). Similarly, once ~~they are the holder of~~a participant holds an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may ~~be obligated~~have to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an ~~increased~~additional compliance obligation ~~in~~(that may be converted to a cash~~,~~ payment requirement) but these are obligations ~~that~~ arise through the act of directly or indirectly emitting ~~pollutants~~greenhouse gas and not an obligation that is incurred through holding an EA. Rather ~~holding~~ an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs and credits). The creation and the maintenance of the Cap and Trade program, including the EAs in circulation, is ~~required by Cap and Trade regulation~~due to legislation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand, although there are significant differences in the New Zealand program compared to the Ontario program (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. ~~These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with.~~ Further, once Ontario is linked to the ~~WCI~~California and Quebec market it ~~is~~will not be the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not completely control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it ~~similar to~~ a ~~"tax"~~charge (non-exchange transaction) on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same -- a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce greenhouse gas emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation effectively requires ~~mandatory~~capped participants to reduce emissions or to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed ~~their allowance of freely distributed EAs.~~the number of allowances they have acquired (i.e., free-of-charge, at auction or by trading) EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be ~~a~~ non-~~reciprocal transaction~~exchange transactions as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

~~It~~Under this model, from an accounting perspective it is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative

requirement that ~~forces~~effectively requires a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the ~~WCI there is no legislative requirement that the participant purchase an EA from the Province.~~California and Quebec market (which is subject to government decisions and regulatory amendments that have not been made) capped participants will be able to meet their obligations by submitting EAs issued by California or Quebec. They will longer be required to effectively purchase EAs from the Province alone.

If the scheme is considered to be ~~in substance like~~analogous to a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade ~~regulations~~legislation. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts:

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike ~~mandatory or voluntary~~capped participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. ~~Mandatory and Voluntary participant~~Capped participants also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's ~~right to~~receipt of payment from a participant arises from the auction process ~~and not solely from legislation.~~ If no EAs are purchased at auction the Province ~~has no right to~~does not receive any payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario makes a decision to link, and has linked, with ~~the WCI~~California and Quebec, then ~~mandatory and voluntary~~some or all of the EAs obtained by capped participants who ~~create~~emit greenhouse gas (or who are responsible for emissions) in Ontario could ~~obtain some or all their EAs from California, Quebec or~~ have

been originally issued by other jurisdictions, as EAs can be purchased through auction or through the secondary market ~~participants.~~ There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a ~~tax~~non-exchange "charge" on emissions, for accounting purposes, does not hold as there is no consistent basis on which this ~~"tax"~~charge is calculated.

- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions ~~as,~~ the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was ~~no cost~~ often limited direct costs to companies from emitting pollution - rather the costs were largely born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a "permit" to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not to provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of the nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for ~~increased~~additional compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to ~~increased~~additional compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has ~~not~~no material impact on the Public Accounts.

b) Escrow proceeds ~~held for auctions~~in the auction process: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the ~~contract[2] is settled by the transfer of EAs~~EAs are the transferred to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the ~~date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of~~auction certification date to the delivery date of the EAs there is no derivative instrument required to be recognized.

~~[2] Please refer to analysis of "Escrow proceeds held for auctions" for explanation of the use of the word "contract" in this memorandum.~~

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation ~~as~~in relation to emissions ~~are~~that have been produced by capped participants are not recognized as assets, whether sold at auction or ~~issued~~distributed as free allowances.

e) Failure of participant to pay ~~increased~~additional compliance obligation: The right to demand payment in lieu of EAs for an ~~increased~~additional compliance obligation is recognized after the time period that a participant has to rectify the shortfall by ~~remitting~~submitting EAs ~~as~~has expired, e.g. on the deadline specified in a notice issued under ~~Section~~subsection 14 (8) of the Act of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to ~~GGRA~~Province's CRF account(s) (credited to GGRA) and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations ~~or increased~~and any additional compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying ~~increased~~additional compliance shortfall by ~~remitting~~submitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) On creation of free and auctioned EAs:

EAs are "goods" created to be sold ~~or distributed~~ at auction to participants or by reserve sale or distributed free of charge to capped participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to ~~increased~~additional compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account~~.~~, as the Province is the sole beneficiary of this account and WCI, Inc does not have authority to give instructions for the funds in this account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot

recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. ~~It is the view of the Province that~~After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the ~~participant's~~participants' sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if ~~DB~~DBNTC fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by various agreements between the entity administering the program on behalf of Ontario and its sub-contractors, including the agreed to terms and conditions governing the auction. ~~The participating jurisdiction should not be liable for DB's error. As the agreements between DB and the Province are still under negotiation, the final~~The contractual arrangements ~~between DB and~~are intended to protect the province from liability for errors by the ~~Province of Ontario should be considered to confirm the above analysis.~~financial services administrator (DBNTC).

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no ~~contract~~mutual understanding of the agreed terms for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report~~.~~ submitted by Monitoring Analytics LLC. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements ~~and internal~~. Internal jurisdiction approvals must also be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred ~~there is a "contract" between a successful bid participant and the Province and the settlement process begins. Legally speaking, the Province is not obligated to issue an EA under legislation until the participant has paid the auction price, and therefore there is no legal obligations of the Province until payment is received. This would suggest that there is no "contract" until some point in the financial settlement process when proceeds are received into Ontario's escrow account. However, for purposes of this analysis the word "contract" is used consistent with the accounting definition found in IFRS 15 IFRS 15 is an appropriate source of GAAP consistent with reference to IFRS 15 for revenue recognition purposes – see Section 6), whereby an arrangement is a contract when both parties have approved the arrangement (in writing or in accordance with customary business practices); the entity can identify each party's rights and payment terms regarding the goods and services to be transferred, there is commercial substance and it is probable that the entity will collect the consideration in exchange for the goods and services (IFRS 15.9). Further uses of the word "contract in this memorandum refers to the accounting sense.~~

and notice provided to the successful participants there is a mutual understanding of the terms of sale and purchase between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to

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the Province's own ~~GGRA bank~~CRF account(s) (credited to the GGRA) until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been ~~delivered~~transferred to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While ~~there is a contract~~the terms of the transfer of EAs for consideration has been agreed upon between the participant and the province, neither party has executed on the ~~contract~~arrangement prior to cash being received into Escrow, and therefore it remains an executory ~~contract~~arrangement until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

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Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow, return of LOCs/LOGs by courier, or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to ~~the auction process.~~settlement.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as ~~contract~~arrangement date: An alternative view ~~to~~ is that the auction date, rather than the certification date ~~as~~is the ~~contract~~ date that the terms of the transfer of EAs is set between the Province and the participant for the sale of EAs ~~is that there is a contract on the auction date~~. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, ~~the Province has run~~once the auction algorithm ~~and~~ has been run the Province does know who the successful ~~bidder~~bidders are and at what price~~,~~ the EAs will be sold and therefore from the Province's perspective there is ~~a contract~~an agreed upon arrangement, as the purchaser stands ready to transact at the bid price and collection of consideration is reasonably assured through the financial assurance process. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed ~~holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.~~

Settlement period/financial settlement date as ~~contract~~arrangement date: ~~As noted above, legally~~Legally there is no obligation of the Province to deliver EAs until cash has been received. Therefore it could be argued that there is no ~~contract~~enforceable obligation of the Province to transfer EAs until the cash is received during the settlement period. It should be noted that the financial settlement date itself is merely the date by which all cash will be received under the escrow process. It is not substantive for accounting purposes in that it does not reflect when the cash is received into the ~~Ontario~~Province's Escrow Settlement account, nor when it is transferred into the ~~GGRA.~~Province's CRF account(s) (credited to GGRA). This view was rejected for accounting purposes because both parties have ~~a good~~an understanding of the auction processes and arrangements to be able to determine their respective rights and obligations and payments terms under the program prior to this point. The auction system is arranged such the financial assurance process ensures that a successful bidder will pay and the Province is legally obligated to transfer the EAs upon receipt of payment. Therefore both the rights and obligations of the parties are enforceable at the auction certification date. (Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) even if accepted, this view ~~was taken it~~ would not substantially change any of the accounting entries~~.~~.)

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the ~~contract~~arrangement that exists from the certification date to the settlement of the ~~contract~~arrangement by delivery of EAs date. The ~~contract~~arrangement is at a fixed price ~~contract~~ as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not a contractual ~~rights~~right to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. ~~Auction contracts~~Successful auction bids to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the ~~contract.~~arrangement

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 ~~increased~~additional compliance obligation. However, when the EAs are ~~issued~~distributed the Province cannot expect that any participants will be subject to the 3 for 1 ~~increased~~additional compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 ~~increased~~additional compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there ~~bring~~being no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 ~~increased~~additional compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for ~~increased~~additional compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay ~~increased~~additional compliance obligation:

An ~~increase~~additional compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough ~~EA "permits"~~EAs during the compliance period or else the participant must obtain a greater number of ~~permits~~EAs, potentially at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for ~~increased~~additional compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or ~~increased~~additional compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction ~~of the WCI~~with whom Ontario links) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the additional compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an ~~increased~~additional compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts (“PS 1000”)

PS 3200, Liabilities (“PS 3200”)

PS 3300, Contingent liabilities (“PS 3300”)

PS 3310, Loan guarantees (“PS 3310”)

PS 3410, Government Transfers (“PS 3410”)

PS 3450, Financial instruments, effective from April 1, 2019 (“PS 3450”)

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant’s cash financial assurance held in escrow in the participant’s sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be ~~remitted~~submitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with ~~the WCI~~California and Quebec it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all the three linked jurisdictions ~~in the WCI~~ and once ~~issued~~distributed all EAs are identical to each other in terms of rights and obligations relating to the EA (notwithstanding each EA does have an identifying number) and so there is no ~~way to determine whether an EA is an~~meaningful distinction between EA's that are "Ontario" ~~EA~~EA's or ~~that~~those of another jurisdiction ~~as all EAs are contractually identical.~~. If a ~~market~~capped participant has purchased an EA that was issued as an allocation from California or Quebec and ~~redeems~~submits it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the ~~issued~~ EAs distributed or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation ~~and regulations~~ there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of ~~issuance~~distribution.

In respect of the EAs that are given away ~~as~~for free ~~allowances~~, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the capped participant

~~registering~~being registered and applying each year to be eligible to receive the EAs. To the extent that that a capped emitter has ~~registered~~applied to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the ~~issue~~distribution of EAs free ~~EAs~~of charge or by auction ~~of other EAs~~, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade ~~system~~program, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA ~~issuance~~distribution, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of ~~Participant's~~participants' cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DBNTC or its parent company, DB. Based on ~~a~~ legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's ~~Escrow~~escrow accounts as there is recourse under both the

indemnification clause of the ~~DB~~DBNTC contract and required insurance (depending on the nature of the error). Further, if ~~the DB~~DBNTC fails to make payment to a participating jurisdiction because it or its parent company bank, DB, has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DBNTC or DB's ~~error~~errors.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between ~~DB~~DBNTC and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation for the sale of EAs? A performance obligation is defined in IFRS 15 as a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor

as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract ~~– which is an agreement~~or, in the case of the Revenue SOP, the terms of service set by legislation or regulation – both resulting in an arrangement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that ~~a contract~~the arrangement is considered to exist between a specific participant and the province to transfer a specified number of EAs.

Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the ~~WCI~~market or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to ~~voluntary~~both capped participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

Based on the above analysis, a ~~contract~~performance obligation is created when a participant successfully bids at auction ~~as~~ and that bid is confirmed as successful in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under ~~these contracts.~~the auction arrangements.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the ~~WCI,~~other jurisdictions, not all the participants ~~may not even~~will be located in Ontario. While the province ~~may have promised~~has set targets for the ~~public~~reduction of ~~Ontario and other parties that they will reduce carbon emissions~~greenhouse gas below the 1990 levels in Ontario ~~to meet emissions~~and has represented that the cap and trade program will help them achieve these targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both an obligation to ~~issue~~distribute the EA in the auction process~~,~~ and ~~also~~ a stand-ready ~~promise~~obligation to ~~redeem~~retire the EA in the future ~~to settle~~in settlement of a compliance obligation. In other words an EA is an intangible "right" that has been ~~issued~~created and distributed by the Province that ~~province~~Province is obligated to ~~redeem~~retire. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province ~~redeems~~retires the ~~EA.~~EA's at the end of the compliance period. This view was rejected because the past event that gives rise to the obligation to ~~redeem~~retire the EA as settlement of a participant's compliance obligation ~~is an obligation that arises~~occurs when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to ~~redeem~~retire all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations.

Therefore Ontario has no obligation to ~~redeem~~retire an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the ~~WCI~~other jurisdictions as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions ~~or to market participants,~~ and likewise there is an obligation to ~~redeem~~retire EAs submitted by Ontario participants, even when these were purchased from ~~another WCI jurisdiction~~California or Quebec (if and when Ontario links) or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to ~~remit~~submit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade ~~and~~or otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no ~~additional asset that~~ creation of an does not have an alternative use ~~that is created by the province to fulfil the contract~~. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and ~~delivery~~transfer of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the ~~contract payment~~auction process must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not ~~technically~~ apply to EAs~~.~~ and is never transferred. However, holding limits are applied. This indicates that EAs can be legally held (below holding limits) or not legally held (above holding limits) which forces a sale of the excess EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date. Holding limits are measured on what is in a participant's CITSS account.
The entity has transferred physical possession of the asset	~~This indicator is not entirely relevant as~~ While EAs do not have physical form, each EA has a unique identifier when created, and as such separately exists and can be identified as being in a specific CITSS account. Under the legislation, the Province has a legal obligation to transfer the EAs to participants once cash payment has been received. This indicates that there is still some action to be taken by the Province in respect of the transfer of control of the EAs that is not met until that transfer has occurred.			~~However the~~The record of a participant's EAs is maintained in the CITSS account and so the right to trade or use an EA is confirmed only upon this date. A Participant only knows which specific EAs it controls (by identifier) when they are credited to the CITSS account. Therefore prior to this point a participant cannot be said to control specific EAs. There is a process performed by jurisdiction staff to transfer EAs on this date. The timing of this transfer and the specific EAs transferred is not controlled by the Participant.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

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Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is ~~set~~determined by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily. Additionally, although the EAs are intangible, they are uniquely identified meaning that the transfer to the participants CITSS account can be seen as substantive delivery of the EAs.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

A point after transfer date: As the EAs can only exist be held in a participant CITSS account within the cap and trade program and legal title never transfers as EAs are not "property" it could be argued that control never passes to the participant and therefore revenue would not be recognized until the retirement of the EA at the end of the compliance period. This view was rejected as legal title is only one indicator and the other indicators suggest that control has passed to the participant at the transfer date. Additionally, as discussed in Section 3 above, the nature of the EA is that it is a permit that the holder has to settle the legislative compliance obligation that arises from producing one ton of emissions. The ability of the participant to be able to exercise that permit is a key determinate of control and this is passed on the transfer date. This is further emphasized by the fact that participants would be expected to recognize EAs as assets under various frameworks such as IFRS or ASPE. Both IFRS and ASPE have a similar definition of an asset as PSAS does, which includes a requirement that an entity controls the asset before recognition. As the same asset cannot be controlled by two parties simultaneously, some symmetry would be reasonable to expect.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash~~.~~ (up to 7 calendar days after the notice), the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to ~~place~~credit the auction proceeds ~~into~~to a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or ~~purpose~~purposes specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be ~~placed~~recorded in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction (as defined by PS 3100) on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to ~~the WCI~~California and Quebec, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of- NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For ~~an~~a grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are ~~remitted~~submitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs ~~issued~~sold or distributed in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has ~~an~~a government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem (retire) the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

FW_ Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Gregory Winston [gregory.winston@ca.ey.com]
Subject: FW: Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP
Date: Tuesday, January 16, 2018 14:43:22

Hi Shyrose,

Would you add us to the visitor list for next Monday?

As discussed, I will bring my now expired pass and have it renewed? Can we also arrange for Greg to receive a contractor pass?

Thanks!

Christina

Christina Chan, FSA | People Advisory Services | Manager

Ernst & Young LLP

Office: +1 416 943 3121 | Christina.Chan@ca.ey.com

From: Sun, Alicia (TBS) [mailto:Alicia.Sun@ontario.ca]
Sent: Tuesday, January 16, 2018 12:40 PM
To: Ma, Patricia (TBS) <Patricia.Ma2@ontario.ca>; Christina Chan <Christina.Chan@ca.ey.com>; Gregory Winston <gregory.winston@ca.ey.com>
Cc: Chan, Vanessa W. (TBS) <Vanessa.W.Chan@ontario.ca>; Patel, Bharat (TBS) <Bharat.Patel3@ontario.ca>
Subject: RE: Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP

Hi Christina,

Monday 1:00 p.m. works for us.

I will send out a meeting invite.

See you.

Alicia

From: Ma, Patricia (TBS)
Sent: January 16, 2018 12:13 PM
To: Christina Chan; Sun, Alicia (TBS); Gregory Winston
Cc: Chan, Vanessa W. (TBS); Patel, Bharat (TBS)
Subject: RE: Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP

Hi Christina,

We'll let you know on a good time for a call this week, tomorrow (Vanessa is away today).

Thanks,

Patricia

From: Christina Chan [mailto:Christina.Chan@ca.ey.com]
Sent: January-16-18 11:56 AM
To: Sun, Alicia (TBS); Gregory Winston
Cc: Chan, Vanessa W. (TBS); Ma, Patricia (TBS); Patel, Bharat (TBS)
Subject: RE: Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP

Hi Alicia,

We are happy to come in early next week. We are available any time after 1pm on Monday, or whenever works best for you on Tuesday. Let us know your preference.

Vanessa/Patricia, would you be available for a call sometime this week to connect so we will be well prepared for the meeting to follow?

I also have it in my notes that we are expecting the assumptions (i.e. “basis”) to be finalized around the 3rd week of January. Please let us know once the basis is chosen so we can provide our comments on the assumptions as requested.

Thanks,

Christina

Christina Chan, FSA | People Advisory Services | Manager

Ernst & Young LLP

Office: +1 416 943 3121 | Christina.Chan@ca.ey.com

From: Sun, Alicia (TBS) [mailto:Alicia.Sun@ontario.ca]
Sent: Tuesday, January 16, 2018 11:51 AM
To: Christina Chan <Christina.Chan@ca.ey.com>
Cc: Chan, Vanessa W. (TBS) <Vanessa.W.Chan@ontario.ca>; Ma, Patricia (TBS) <Patricia.Ma2@ontario.ca>; Patel, Bharat (TBS) <Bharat.Patel3@ontario.ca>
Subject: Getting Ready for Pension Work - HOOPP, PSPP, and CAATPP

Hi Christina,

How are you?

Our pension work for the Budget is about to start, and we are expecting to receive actuarial letters from pension plans around Jan. 26. I wonder whether you can come in early next week to go through a few items for PSPP and HOOPP to get the models ready.

We probably need an hour and a half. If you need more background on what we are looking for, please feel free to contact Vanessa or Patricia.

Please let me know what time works for you.

Thank you very much and see you soon.

Alicia

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FW_ Interim invoice.rtf

From: Petsche, Nadine (TBS) []
To: uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Interim invoice
Date: Monday, June 19, 2017 16:15:07
Attachment 1: image001.gif
Attachment 2: Invoice-C100093008.pdf

Thanks Uros.

We'll commence the payment process.

Nadine

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: June 19, 2017 1:50 PM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani; Christina Chan; Sarah Anderton
Subject: Interim invoice

Hi Nadine,

Further to your discussion with Shayan, here is the invoice for $65k. As you know, our work is on-going. We are also mailing a hard copy of this invoice today, but I thought you'd appreciate receiving a soft copy too.

If it is at all possible to process the payment before the end of the month (our year-end) that would be greatly appreciated.

Many thanks,

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

Invoice-C100093008.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100093008.pdf (243550 Bytes).

FW_ Invoice.rtf

From: Donaldson, Mark (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Invoice
Date: Thursday, October 19, 2017 14:19:25
Attachment 1: image001.gif
Attachment 2: Invoice-C100109767.pdf

Do you look after this?

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: October 19, 2017 2:05 PM
To: Veinot, Cindy (TBS); Donaldson, Mark (TBS)
Cc: Christina Chan; Gregory Winston
Subject: Invoice

Hi Cindy and Mark,

We have issued our final invoice today, and I am attaching a soft copy of it here for your convenience. This invoice covers the period to the conclusion of our contact, at 30 September 2017. You will note that the sum of all of our invoices (approx. $268k) has come in under the overall budget for the contract (approx. $299k).

Cindy, as you and I discussed last month, I believe there is a need and an opportunity to further improve pension reporting by the province. In particular, we discussed the work around assumption setting processes and documentation. This is the most important and strategic piece, but I think there is also further work that needs to be done on variance reconciliation and reporting, improvements how actuarial information is obtained and used, and further work related to OPEB plans.

Most of this work is continuation of the work we've been doing so far, and we would be available to continue supporting you in this regard. I recall that you were going to set up a meeting with Nancy Kennedy – please let me know if that still makes sense.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

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Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

Invoice-C100109767.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100109767.pdf (244653 Bytes).

FW_ Meeting this Thursday_.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Meeting this Thursday?
Date: Wednesday, November 09, 2016 14:12:51

Pls. advise?

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: November 9, 2016 1:03 PM
To: Virani, Shyrose (TBS)
Cc: Provis, Ian (TBS); michael.hawtin@ca.pwc.com
Subject: Meeting this Thursday?

Hi Shyrose,

I have two calendar invitations in the coming week for the cap and trade project - tomorrow at 1-2pm and also on Tuesday at 10-11am. The Tuesday one is important, but in light of it I thought we were going to cancel the Thursday one? I don't think we need both. Please confirm.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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FW_ OTTP -- history re_ use of surplus.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: OTTP -- history re: use of surplus
Date: Monday, September 19, 2016 11:28:04
Attachment 1: Key Funding Decisions.pdf

---

print

From: Veinot, Cindy (TBS)
Sent: September 10, 2016 7:16 AM
To: Hatzis, Len (TBS); Kaufman, Paul (TBS); Petsche, Nadine (TBS); Killoch, Alex (MOF); Raymond, Martin (CA - Montreal)
Cc: Fong, Pauline (TBS); Patel, Bharat (TBS)
Subject: OTTP -- history re: use of surplus

I think may be a very useful document re: the past – summarizes use of surplus going back to 1990.

I found this document on a website www.mypensionhub.com

The description of the website is below and I think its legit.

“This website houses information to help affiliate pension representatives educate members on plan funding and other key pension matters.

This website is maintained by the Ontario Teachers’ Pension Plan on behalf of a communications working group (CWG) made up of representatives of: l’Association des enseignantes et des enseignants franco-ontariens (AEFO), Elementary Teachers’ Federation of Ontario (ETFO), Ontario English Catholic Teachers’ Association (OECTA), Ontario Secondary School Teachers’ Federation (OSSTF), Ontario Teachers’ Federation (OTF), Ontario Government and Ontario Teachers’ Pension Plan.

Key Funding Decisions.pdf

Key Funding Decisions Since 1990

Plan Funding

The Ontario Teachers' Federation (OTF) and the Ontario government, which jointly sponsor the Ontario Teachers' Pension Plan, must file a funding valuation with the provincial pension regulator at least every three years. A valuation must be filed with assets and liabilities (the cost of future pensions) in balance.

OTF and the Ontario government can file a valuation earlier than required to help manage the plan's funding status.

The following chart shows how OTF and the Ontario government have used surplus funds or resolved funding shortfalls for each valuation filed with the regulator since the inception of the Teachers' pension plan as an independent entity in 1990.

For more information on plan funding, visit the Corporate section of our website at www.otpp.com.

Funding decisions

Year	Valuation status and key decisions
1990	A preliminary unfunded liability of $7.8 billion to be amortized over 40 years by special payments from the Ontario government; basic contribution rate increased to 8% from 7%.
1993	A preliminary $1.5 billion surplus was distributed: $1.2 billion used to reduce government's special payments; $0.3 billion used to offset government cost reductions in the education sector (social contract days).
1996	A preliminary $0.7 billion surplus was distributed: $0.6 billion used to reduce early retirement penalty to 2.5% from 5% for each point short of 90 factor and lower the CPP reduction after age 65 (to 0.68% from 0.7%).
1998	A preliminary $6.8 billion surplus was distributed: $2.2 billion to pay for the 85 factor window from 1998 to 2002 and further lower the CPP reduction to 0.6%; $4.6 billion to reduce the value of special payments owed by the Ontario government. OTF and the Ontario government agree future surplus would be used to eliminate the government's remaining special payments, and the next $6.2 billion surplus would be available to OTF for benefit improvements.

Year	Valuation status and key decisions
1999	A preliminary $3.5 billion surplus was distributed to eliminate government's remaining special payments.
2000	$4.5 billion surplus; no changes to benefits or contribution levels.
2001	A preliminary $6.8 billion surplus was distributed: $6.2 billion to pay for benefit improvements, including a permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average Year's Maximum Pensionable Earnings (YMPE) to calculate CPP reduction; pension recalculation based on approximate best-5 salary years for older pensioners; and top-up waived for Long-Term Income Protection (LTIP) contributions. The remaining $76 million was set aside in a contingency reserve to be used by OTF at a later date.
2002	$1.9 billion surplus; no changes to benefits or contribution levels.
2003	$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary $6.1 billion shortfall was resolved, leaving plan with a $0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary $12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary $2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary $17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.

Year	Valuation status and key decisions
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	$6.8 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 for pension credit earned after 2009 to 70% from 60% of the increase in the cost of living. Both changes go into effect in 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.

FW_ On our way to Queens Park. .rtf

From: Virani, Shyrose (TBS) []
To: Stretovitch, Ana (TBS) [Ana.Stretovitch@ontario.ca]
Subject: FW: On our way to Queens Park.
Date: Wednesday, May 10, 2017 14:41:18
Attachment 1: image001.png

Ana, pls. register Uros Karadzic

From: Shayan Jafrani [mailto:Shayan.Jafrani@ca.ey.com]
Sent: May 10, 2017 2:33 PM
To: Virani, Shyrose (TBS)
Cc: Uros Karadzic
Subject: On our way to Queens Park.

Hi Shyrose,

Uros and I are about to leave for our 3pm meeting at QP shortly. I have my access card but we will likely need someone to sign Uros in.

We'll call from security.

Thanks,

Shayan

Shayan Jafrani, FSA, FCIA | Senior Manager | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada

Phone: +1 416 943 2975 | Cell Phone: +1 647 885 9630
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image001.pdf

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FW_ Outline of position paper proposed allocations Oct 7.docx.rtf

From: Virani, Shyrose (TBS) []
To: Monteiro, Belinda (TBS) [Belinda.Monteiro@ontario.ca]
Subject: FW: Outline of position paper proposed allocations Oct 7.docx
Date: Monday, October 17, 2016 09:24:16

Here you go

From: Petsche, Nadine (TBS)
Sent: October 16, 2016 11:43 PM
To: lucy.durocher@ca.pwc.com
Cc: Virani, Shyrose (TBS)
Subject: Re: Outline of position paper proposed allocations Oct 7.docx

Thanks Lucy. I am copying Shyrose on this response. I think we would likely just need his name and to get the necessary clearance in place. Shyrose will be in touch if further details are required.

Regards,

Nadine

From: lucy.durocher@ca.pwc.com

Sent: Sunday, October 16, 2016 11:22 AM

To: Petsche, Nadine (TBS)

Subject: Re: Outline of position paper proposed allocations Oct 7.docx

Hi Nadine,

In respect of one of the sections discussing the differences between the funding valuations/OTPP financial statements and the Province's financial statements, I think it would be helpful if I could get our actuary to read through the write up, particularly in respect of the funding valuation differences. Currently the SOW does not list our actuary as someone performing work (to date all my conversations with him have been high level and theoretical). However, I would like to get him added to the SOW as vendor personnel.

Individual's Legal Name

Individual's Role and Experience Level

Service Category

Per Diem Rate

Mario Chassé

General Consultant (Actuarial), Level 2

Service Category 2

See “charges on a per diem rate basis”

I can ask him to sign a confidentiality agreement.
What else should be done to ensure that the SOW reflects that he will be providing some work under the contract?

Thanks,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 10/07/2016 04:02 PM
Subject: Outline of position paper proposed allocations Oct 7.docx

Hi Lucy.
As discussed, the attached version of the paper outline includes proposed section allocations. Please let me know if any of the notes are inconsistent with your understanding.
Thanks and have a wonderful Thanksgiving weekend!
Nadine[attachment "Outline of position paper proposed alloations Oct 7.docx" deleted by Lucy Durocher/CA/ABAS/PwC]

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FW_ PS 3250.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: PS 3250
Date: Wednesday, February 15, 2017 11:54:15
Attachment 1: image002.png
Attachment 2: PS 3250.pdf

Hi Shyrose,

Would you mind printing out the attached for Shayan and I (2 copies)?

Thank you!

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP

Office: +1 416 943 3121 | Christina.Chan@ca.ey.com

From: Shayan Jafrani
Sent: Tuesday, February 14, 2017 11:03 AM
To: Christina Chan <Christina.Chan@ca.ey.com>
Subject: FW: PS 3250

Shayan Jafrani, FSA, FCIA | Senior Manager | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 2975 | Cell Phone: +1 647 885 9630
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PS 3250.pdf

Canada Accounting & Auditing
Chartered Professional Accountants of Canada (CPA Canada, CSRA and CAARS)
CPA Canada Standards and Guidance Collection
Public Sector Accounting
Public Sector Accounting Standards
Specific Items — Financial Statement Items [PS 3030 — PS 3510]
PS 3250 Retirement benefits

PS 3250 Retirement benefits

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Purpose and scope

.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.

.002 In this Section, terms that appear in **bold type** are defined in the glossary of terms.

.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.

.004 If employees and/or retirees are covered by more than one **retirement benefit plan**, then a government needs to determine its obligation separately for each plan.

.005 The standards in this Section are based on the accounting framework recommended in FINANCIAL STATEMENT OBJECTIVES, Section PS 1100, and FINANCIAL STATEMENT PRESENTATION, Section PS 1201. That framework emphasizes the need to account for all liabilities incurred by a government to help legislators, taxpayers, investors and other users of **financial statements** assess: a government's future cash requirements from taxes and other revenues; its ability to meet financial obligations, both short-term and long-term; and its ability to maintain current services and finance new programs. Such assessments are essential when making financial decisions in government and when evaluating those decisions.

.006 Accounting for all of the retirement benefits incurred by governments is

particularly important because many of those governments have accumulated significant liabilities. Many governments have chosen not to set aside funds to meet retirement benefit payments when they become due. Where those liabilities have not been recorded, financial statements do not adequately provide all of the information needed by users to help them assess a government's financial position and results of operations. It is important that financial statements account for a government's liabilities for all retirement benefits to show clearly the extent to which these obligations are to be paid from cash to be raised from future tax and other revenue sources.

.007 The basis for determining obligations for retirement benefits set out in this Section is also appropriate for determining a government's contractual obligations arising from guarantees or commitments to employee retirement benefit plans of other public sector organizations that are not part of the government reporting entity. Such obligations exist, for example, when a provincial government agrees to guarantee defined retirement benefits for employees of local school boards, agrees to guarantee a minimum rate of return on retirement benefit fund assets, or agrees to provide a significant portion of the funds required by a plan sponsor. A careful reading and evaluation of such agreements is necessary to determine the substance of the obligation and whether a **liability**, **contractual obligation** or **contingency** exists that would be reported in a government's financial statements.

The objectives of funding and accounting

.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An **actuarial valuation for funding purposes** is performed to calculate the contributions required to secure the benefits promised.

.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. Accordingly, it is necessary to develop accounting estimates of liabilities for retirement benefits and expenses using an **actuarial cost method** and **actuarial assumptions** that ensure essential information required for fair presentation of financial condition and results of operations can be reported in government financial statements.

.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.

Defined benefit and defined contribution plans

.011 Two types of benefit plans are addressed in this Section — **defined benefit plans** and **defined contribution plans**. A defined benefit plan

is one that specifies either the benefits to be received by employees after retirement or the method for determining those benefits. Generally, the amount and value of the benefits to be paid depend on a number of factors and events. These include how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation and retirement age. When a government provides benefits under a defined benefit plan, it is at risk with respect to the amount of the benefit that each employee will receive (actuarial risk) and with respect to the investment returns on any assets set aside to pay for the cost of these benefits (investment risk).

.012 When a government provides benefits under a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. A defined contribution plan (or money purchase plan) is one in which a government's contributions in respect of services rendered by employees are specified. The government is required by the plan to make a specific fixed contribution each period. If that contribution is made, no additional government contributions are required now or in the future for the related service. The employees are at risk. This is generally because the amount of the benefit that will be payable to an employee is dependent upon the funds accumulated for each employee's account and the investment earnings on the accumulated funds.

.013 Because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of a particular plan makes it a defined benefit or a defined contribution plan.

.014 In some circumstances, a benefit plan may include both defined benefit and defined contribution promises. The plan, for example, may guarantee a basic defined retirement benefit and state that additional benefits, such as inflation protection, will be provided on a defined contribution basis. In such circumstances, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan. Once the type(s) of promise is identified, the accounting and reporting principles in this Section would be followed accordingly.

Defined benefit pension plans

Liability and expense

.015 Obligations for retirement benefits result from a promise by a government to provide retirement benefits to employees because of retirement in return for their services. The obligations arise as employees render services. Therefore, as employees render services, the value of the retirement benefits attributed to those services would be recorded as a liability and expense as are other forms of current compensation.

.016 *The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date.* [SEPT. 2001]

.017 The components of the **retirement benefit liability** are:

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

(b) **plan assets**, if any; and

(c) unamortized **actuarial gains and losses**.

.018 The cost of retirement benefits promised during the period is comprised of the **retirement benefits expense**, and the **retirement benefits interest expense**.

.019 The components of the retirement benefits expense are:

(a) **current period benefit cost**;

(b) cost of plan amendments incurred during the period;

(c) net actuarial gains or losses recognized in the determination of the cost of a plan amendment in accordance with paragraphs PS 3250.068 and PS 3250.071;

(d) gains and losses arising from plan settlements and curtailments incurred during the period;

(e) amortization of actuarial gains and losses;

(f) the amount recognized as a result of a temporary deviation from the plan, determined in accordance with paragraph PS 3250.073;

(g) the change in a valuation allowance against the carrying amount of an **accrued benefit asset**, determined in accordance with paragraph PS 3250.050; less

(h) employee contributions made during the period.

.020 The retirement benefits interest expense is the net of:

(a) the interest cost on the accrued benefit obligation determined by applying the discount rate determined at the beginning of the period in accordance with paragraph PS 3250.044 to the average value of the accrued benefit obligation for the period; and

(b) the expected return on plan assets for a defined benefit plan, determined by applying the assumed rate of return on plan assets to the average market-related value of assets for the period.

.021 The retirement benefits expense and the retirement benefits interest expense would be disclosed separately in the notes to the financial statements. A separate disclosure is needed to ensure that the amount reported as the retirement benefit expense is not affected by the purely financial decision of a government to fund or not fund the plan.

Actuarial cost methods

.022 Accounting for retirement benefits on the basis of employee services reflects the fact that there is no obligation for an employee when hired and that an obligation for retirement benefits exists as the employee renders service. The accounting task is to determine how to attribute the cost of the total retirement benefits promised to each period of employee service.

.023 For defined benefit plans, there are two main groups of actuarial cost methods. They are **level cost methods** and **accrued benefit methods**. Under the level cost methods, retirement benefit expenses are computed in such a manner as to produce a total current period benefit cost that remains constant, either in absolute dollars or as a percentage

of salary, throughout an employee's service life. However, level cost methods are not recommended for accounting purposes because they do not reflect the cost of benefits earned by employees to the financial statement date.

.024 Under the accrued benefit methods, a distinct unit of retirement benefit is associated with each year of employee service rendered to the financial statement date. The actuarial present value of that unit of benefit is computed separately for the period during which it accrued. These methods are recommended because they reflect more directly the cost of retirement benefits earned by employees to the financial statement date.

.025 *An accrued benefit method should be used to attribute the cost of retirement benefits to the periods of employee service.* [SEPT. 2001]

.026 For certain **flat benefit retirement plans**, benefits vary only with periods of service rendered. For those plans, future salary and wage changes do not enter into the determination of the cost of retirement benefits earned to the financial statement date. For other defined benefit plans, such as **final pay retirement plans**, future salary and wage changes need to be incorporated into the cost of retirement benefits earned to the financial statement date because the benefit promise is based on future salary and wage levels. To estimate those levels, forecasts are needed of future inflation rates and of future salary increases. Similarly, for retirement medical plans, forecasts are needed of medical inflation rates.

.027 Accounting for the effect of future salary and wage changes ensures consistency when determining the present value of the cost of the retirement benefits earned to the financial statement date, i.e., the accrued benefit obligation. Because the discount rate used to determine that obligation includes an inflation component, for consistency the amount of the retirement benefits to be discounted must also include an inflation component. If only the discount rate used to determine the obligation includes an inflation component, then the accrued benefit obligation and expense would be understated significantly.

.028 One accrued benefit method that incorporates the effect of future salary and wage changes and attributes the value of retirement benefits to the years of employee service is the **projected benefit method prorated on services**. Under this method, generally an equal portion of the total estimated benefit, with salary projection for final pay plans and projection of medical inflation for retirement medical plans, is attributed to each year of service. The actuarial present value of the accrued retirement benefits is derived after the benefits are attributed to the years of service up to the financial statement date.

.029 *The projected benefit method prorated on services should be used to attribute the cost of retirement benefits to the periods of employee service.* [SEPT. 2001]

.030 When a retirement plan provides benefits that accrue in a non-uniform manner, the projected benefit method prorated on services may need to be adjusted to reflect the manner in which retirement benefits are earned by employees. For example, a pension plan formula may state that the pension benefit accrues at one percent of salary for the first 15 years and at two percent of salary for the final 20 years. In this circumstance, the prorating of the total estimated benefit to each accounting period would be adjusted to reflect the rates at which pension benefits are earned in that 35-year period.

.031 In some retirement plans, benefits promised in a contractual agreement or in legislation include inflation protection for current and future retirees and for former employees who have **vested** retirement benefits. For those plans, it is necessary to incorporate the impact of inflation protection in the determination of the cost of retirement benefits earned to the financial statement date.

.032 In other retirement plans, regular benefit increases for inflation protection may be provided even when such protection is not promised in a contractual agreement or in legislation. For those plans, careful analysis and professional judgment are needed to determine the substance of a government's obligation. If a regular pattern of benefit increases can be established over a reasonable period, it may be appropriate to incorporate the cost of such inflation protection in the cost of retirement benefits earned to the financial statement date and reported as an accrued benefit obligation.

Asset valuation

.033 The periodic valuation of plan assets is important because, to determine its retirement benefit liability and expense, a government needs to value the assets set aside for the purpose of meeting benefit payments.

.034 Most government plans require contributions from the employees as well as from the sponsoring government. Some governments place those contributions in a separate fund, which invests them in marketable assets. Those contributions and earnings are used to meet benefit payments to current and future retirees.

.035 When determining a government's retirement benefit liability and expense, plan assets would be valued at market-related values. Under this method, plan assets are recorded at market value or they are adjusted to market value over a period not to exceed five years. Values adjusted to market closely approximate current economic value in a manner that can minimize short-term fluctuations. Market-related values would be used because they are objective and verifiable. Once a basis of valuation is chosen it would be applied consistently.

.036 For some assets, such as real estate investments or non-marketable securities, market values are not readily available. For such assets, a method that approximates market can be used. For example, independent appraisals could be obtained, market values of similar properties could be reviewed, or future expected cash flows discounted at a market rate could be determined.

.037 *For a defined benefit plan, plan assets should be valued at market-related values.* [SEPT. 2001]

.038 In some cases governments issue non-marketable securities to their benefit funds on the condition that those securities are held in the fund to maturity. Market-related values for these assets may not be readily determinable. In such cases, non-marketable securities can be valued at cost.

Measurement date

.039 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and

as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Actuarial assumptions

.040 Accounting for retirement benefit obligations of defined benefit plans requires forecasts of future events, such as inflation rates, investment returns, interest rates, wage and salary increases, medical inflation and employee turnover and mortality. Such forecasts form the basis of actuarial assumptions.

.041 Each key actuarial assumption would be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation. The assumptions would take into account the expected long-term experience of the plan and the short-term forecast. Such an approach ensures that the reported accrued benefit obligation and expense recognize the long-term nature of retirement benefit promises as well as the experience of the plan expected in the short term. Assumptions about the long-term future, however, are not to be unduly influenced by the experience expected in the short term. At each actuarial valuation, assumptions need to be reassessed; they would be revised if expectations about the future change. All assumptions are based on the presumption that the plan will continue in effect in the absence of evidence to the contrary.

.042 *Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts.* [SEPT. 2001]

.043 One commonly used approach that meets this standard is the use of streamed rate assumptions. Under the streamed rate approach, the short-term forecast of fund asset earnings, for example, would reflect the rates of return that assets currently held in the fund will earn until their maturity. As those assets mature, assumptions about their expected earnings on reinvestment would move to the expected long-term rate. Similarly, there would be streamed rate assumptions for salary increases.

.044 The actuarial assumptions underlying the valuation of the retirement benefit liability and expense would be internally consistent. For example, when a government determines its discount rates by reference to its plan asset earnings, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the short-term forecast of rates of return on assets currently held in the fund. When a government determines its discount rates by reference to its cost of borrowing, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the specific rates of interest and the periods committed to by the government on the amounts borrowed.

.045 *Actuarial assumptions should be internally consistent.* [SEPT. 2001]

.046 Internally consistent assumptions about future inflation rates are particularly important because of the significant impact those rates have on the reported accrued benefit obligation and related expenses. The same assumptions about future inflation need to be used when forecasting future rates of return on fund assets, future costs of borrowing and future salary and wage increases, and when determining the appropriate discount rates. In addition, methods of developing actuarial assumptions need to be consistent over time.

.047 Measurement of the cost of future medical benefits requires assumptions about the level and frequency of future claims and the cost of meeting those claims. The level and frequency of claims are particularly sensitive to the age of employees (and their beneficiaries) and may be sensitive to other factors, such as gender and geographical location. A government estimates future medical costs on the basis of historical data about its own experience, supplemented when necessary by historical data from other entities, insurance enterprises, medical providers or other sources. Historical data is adjusted to reflect any differences in demographic mix of the population or when there is reliable evidence that historical trends will not continue.

.048 Certain medical claims may be covered by governmental programs under existing law or by other providers of health care benefits. Benefit coverage by governmental programs is assumed to continue as provided by the present law and by other providers pursuant to their present plans.

.049 When making assumptions about future events, a government would obtain expert assistance from internal or external sources. One source of expert assistance is the **actuary** carrying out the actuarial computations. Periodic assessments are needed to ensure that the assumptions continue to be relevant.

Limit on the carrying amount of an accrued benefit asset

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

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

.054 The adjusted benefit asset is then compared to the **expected future**

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

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

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

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

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

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

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

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

Actuarial gains and losses

.060 The periodic actuarial valuation of a government's obligation for

retirement benefits will usually determine that adjustments are required due to experience different from that assumed or to changes in actuarial assumptions. Adjustments are needed when the actual experience of the benefit plan is different than that expected. Adjustments due to changes in actuarial assumptions are needed when a government believes revised assumptions are necessary to reflect a relatively permanent change in expected experience or to reflect new information. Adjustments are inevitable because the actuarial valuation requires ongoing forecasts of uncertain future events.

.061 Actuarial gains and losses would be amortized over a reasonable future period because of their tentative nature and because further adjustments will likely be required in the future. A reasonable future period is the **expected average remaining service life of the related employee group**. Amortization may commence in the period following the determination of the adjustment. Actuarial gains and losses would be determined on a market value basis or a basis adjusted to market value, consistent with paragraph PS 3250.035.

.062 *Except in the circumstances in paragraph* PS 3250.068*,* PS 3250.071 *and* PS 3250.078*, actuarial gains and losses should be amortized to the liability or asset and the related expense in a systematic and rational manner over the expected average remaining service life of the related employee group.* [SEPT. 2001]

Prior period service costs arising from plan amendments

.063 A plan amendment occurs when a benefit plan is changed or initiated. In such circumstances, retroactive credit may be given to employees for services rendered previously and, as a result, **prior period service costs** are incurred. For example, if the benefit formula is changed from one percent to two percent of final pay per year of service, the extra one percent may be credited to employees for years of service prior to the change.

.064 Plan amendments include the inception of a new plan that grants retroactive credit for past service, an increase in benefits related to past service for active employees, or an increase in benefits for former employees already retired.

.065 The cost of plan amendments related to prior period employee services would be accounted for as an expense in the period of the plan amendment. This method is recommended because it ensures that, when a government provides retroactive credit to employees for past services, legislators, taxpayers and investors are provided a full accounting of the cost of that decision in the period the decision is made. Such an accounting ensures that the effect of that decision, as it relates to the cost of prior period services, is recognized as an expense in the period a liability is incurred. It also provides information needed to assess the extent to which future revenues are required by a government to pay for past transactions because all retirement benefit liabilities are accounted for in the financial statements.

.066 *The cost of plan amendments related to prior period employee services should be accounted for in the period of the plan amendment.* [SEPT. 2001]

.067 While all plan amendments related to prior period employee services are accounted for in the period of the plan amendment, the existence of the plan amendment may affect the recognition of actuarial gains, as

described in paragraph PS 3250.068.

.068 *In the period of a plan amendment related to prior period employee services that results in an increase in the accrued benefit obligation, if net unamortized actuarial gains exist, these should be recognized immediately, to a maximum of the prior period service cost, and offset against the prior period service cost in the statement of operations, with separate disclosure in the notes.* [SEPT. 2001]

.069 When a government makes a plan amendment related to prior period employee services and has net unamortized actuarial gains, it would recognize these net unamortized actuarial gains immediately in the statement of operations, to a maximum of the prior period service cost. Recognition would be applied first to the oldest net unamortized actuarial gains within a plan. These actuarial gains would be deducted from the prior period service cost in the statement of operations. The notes to the financial statements would disclose this information.

.070 A plan amendment may decrease, rather than increase, a government's accrued benefit obligation. A decrease in the accrued benefit obligation would be accounted for immediately in the period of the plan amendment. The existence of the plan amendment may affect the recognition of actuarial losses as described in paragraph PS 3250.071.

.071 *In the period of a plan amendment related to prior period employee services that results in a decrease in the accrued benefit obligation, if net unamortized actuarial losses exist, these should be recognized immediately, to a maximum of the decrease in the accrued benefit obligation. The net amount would be recognized in the statement of operations, with separate disclosure in the notes.* [SEPT. 2001]

.072 In the period of a plan amendment that decreases the accrued benefit obligation any net unamortized actuarial losses would be recognized immediately to a maximum of the decrease in the accrued benefit obligation. Recognition would be applied first to the oldest unamortized net actuarial losses within a plan.

Temporary deviation from the benefit plan

.073 A government may decide to deviate temporarily from the provisions of a benefit plan to increase or decrease the government's share of the benefit costs incurred in the current period or past periods. For example, a government may grant an employee contribution holiday as a temporary deviation from the normal terms of the benefit plan. A government would look to the substance of the temporary deviation to determine the most appropriate accounting.

Plan settlements and curtailments

.074 A **plan settlement** and a partial plan settlement consist of the discharge, in whole or in part, of a government's obligation existing under a retirement benefit plan. They are irrevocable events by which a government or a plan is relieved of the primary obligation to pay all or some of the benefits promised and is relieved of significant risks in relation to the obligation or the assets used to make settlement. When a full plan settlement occurs, a future actuarial valuation is not required because the government no longer has an obligation related to that plan. Because the cost of discharging the obligation may differ from the related liability recognized previously, a gain or loss may arise.

.075 A **plan curtailment** is an event that reduces significantly the expected

years of future service of present employees or eliminates, for a significant number of employees, the accrual of defined benefits for some or all of their future services. Plan curtailments include termination of a significant number of employees earlier than expected which may involve eliminating a government organization or program; they also include suspension of a plan so that a significant number of employees do not earn additional defined benefits for future services. When a plan curtailment occurs, future actuarial valuations are required because, even though the government's future obligations have been reduced, the government continues to have an obligation related to that plan.

.076 Generally, the act of settling or curtailing a retirement plan will result in a gain or loss because the actual cost of the settlement or curtailment will differ from the obligation recorded previously. Gains and losses determined upon a plan settlement or curtailment would be accounted for in the statement of operations in the period of the settlement or curtailment. This approach is recommended for plan settlements because the amount of the liability is known, it relates to services previously provided and it has been settled. Similarly, if a government settles only a part of a retirement plan obligation, the related gains and losses would be recognized immediately. This approach is also recommended for plan curtailments because the retirement benefit obligation is known with greater certainty, it relates to past employee services and the employees might no longer work for the government. For plan curtailments, the portion of the total gains and losses that would be accounted for would relate to the employees affected by the curtailment.

.077 In some circumstances, there will be unamortized actuarial gains and losses incurred prior to the plan settlement or curtailment. The net unamortized balances related to the obligation settled or to the employees affected by the curtailment would be recognized in the period of settlement or curtailment, and is included as part of the gain or loss arising on settlement or curtailment.

.078 *Gains and losses determined upon a plan settlement or curtailment should be accounted for in the period of the settlement or curtailment.* [SEPT. 2001]

Joint defined benefit plans

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

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

the definition of a joint defined benefit plan.

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]

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

Disclosure

.083 The notes and schedules integral to the financial statements would disclose the methods and judgments applied in accounting for accrued benefit obligations and expenses. Full disclosure is particularly important for retirement obligations because the measurements depend heavily upon judgments rather than objective evidence.

.084 *Financial statements should disclose:*

(a) a general description of retirement benefit plans, benefit formulae and funding policy, including a description of significant changes to retirement benefit plans during the period;

(b) the accrued benefit obligation at the end of the period, as determined by the actuarial valuation;

(c) the market value of plan assets at the beginning and the end of the period and, if different, the market-related value of plan assets at the beginning and the end of the period;

(d) the amount of retirement benefit liability or accrued benefit asset at the end of the period, indicating separately the amount of any valuation allowance determined in accordance with paragraph PS 3250.050*.*

(e) unamortized actuarial gains and losses and the periods of amortization;

(f) current period benefit cost;

(g) cost of plan amendments incurred during the period;

(h) net actuarial gains or losses recognized in the determination of the cost of plan amendments in accordance with paragraphs PS 3250.068 *and* PS 3250.071*;*

(i) other gains and losses on accrued benefit obligations arising during the period;

(j) other gains and losses on plan assets arising during the period;

(k) gains and losses arising from plan settlements and curtailments incurred during the period;

(l) amortization of actuarial gains and losses reflected in the current

year expense;

(m) the amount recognized as a result of a temporary deviation from the plan, determined in accordance with paragraph PS 3250.073*;*

(n) the change in a valuation allowance determined in accordance with paragraph PS 3250.050*;*

(o) the amount of contributions by employees during the period;

(p) the components of the retirement benefits interest expense for the period;

(q) the amount of contributions by the government during the period;

(r) the amount of benefits paid during the period;

(s) the expected return and actual return on plan assets during the period;

(t) assumptions about long-term inflation rates, expected rate of return on plan assets, assumed health care cost trends, rate of compensation increase (for pay-related plans) and discount rate; and

(u) the date of the most recent actuarial valuation performed for accounting purposes. [SEPT. 2001]

.085 Some of this disclosure information may be presented in reconciliations of the beginning and ending balances of the accrued benefit obligation and plan assets for the period, taking into account any unamortized actuarial gains or losses existing at the financial statement date.

.086 A reconciliation of the beginning and ending balances of the accrued benefit obligation would include the items disclosed in accordance with paragraph PS 3250.084(b), (i), (k) and (o)-(r). A reconciliation of the beginning and ending balance of plan assets for the period would include the items disclosed in accordance with paragraph PS 3250.084(c), (f)-(g), (j)-(k), (m), (o)-(p) and (r).

.087 *A government should provide these disclosures separately for plans that provide pension benefits and plans that provide retirement benefits other than pensions.* [SEPT. 2001]

.088 *A government that has aggregated disclosures for its defined benefit pension plans, or for its other defined benefit retirement plans, should provide the disclosures separately for the aggregate of plans with accrued benefit obligations in excess of plan assets.* [SEPT. 2001]

.089 The level of detail disclosed by governments would reflect the highly aggregated nature of financial statements. In deciding the level of detail to disclose, governments would consider the usefulness of the information to the reader in assessing the nature of, and the costs associated with, a government's retirement benefit plans. The level of disclosure would also consider the sensitivity of the information in relation to the government's financial position.

.090 The description of the significant benefit plans and benefit formulae might include the plan surplus or deficit at the end of the period, demographic information about the participants and whether the benefit obligation includes the cost of inflation protection. The description of the funding policy might include the major types of plan assets and the basis of their valuation. The extent to which the fund holds securities of the

sponsoring government would normally be disclosed.

.091 Governments are encouraged to provide additional disclosures about the significant actuarial assumptions underlying the reported amount of a government's accrued benefit obligation when the disclosures will enhance the financial statement users' understanding of that amount.

.092 A government may also choose to disclose a forecast of the cash required to pay its retirement benefit obligations in the short term, the medium term and the long term. If provided, such a forecast would include the amounts required in the next five years, and thereafter.

.093 *For joint defined benefit plans, in addition to the disclosures required in paragraphs* PS 3250.084 *government financial statements should disclose:*

(a) the significant accounting policies for joint plans;

(b) a description of the unique nature and terms of any joint plans;

(c) the government's share of the risks and benefits under the plans; and

(d) the total financial status of any joint plans. [SEPT. 2001]

.094 Users of government financial statements need an appreciation of the magnitude of the retirement benefit plans that governments jointly sponsor and the government's responsibility under the terms of any joint plans.

Defined contribution plans

.095 When a government establishes a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. The government typically agrees to contribute a certain amount in each period for services rendered by the employees and has no responsibility to make any further contributions. It is the employees who are at risk. This is generally because the amount of the benefit that will be payable to them is entirely dependent upon the amount of funds accumulated for each employee's account and the economic conditions prevailing at the retirement date (see paragraphs PS 3250.011-.014 for a further discussion of defined contribution plans).

Liability and expense

.096 For the most part, defined contribution plans do not present particular accounting problems. If the formula calls for government contributions on a regular predetermined basis and if those contributions have been made, then the expense recorded in the statement of operations is simply the required contribution of the accounting period. If the contributions have not been made as required, the retirement benefit expenses would include interest accrued during the period on any outstanding amounts payable to the fund. The liability for retirement benefits recorded in the statement of financial position would be the difference between the amount the government was required to contribute and the amount that was contributed to the financial statement date, including accumulated interest on any outstanding amounts payable to the fund at the financial statement date.

.097 *For defined contribution plans:*

(a) *the liability for retirement benefits should be the difference between the amount a government was required to contribute and the amount that was contributed by the financial statement date including accumulated interest on any outstanding amounts payable to the fund at the financial statement date;*

(b) *the retirement benefit liability should be accounted for in the statement of financial position;*

(c) *the expense for retirement benefits should be the amount of required contributions provided for employees' services rendered in the period. Interest accrued during the period on any outstanding amounts payable to the fund should be accounted for as a retirement benefit interest expense; and*

(d) *the retirement benefit expense and the retirement benefit interest expense should be accounted for in the statement of operations.* [SEPT. 2001]

.098 When a defined contribution plan is amended, a government may agree to make contributions in respect of past service. The cost of current and expected future years' contributions related to a past service plan amendment is recognized immediately in the period the decision is made to amend the plan.

.099 *For a defined contribution plan, the cost of current and expected future years' contributions related to a past service plan amendment should be accounted for in the period of the plan amendment.* [SEPT. 2001]

Disclosure

.100 *For defined contribution plans, financial statements should disclose:*

(a) *a general description of benefit plans, contribution formulae and funding policy;*

(b) *the expense recognized for the period; and*

(c) *a description of significant changes to benefit plans during the period.* [SEPT. 2001]

.101 The description of the significant retirement benefit plans and contribution formulae might include demographic information about the participants.

.102 The description of the funding policy might also include: the employee and government contributions during the accounting period; the major types of plan assets, the total amounts and the basis of their valuation; and the extent to which the fund holds securities of the sponsoring government.

.103 The description of significant changes to the plan or to the financing of the plan might also include which employee group(s) is affected and a description of the impact of such changes on current and future retirement benefit liabilities and related expenses.

.104 The level of detail disclosed by governments would reflect the highly aggregated nature of financial statements. In deciding the level of detail to disclose, governments would consider the usefulness of the information to the reader in assessing the nature of, and the costs associated with, a government's retirement benefit plans. The level of disclosure would also consider the sensitivity of the information in

relation to the government's financial position.

Multiemployer and multiple-employer benefit plans

Multiemployer plans

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

.106 The federal and most provincial governments sponsor defined benefit plans in which many public sector organizations participate. Many local governments participate in such multiemployer plans. When benefits are provided to employees through a multiemployer plan, the amount for which an individual government is obligated under the plan may not be quantified. Generally, a contribution rate is established for each period to ensure that the plan assets are adequate to cover the plan's future benefit payments.

.107 When a government sponsors a defined benefit multiemployer retirement benefit plan, it has the responsibility to ensure that the defined benefits promised to employees are met. In that circumstance the sponsoring government is at risk for future experience gains or losses and would account for its related obligation for the entire multiemployer plan as a defined benefit plan.

.108 *When a government sponsors a defined benefit multiemployer retirement plan, the government should follow the standards for defined benefit plans in accounting for its obligation for the plan.* [SEPT. 2001]

.109 Although a multiemployer plan may have the characteristics of a defined benefit plan, sufficient information to follow the standards for defined benefit plans is normally not available for each participating employer other than the sponsoring government. For this reason, a multiemployer plan is accounted for by each participating government following the standards for defined contribution plans.

.110 *When benefits are provided to employees through a multiemployer retirement benefit plan, each entity participating in the plan, other than the sponsoring government, should follow the standards for defined contribution plans.* [SEPT. 2001]

.111 *The government should disclose any available information about any surplus or deficit in a multiemployer plan, the basis used to determine the surplus or deficit and the implications, if any, for the government.* [SEPT. 2001]

Multiple-employer plans

.112 A **multiple-employer plan** is a defined benefit plan maintained by more than one entity that is not a multiemployer plan. In contrast to multiemployer plans, a multiple-employer plan maintains separate accounts for each entity so that contributions provide benefits only for employees of the contributing entity. In addition, multiple-employer plans are intended to allow participating entities, commonly in the same

industry, to pool their plan assets for investment purposes and to reduce the cost of plan administration. Multiple-employer plans may have features that allow participating entities to have different benefit formulae, with the entity's contributions to the plan based on the benefit formula selected by the entity.

.113 When benefits are provided to employees through a defined benefit multiple-employer plan, each government in the plan follows the standards on defined benefit plans and bases its accounting for plan assets on its proportionate interest in the assets of the multiple-employer plan.

.114 *When benefits are provided to employees through a defined benefit multiple-employer retirement plan, each entity in the plan should follow the standards for defined benefit plans.* [SEPT. 2001]

Transitional provisions

.115 When implementing this Section, governments may have an initial unrecorded liability.

.116 The initial unrecorded liability would be accounted for as a change in accounting policy applied retroactively. This method is recommended because it ensures that all liabilities incurred to the financial statement date are accounted for in the statement of financial position. Such an accounting is needed to help users of financial statements assess the impact those liabilities may have on:

(a) a government's future cash requirements from revenues and other sources;

(b) a government's ability to meet its financial obligations, both short-term and long-term; and

(c) a government's ability to maintain the level and quality of its services and to finance new programs.

.117 *This Section should be accounted for as a change in accounting policy applied retroactively.* [SEPT. 2001]

Timing of actuarial valuations

.118 Most governments do not have full actuarial valuations performed annually because of the magnitude of the information gathering and processing required. **Actuarial valuations for accounting purposes** would generally be done once every three years because of the financial importance of retirement benefit obligations. They would be done as close to the related financial statement date as is practical. In the years between valuations, an extrapolation would be used to compute the expected accrued benefit obligation and related expenses. Each year the government reviews matters such as changes to the plan, the actuarial assumptions, occurrence of settlements and curtailments, changes to the employee group and the rate of return on plan assets, and determines whether such matters necessitate any adjustments to the extrapolations. When the effect of any change is significant, a new valuation may be necessary.

.119 In the period a government implements this Section, it would need to assess whether a new actuarial valuation of its retirement benefit obligations is needed. A new valuation would be needed, for example, if the prior one is not current or is not prepared in accordance with this

Section.

Glossary

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

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

Actuarial assumptions are made as to the occurrence of a future event that will affect retirement benefit costs and obligations. They include assumptions about such matters as mortality, withdrawal, disability and retirement and about changes in compensation, interest on obligations and investment earnings.

Actuarial cost methods are used to determine the cost of providing retirement benefits and to allocate that cost to specific time periods. The two main families of actuarial valuation methods are:

Accrued benefit methods (also known as unit credit or single premium actuarial cost methods) — Under these methods a distinct unit of retirement benefit is associated with each year of credited service and the actuarial present value of that unit of benefit is separately computed for the period during which it is presumed to have accrued. Salary projection, when appropriate, is required.

Projected benefit method prorated on services — Under this accrued benefit method, generally an equal portion of the total estimated benefit (i.e., with salary projection, when appropriate) is attributed to each year of service. The actuarial present value of the accrued retirement benefits is derived after the benefits are attributed to the years of service up to the date of determination.

Level cost methods — Under these methods the retirement benefit cost assigned to any period is either the same dollar amount or the same percentage of compensation as any other period, and is a portion of the cost of the total prospective benefits of an employee group, either in absolute dollars or as a percentage of salary. (Entry age, attained age and aggregate actuarial cost methods are included in this family of methods.)

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

(a) experience different from that assumed; or

(b) changes in an actuarial assumption.

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

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

An **actuary** is a Fellow of the Canadian Institute of Actuaries.

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

A **contingency** is the result of an existing condition or situation involving uncertainty that will ultimately be resolved when one or more future events occur or fail to occur. Resolution of the uncertainty may confirm the acquisition of an asset or the reduction of a liability or the loss or impairment of an asset or the incurrence of a liability.

Contractual obligations are obligations of a government to others that will become liabilities when the terms of those contracts or agreements are met.

The **current period benefit cost** is the actuarial present value of benefits attributed to services rendered by employees in the period.

A **defined benefit plan** specifies either the benefits to be received by employees after retirement or the method for determining those benefits. The most commonly used defined benefit plans are:

Final pay plan — Bases benefits on an employee's length of service and compensation over a specified number of years (usually the years of an employee's highest earnings).

Flat benefit plan — Provides a specified benefit for each year of service rendered; the benefit earned in each period is usually fixed and determinable under the terms of the plan and the amount of benefits to be received varies only with the years of service rendered.

A **defined contribution plan** is one in which the employer's contributions are fixed, usually as a percentage of compensation, and allocated to specific individuals. The retirement benefit for each employee is the amount that can be provided at retirement based on the accumulated contributions made on that individual's behalf and investment earnings on those contributions.

The **expected average remaining service life (EARSL) of the related employee group** is the total number of years of future services expected to be rendered by that group divided by the number of employees in the group. The calculation of expected future services considers population decrements based on the actuarial assumptions but is not weighted by benefits or compensation.

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

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

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

Financial statements are summary financial statements published by a government that report on the financial position and changes in financial position of the government reporting entity. Such statements present aggregated information and serve as a means by which a government demonstrates its accountability for the financial affairs and resources entrusted to it.

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

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

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

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

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

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

Liabilities are present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits.

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

A **multiple-employer plan** is a defined benefit plan maintained by more than one entity that is not a multiemployer plan. In contrast to multiemployer plans, a multiple-employer plan maintains separate accounts for each entity so that contributions provide benefits only for employees of the contributing entity. In addition, multiple-employer plans are intended to allow participating entities, commonly in the same industry, to pool their plan assets for investment purposes and to reduce the cost of plan administration. Multiple-employer plans may have features that allow participating entities to have different benefit formulae, with the entity's contributions to the plan based on the benefit

formula selected by the entity.

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

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

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

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

A **plan curtailment** occurs when the expected years of future service to be rendered by the existing employee group are reduced significantly or when benefits will not be earned by employees for some or all future periods.

A **plan settlement** occurs when an employer legally discharges the obligation for accrued retirement benefits either by transferring assets directly to plan participants in exchange for their rights to retirement benefits or by purchasing annuity contracts in which a third party unconditionally undertakes to pay all accrued retirement benefits.

A **prior period service cost** is the increase in the accrued benefit obligation associated with past service benefit improvements.

The **retirement benefit expense** is the cost of the retirement benefits promised during the period in exchange for services rendered during the period.

The **retirement benefit interest expense** is the cost of financing an unfunded retirement benefit obligation during the period.

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

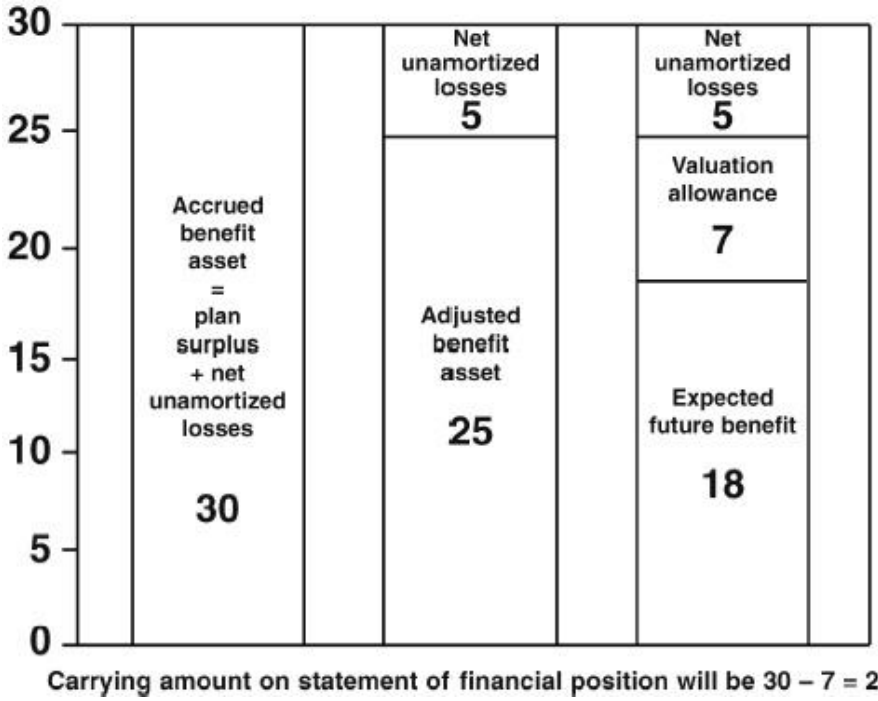
A **retirement benefit plan** is any arrangement (contractual or otherwise) by which a program is established to provide retirement income and other benefits to employees and/or retirees.

Retirement benefits are benefits expected to be provided after retirement to employees and their beneficiaries. These benefits include pension income, health care benefits, life insurance, and other miscellaneous benefits provided to employees after retirement.

Vesting is the recognition of the employees' rights to receive retirement benefits that are no longer conditional on the employees remaining in the service of the employer.

Appendix A — Limit on accrued benefit asset

Limit on accrued benefit asset



The carrying amount on the statement of financial position would be the accrued benefit asset of $30 less the valuation allowance of $7 for an amount of $23.

Appendix B — Illustrative examples

ILLUSTRATIVE EXAMPLES

The following examples have been prepared by CPA Canada staff to illustrate how the standards in Section PS 3250 might be implemented.

The examples are illustrative only and matters of principle relating to particular situations should be decided in the context of the Section. They are not intended to indicate preferred formats nor to prescribe standardized note disclosure, as variations in format and wording will be necessary to meet the requirements of differing circumstances.

For ease of presentation, selections are made from accounting alternatives permitted by the Section.

Example 1 — Defined benefit pension plan, assuming a separate pension fund is maintained

Example 2 — Defined benefit plan for retirement benefits other than pensions, assuming a separate fund is not maintained

Example 1 — Defined benefit pension plan, assuming a separate pension fund is maintained

The government sponsors contributory defined benefit pension plans for substantially all of its employees and for members of its Legislature. There are three main plans — the Public Service Plan, the Provincial Judges' Plan and the Elected Representatives' Plan. The Public Service and the Provincial Judges' plans provide for pensions equal to 1.5 percent of the average of the five highest years' salary for each year of service to a maximum of 35 years. The Elected Representatives' Plan provides for

pensions equal to four percent of the average of five years' session indemnities for each year of service to a maximum of 15 years. The plans do not provide inflation protection. The average age of the 45,000 active employees is 42. There are 5,000 former employees who are entitled to deferred pension benefits and 11,000 retirees now receiving benefits.

Each year employees contribute seven percent of their salary to a separate pension fund and the government contributes an equal amount. While the government and employees are required to contribute equal amounts into the pension fund, the government retains the full risk of the accrued benefit obligation. The pension fund invests monies from the contributions in securities of organizations external to the government reporting entity as well as investing in some non-marketable bonds of the government.

At the beginning of fiscal year 20X1, an actuarial valuation of the government's employee pension obligations was done for accounting purposes using the projected benefit method prorated on services. The liability for pensions recorded in the statement of financial position was $400 million. For purposes of this example it is assumed that there were no unamortized actuarial gains or losses at that time.

Key actuarial assumptions used in the valuation were based on the government's best estimates. Those assumptions involve forecasts of expected future inflation rates, investment returns, wage and salary increases, and employee turnover and mortality. A second actuarial valuation for accounting purposes was performed at the end of fiscal year 20X3. During the second valuation, the actuarial assumptions included in the first one were reviewed and no changes were considered necessary.

During fiscal 20X4, a plan amendment was made to the Public Service Plan increasing the benefits from 1.5 percent to two percent of the average of the five highest years' salary for each year of service to a maximum of 35 years. The plan amendment was effective March 31, 20X4 and relates to both future and past services. The government is responsible for funding the pension liability of $25 million related to past services over the next 12 years. The increase in current period benefit costs due to rendering of service for fiscal 20X5 was $1.5 million.

	April 1, 20X0	March 31, 20X3
Accrued benefit obligation	$1.5 billion	$2.2 billion
Pension fund asset	$1.1 billion	$1.8 billion
Pension liability recorded in the statement of financial position	$ .4 billion	$ .4 billion
	========	========
Expected average remaining service life of related employee groups (EARSL)		12 years
Plan amendment March 31, 20X4		$25,000

Expected current period benefit cost:		
20X1	$200 million	
20X2	$220 million	
20X3	$240 million	
20X4		$240 million
20X5		$250 million
20X5 related to plan amendment		$1.5 million
20X6		$260 million

Expected rates of return	8%
Expected salary escalations	5%
Expected inflation rates	3%

The following amounts related to other pension experience incurred throughout the period:

($ millions)	20X1	20X2	20X3	20X4
Employee funding contributions	110	115	120	126
Government funding contributions:				
— related to current service	110	115	120	126
Benefit payments to retirees	105	109	115	119

Exhibit I — Interest during the year on the average pension liability outstanding during the year

($ thousands)	20X1	20X2	20X3	20X4
Interest on expected average accrued benefit obligation:				
Accrued benefit obligation — opening balance (a)	1,500,000	1,718,800	1,971,744	2,200,000
Add: Current period benefit cost (b)	100,000	110,000	120,000	120,000
Deduct: Benefit payments (b)	(52,500)	(54,500)	(57,500)	(59,500)
Average accrued benefit obligation	1,547,500	1,774,300	2,034,244	2,260,500
Interest at 8% on average accrued benefit obligation	123,800	141,944	162,740	180,840

Expected earnings on average pension fund assets:				
Pension fund assets — opening balance (a)	1,100,000	1,417,600	1,598,048	1,800,000
Add: Employee and government funding contributions (b)	110,000	115,000	120,000	126,000
Deduct: Benefit payments (b)	(52,500)	(54,500)	(57,500)	(59,500)
Average pension fund assets	1,157,500	1,478,100	1,660,548	1,866,500
Expected earnings on average pension fund assets at 8%	92,600	118,248	132,844	149,320
Total interest during the period on the average pension liability outstanding during the period (c)	31,200	23,696	29,896	31,520

(a) In the period of an actuarial valuation, the opening balance of the accrued benefit obligation is the actuarially determined amounts (opening balances 20X1 and 20X4). In the periods between valuations (20X2 and 20X3), the opening balance is equal to the expected closing balance for the previous year as determined in Exhibit II. The opening balance of pension fund assets is the actual amount reported in the financial records of the fund.

(b) Accrued, or assumed to take place, evenly throughout the year, therefore interest is accrued on one-half of the total.

(c) Interest during the year on average pension liability outstanding during the year = 8% of [(average accrued benefit obligation) – (average pension fund assets)].

Exhibit II — Expected closing balance of accrued benefit obligation

($ thousands)	20X1	20X2	20X3	20X4
Accrued benefit obligation — opening balance	1,500,000	1,718,800	1,971,744	2,200,000
Add: Current period benefit cost	200,000	220,000	240,000	240,000
Increase due to plan amendment	—	—	—	25,000
Interest accrued (Exhibit I)	123,800	141,944	162,740	180,840
Deduct: Benefit payments	(105,000)	(109,000)	(115,000)	(119,000)
Expected closing balance	1,718,800	1,971,744	2,259,484	2,526,840

Exhibit III — Expected closing balance of pension fund

assets

($ thousands)	20X1	20X2	20X3	20X4
Pension fund assets — opening balance (actual)	1,100,000	1,417,600	1,598,048	1,800,000
Add: Employee and government funding and contributions	220,000	230,000	240,000	252,000
Expected earnings (Exhibit I)	92,600	118,248	132,844	149,320
Deduct: Benefit payments	(105,000)	(109,000)	(115,000)	(119,000)
Expected closing balance	1,307,600	1,656,848	1,855,892	2,082,320

Exhibit IV — Amortization of actuarial gains / losses on accrued benefit obligation

($ thousands)	20X1	20X2	20X3	20X4
Expected closing balance of accrued benefit obligation at March 31 (Exhibit II)	N/A	N/A	2,259,484	N/A
Actual accrued benefit obligation (per the March 31, 20X3 actuarial valuation)			2,200,000	
Actuarial gain			59,484	
EARSL			12 years	
Annual amortization over EARSL			4,957	

(a) A straight-line method is used to amortize actuarial gains and losses over the expected average remaining service life of the related employee groups. Amortization commences in the year following the effective date of the related actuarial valuation.

Exhibit V — Amortization of actuarial gains / losses on pension fund asset earnings

($ thousands)	20X1	20X2	20X3	20X4
Expected closing balance of pension fund assets at March 31 (Exhibit III)	1,307,600	1,656,848	1,855,892	2,082,320
Actual pension fund assets	1,417,600	1,598,048	1,800,000	2,142,320
Actuarial gain (loss)	110,000	(58,800)	(55,892)	60,000
EARSL	12 years	12 years	12 years	12 years
Annual amortization over EARSL	9,167	(4,900)	(4,658)	5,000

Exhibit VI — Unamortized actuarial gains and losses

($ thousands)	20X1	20X2	20X3	20X4
Unamortized actuarial gains and losses — opening balance	—	110,000	42,033	41,358
Actuarial gains (losses) due to:				
— accrued benefit obligation (Exhibit IV)	—	—	59,484	—
— earnings on pension fund assets (Exhibit V)	110,000	(58,800)	(55,892)	60,000
Amortization recorded during the year:				
— accrued benefit obligation (Exhibit IV)	—	—	—	(4,957)
— earnings on pension fund assets (Exhibit V)	—	(9,167)	(4,267)	391
— recognition of net unamortized actuarial gains as an offset to prior period service cost (a)	—	—	—	(25,000)
Unamortized actuarial gains and losses — closing balance	110,000	42,033	41,358	71,792

(a) When the cost of a plan amendment that improves a benefit related to prior service is offset against net actuarial gains, the cost is offset first against the oldest gains. Additionally, it is only offset against gains in the Public Service Plan.

Exhibit VII — Liability recorded in the statement of financial position

($ thousands)	20X1	20X2	20X3	20X4
Accrued benefit obligation — closing balance (a) (Exhibit II)	1,718,800	1,971,744	2,200,000	2,526,840
Deduct: Pension fund assets — closing balance (Exhibit III)	(1,417,600)	(1,598,048)	(1,800,000)	(2,142,320)
Unamortized actuarial gains / losses (Exhibit VI)	110,000	42,033	41,358	71,792
Pension liability	411,200	415,729	441,358	456,312

(a) In the period of an actuarial valuation, this is the actuarially determined amount (closing balance 20X3). In the periods between valuations, this is an expected closing balance.

Exhibit VIII — Expenses recorded in the statement of

operations

($ thousands)	20X1	20X2	20X3	20X4
Pension expense:				
Current period benefit cost	200,000	220,000	240,000	240,000
Prior period cost of plan amendment incurred during the year	—	—	—	25,000
Recognition of unamortized net actuarial gains	—	—	—	(25,000)
Amortization of actuarial gains / losses (Exhibit VI)	—	(9,167)	(4,267)	(4,566)
	200,000	210,833	235,733	235,434
Less: Employee contributions	(110,000)	(115,000)	(120,000)	(126,000)
Pension expense	90,000	95,833	115,733	109,434
Pension interest expense:				
Interest during year on the average pension liability outstanding during the year (Exhibit I)	31,200	23,696	29,896	31,520
Total pension-related expenses	121,200	119,529	145,629	140,954

Exhibit IX — Non-cash items recorded in the statement of cash flow

($ thousands)	20X1	20X2	20X3	20X4
Pension liability:				
— beginning of year (Exhibit VII)	400,000	411,200	415,729	441,358
— end of year (Exhibit VII)	411,200	415,729	441,358	456,312
Increase in pension liability	11,200	4,529	25,629	14,954

Financial Statement Disclosure

Illustrative Note to the Financial Statements

The government sponsors contributory defined benefit pension plans for substantially all of its employees and for members of its Legislature. There are three main plans — the Public Service Plan, the Provincial Judges' Plan and the Elected Representatives' Plan. The plans provide pensions based on length of service and final average earnings. They do

not provide for inflation protection. The average age of the 45,000 active employees covered by the plans is 42. There are 5,000 former employees who are entitled to deferred pension benefits. At present, the plans provide benefits for 11,000 retirees; benefit payments were $119 million in 20X4 and $115 million in 20X3.

Employees make contributions equal to seven percent of their salary and the government contributes an equal amount. In 20X4, total contributions for current year's service were $252 million (20X3 — $240 million). Total benefit payments to retirees during the year were $119 million (20X3 — $115 million). A separate pension fund is maintained. Pension fund assets are invested primarily in marketable investments of organizations external to the government reporting entity, with some invested in non-marketable bonds of the government. The pension liability at March 31 includes the following components:

($ thousands)	20X4	20X3
Accrued benefit obligation	2,526,840	2,200,000
Pension fund assets:		
Marketable securities	(1,942,320)	(1,610,000)
Government bonds	(200,000)	(190,000)
	384,520	400,000
Unamortized actuarial gains / losses	71,792	41,358
Pension liability	456,312	441,358

Actuarial valuations for accounting purposes are performed triennially using the projected benefit method prorated on services. The most recent actuarial report was prepared at March 31, 20X3. The accrued benefit obligation shown for 20X4 is based on an extrapolation of that 20X3 valuation. There is a net unamortized actuarial gain to be amortized on a straight-line basis over the expected average remaining service life of the related employee groups (12 years).

The actuarial valuation was based on a number of assumptions about future events, such as inflation rates, interest rates, wage and salary increases and employee turnover and mortality. The assumptions used reflect the government's best estimates. The expected inflation rate is three percent. The discount rate used to determine the accrued benefit obligation is eight percent.

Pension fund assets are valued at market values. The expected rate of return on plan assets is eight percent. The actual return on plan assets was 8.6 percent. Plan assets include government bonds valued at an estimated market value of $200 million (20X3 — $190 million).

The total expenses related to pensions include the following components:

($ thousands)	20X4	20X3
Current period benefit cost	240,000	240,000
Prior period cost of plan amendment	25,000	—

Recognition of net unamortized actuarial gains	(25,000)	—
Amortization of actuarial gains / losses	(4,566)	(4,267)
	235,434	235,733
Less: Employee contributions	(126,000)	(120,000)
Pension expense	109,434	115,733
Interest cost on the average accrued benefit obligation	180,840	162,740
Expected return on average pension plan assets	(149,320)	(132,844)
Pension interest expense	31,520	29,896
Total expenses related to pensions	140,954	145,629

The pension expense is included in the statement of operations as a component of program expenses. The pension interest expense is included in the public debt interest expense.

On March 31, 20X4, a plan amendment was made to the Public Service Plan increasing the rate at which pension benefits accrue. The amendment relates to both future and past service. The benefit accrual of $25 million is based on an actuarial valuation of the increase in the accrued benefit obligation due to past service. The government intends to fund this amount over a 12-year period ($1 million in 20X4).

Statement of Financial Position (excerpts)

As at March 31 ($ thousands)	20X4	20X3
Liabilities		
Accounts payable	x	x
Accrued liabilities	x	x
Borrowings		
Treasury bills	x	x
From other governments	x	x
Bonds payable to pension fund (note)	200,000	190,000
Other	x	x
Pension liability (note)	456,312	441,358
Total liabilities	x	x
Excess of liabilities over financial assets	x	x

Statement of Operations (excerpts)

For the year ended March 31 ($ thousands)		20X4	20X3
Expenses			
Health	(includes pension expense)	x	x
Education ...etc.		x	x
Public debt interest (includes pension interest expense)		x	x
		x	x
		=====	=====

Example 2 — Other retirement benefits plan

The government provides certain retiree health and life insurance benefits to its employees. The plan is unfunded and requires no contribution from employees.

In 20X3 the government adopted accrual accounting for the benefit plan. Prior to that date the government recognized benefit expenses equal to its payments for the actual costs incurred by the retirees and no liability for retirement benefits other than pensions was recorded in the statement of financial position.

At the beginning of fiscal year 20X3, an actuarial valuation of the government's obligations for retirement benefits other than pensions was done for accounting purposes using the projected benefit method prorated on services. Key actuarial assumptions used in the valuation were based on the government's best estimates. Those assumptions involve forecasts of expected future inflation rates, cost of long-term debt, employee mortality and medical costs. A second actuarial valuation for accounting purposes was performed at the end of fiscal year 20X5. During the second valuation, the actuarial assumptions included in the first one were reviewed and no changes were considered necessary.

($ thousands)	April 1, 20X2	March 31, 20X5
Accrued benefit obligation	100,000	150,000
Expected average remaining service life of related employee groups (EARSL)	12 years	
Plan amendment September 30, 20X5		10,000
Expected current period benefit cost:		
20X3	3,500	
20X4	3,800	

20X5	4,000	
20X6		4,000
20X6 related to plan amendment		500
20X7		5,200
20X8		5,400

Expected cost of long-term debt	8%	
Expected salary escalations	5.5%	
Expected medical inflation rates	10%	
Expected inflation rates	5.5%	

Benefit payments to retirees	20X3	2,500
	20X4	2,800
	20X5	2,900
	20X6	3,100

Exhibit I — Interest during the year on the average liability for retirement benefits other than pensions outstanding during the year

($ thousands)	20X3	20X4	20X5	20X6
Interest on expected average accrued benefit obligation:				
Accrued benefit obligation — opening balance (a)	100,000	109,040	118,803	150,000
Add: Current period benefit cost (b)	1,750	1,900	2,000	2,125
Increase in accrued benefit obligation due to plan amendment (c)	—	—	—	5,000
Deduct: Benefit payments (b)	(1,250)	(1,400)	(1,450)	(1,550)
Average accrued benefit obligation	100,500	109,540	119,353	155,575
	======	======	======	======
Interest at 8% on average accrued benefit obligation (d)	8,040	8,763	9,548	12,446

(a) In the period of an actuarial valuation, the opening balance of the accrued benefit obligation is the actuarially determined amounts (opening balances 20X3 and 20X6). In the periods between valuations (20X4 and 20X5), the opening balance is equal to the

expected closing balance for the previous year.

(b) Accrued, or assumed to take place, evenly throughout the year, therefore interest is accrued on one-half of the total.

(c) Since the plan amendment was effective mid-year, interest is earned for one-half of the year on the increase in accrued benefit obligation due to past service = ½ (10,000). Similarly, interest is earned on the increase in the current period benefit cost following the plan amendment. The average current period benefit cost in 20X6 is, therefore, = ½ (4,000) + ¼ (500).

(d) Interest during the year on average liability outstanding during the year = 8% of average accrued benefit obligation.

Exhibit II — Expected closing balance of accrued benefit obligation

($ thousands)	20X3	20X4	20X5	20X6
Accrued benefit obligation — opening balance	100,000	109,040	118,803	150,000
Add: Current period benefit cost	3,500	3,800	4,000	4,500
Increase due to plan amendment	—	—	—	10,000
Interest accrued (Exhibit I)	8,040	8,763	9,548	12,446
Deduct: Benefit payments	(2,500)	(2,800)	(2,900)	(3,100)
Expected closing balance	109,040	118,803	129,451	173,846

Exhibit III — Amortization of actuarial gains / losses on accrued benefit obligation

($ thousands)	20X3	20X4	20X5	20X6
Expected closing balance of accrued benefit obligation at March 31 (Exhibit II)	N/A	N/A	129,451	N/A
Actual accrued benefit obligation (per the March 31, 20X5 actuarial valuation)			150,000	
Actuarial gain (loss)			(20,549)	
EARSL			12 years	
Annual amortization over EARSL			(1,712)	

(a) A straight-line method is used to amortize actuarial gains and losses over the expected average remaining service life of the related employee groups. Amortization commences in the year following the effective date of the related actuarial valuation.

Exhibit IV — Unamortized actuarial gains and losses

($ thousands)	20X3	20X4	20X5	20X6
Unamortized actuarial gains and losses — opening balance	N/A	N/A	—	(20,549)
Actuarial gains (losses) due to:				
— accrued benefit obligation (Exhibit III)			(20,549)	—
Amortization recorded during the year:				
— accrued benefit obligation (Exhibit III)			—	1,712
— recognition of net unamortized actuarial gains as an offset to prior period service cost			—	—
			(20,549)	(18,837)

Exhibit V — Liability for retirement benefits recorded in the statement of financial position

($ thousands)	20X3	20X4	20X5	20X6
Accrued benefit obligation — closing balance (a) (Exhibit II)	109,040	118,803	150,000	173,846
Unamortized actuarial gains / losses (Exhibit IV)	—	—	(20,549)	(18,837)
Liability for retirement benefits	109,040	118,803	129,451	155,009

(a) In the period of an actuarial valuation, this is the actuarially determined amount (closing balance 20X5). In the periods between valuations, this is an expected closing balance.

Exhibit VI — Expenses recorded in the statement of operations

($ thousands)	20X3	20X4	20X5	20X6
Retirement benefit expense:				
Current period benefit cost	3,500	3,800	4,000	4,500
Prior period cost of plan amendment incurred during the year	—	—	—	10,000
Recognition of unamortized net actuarial gains	—	—	—	—

Amortization of actuarial gains / losses (Exhibit III)	x	x	x	1,712
Retirement benefit expense	3,500	3,800	4,000	16,212
Retirement benefit interest expense (Exhibit I)	8,040	8,763	9,548	12,446
Total expenses related to retirement benefits	11,540	12,563	13,548	28,658

Financial Statement Disclosure

Illustrative Note to the Financial Statements

The government sponsors a defined benefit plan for retirement benefits other than pensions for substantially all of its employees. The plan provides extended health and dental as well as life insurance to employees.

Total benefit payments to retirees during the year were $3.1 million (20X5 — $2.9 million). The plan is unfunded and requires no contribution from employees. The retirement benefit liability at March 31 includes the following components:

($ thousands)	20X6	20X5
Accrued benefit obligation	173,846	150,000
Unamortized actuarial gains / losses	(18,837)	(20,459)
Retirement benefit liability	155,009	129,451

Actuarial valuations for accounting purposes are performed triennially using the projected benefit method prorated on services. The most recent actuarial report was prepared at March 31, 20X5. The accrued benefit obligation shown for 20X6 is based on an extrapolation of that 20X5 valuation. There is a net unamortized actuarial loss to be amortized on a straight-line basis over the expected average remaining service life of the related employee groups (12 years).

The actuarial valuation was based on a number of assumptions about future events, such as inflation rates, interest rates, medical inflation rates, wage and salary increases, and employee turnover and mortality. The assumptions used reflect the government's best estimates. The expected inflation rate is 5.5 percent. The discount rate used to determine the accrued benefit obligation is eight percent.

The total expenses related to retirement benefits other than pensions include the following components:

($ thousands)	20X6	20X5
Current period benefit cost	4,500	4,000
Prior period cost of plan amendment	10,000	—

Amortization of actuarial gains / losses	1,712	—
Retirement benefit expense	16,212	4,000
Retirement benefit interest expense	12,446	9,548
Total expenses related to retirement benefits	28,658	13,548

The retirement benefit expense is included in the statement of operations as a component of program expenses. The retirement benefit interest expense is included in the public debt interest expense.

On September 30, 20X5, a plan amendment was made to the plan increasing the rate at which retirement benefits accrue. The amendment relates to both future and past service. The benefit accrual of $10 million is based on an actuarial valuation of the increase in the accrued benefit obligation due to past service.

Statement of Financial Position (excerpts)

As at March 31 ($ thousands)	20X6	20X5
Liabilities		
Accounts payable	x	x
Accrued liabilities	x	x
Borrowings		
Treasury bills	x	x
From other governments	x	x
Other	x	x
Retirement benefit liability (note)	155,009	129,451
Total liabilities	x	x
Excess of liabilities over financial assets (a)	x	x

(a) The opening balance of the excess of liabilities over financial assets in 20X3 has been restated to reflect a change in accounting policy for employee retirement benefit obligations applied retroactively. The effect of this restatement is as follows:

($ thousands)	
Excess of liabilities over financial assets — beginning of year:	
As previously reported	x
Adjustments due to change in accounting policy applied retroactively	100,000
As restated	x

Excess of expenses over revenues during the year	x
Excess of liabilities over financial assets — end of year	x
	=====

Statement of Operations (excerpts)

For the year ended March 31 ($ thousands)		20X6	20X5
Expenses			
Health	(includes retirement benefit expense)	x	x
Education ...etc.		x	x
Public debt interest (includes retirement benefit interest expense)		x	x
		x	x
		=====	=====

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FW_ PS 3250.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: PS 3250
Date: Wednesday, February 15, 2017 11:54:15
Attachment 1: image002.png
Attachment 2: PS 3250.pdf

Hi Shyrose,

Would you mind printing out the attached for Shayan and I (2 copies)?

Thank you!

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP

Office: +1 416 943 3121 | Christina.Chan@ca.ey.com

From: Shayan Jafrani
Sent: Tuesday, February 14, 2017 11:03 AM
To: Christina Chan <Christina.Chan@ca.ey.com>
Subject: FW: PS 3250

Shayan Jafrani, FSA, FCIA | Senior Manager | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 2975 | Cell Phone: +1 647 885 9630
EY/Comm: 1675237 | Shayan.Jafrani@ca.ey.com
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Specific Items — Financial Statement Items [PS 3030 — PS 3510]
PS 3250 Retirement benefits

PS 3250 Retirement benefits

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Purpose and scope

.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.

.002 In this Section, terms that appear in **bold type** are defined in the glossary of terms.

.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.

.004 If employees and/or retirees are covered by more than one **retirement benefit plan**, then a government needs to determine its obligation separately for each plan.

.005 The standards in this Section are based on the accounting framework recommended in FINANCIAL STATEMENT OBJECTIVES, Section PS 1100, and FINANCIAL STATEMENT PRESENTATION, Section PS 1201. That framework emphasizes the need to account for all liabilities incurred by a government to help legislators, taxpayers, investors and other users of **financial statements** assess: a government's future cash requirements from taxes and other revenues; its ability to meet financial obligations, both short-term and long-term; and its ability to maintain current services and finance new programs. Such assessments are essential when making financial decisions in government and when evaluating those decisions.

.006 Accounting for all of the retirement benefits incurred by governments is

particularly important because many of those governments have accumulated significant liabilities. Many governments have chosen not to set aside funds to meet retirement benefit payments when they become due. Where those liabilities have not been recorded, financial statements do not adequately provide all of the information needed by users to help them assess a government's financial position and results of operations. It is important that financial statements account for a government's liabilities for all retirement benefits to show clearly the extent to which these obligations are to be paid from cash to be raised from future tax and other revenue sources.

.007 The basis for determining obligations for retirement benefits set out in this Section is also appropriate for determining a government's contractual obligations arising from guarantees or commitments to employee retirement benefit plans of other public sector organizations that are not part of the government reporting entity. Such obligations exist, for example, when a provincial government agrees to guarantee defined retirement benefits for employees of local school boards, agrees to guarantee a minimum rate of return on retirement benefit fund assets, or agrees to provide a significant portion of the funds required by a plan sponsor. A careful reading and evaluation of such agreements is necessary to determine the substance of the obligation and whether a **liability**, **contractual obligation** or **contingency** exists that would be reported in a government's financial statements.

The objectives of funding and accounting

.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An **actuarial valuation for funding purposes** is performed to calculate the contributions required to secure the benefits promised.

.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. Accordingly, it is necessary to develop accounting estimates of liabilities for retirement benefits and expenses using an **actuarial cost method** and **actuarial assumptions** that ensure essential information required for fair presentation of financial condition and results of operations can be reported in government financial statements.

.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.

Defined benefit and defined contribution plans

.011 Two types of benefit plans are addressed in this Section — **defined benefit plans** and **defined contribution plans**. A defined benefit plan

is one that specifies either the benefits to be received by employees after retirement or the method for determining those benefits. Generally, the amount and value of the benefits to be paid depend on a number of factors and events. These include how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation and retirement age. When a government provides benefits under a defined benefit plan, it is at risk with respect to the amount of the benefit that each employee will receive (actuarial risk) and with respect to the investment returns on any assets set aside to pay for the cost of these benefits (investment risk).

.012 When a government provides benefits under a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. A defined contribution plan (or money purchase plan) is one in which a government's contributions in respect of services rendered by employees are specified. The government is required by the plan to make a specific fixed contribution each period. If that contribution is made, no additional government contributions are required now or in the future for the related service. The employees are at risk. This is generally because the amount of the benefit that will be payable to an employee is dependent upon the funds accumulated for each employee's account and the investment earnings on the accumulated funds.

.013 Because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of a particular plan makes it a defined benefit or a defined contribution plan.

.014 In some circumstances, a benefit plan may include both defined benefit and defined contribution promises. The plan, for example, may guarantee a basic defined retirement benefit and state that additional benefits, such as inflation protection, will be provided on a defined contribution basis. In such circumstances, a government would determine its obligation for the defined benefit component of the plan as a defined benefit plan and the defined contribution component of the plan as a defined contribution plan. Once the type(s) of promise is identified, the accounting and reporting principles in this Section would be followed accordingly.

Defined benefit pension plans

Liability and expense

.015 Obligations for retirement benefits result from a promise by a government to provide retirement benefits to employees because of retirement in return for their services. The obligations arise as employees render services. Therefore, as employees render services, the value of the retirement benefits attributed to those services would be recorded as a liability and expense as are other forms of current compensation.

.016 *The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date.* [SEPT. 2001]

.017 The components of the **retirement benefit liability** are:

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

(b) **plan assets**, if any; and

(c) unamortized **actuarial gains and losses**.

.018 The cost of retirement benefits promised during the period is comprised of the **retirement benefits expense**, and the **retirement benefits interest expense**.

.019 The components of the retirement benefits expense are:

(a) **current period benefit cost**;

(b) cost of plan amendments incurred during the period;

(c) net actuarial gains or losses recognized in the determination of the cost of a plan amendment in accordance with paragraphs PS 3250.068 and PS 3250.071;

(d) gains and losses arising from plan settlements and curtailments incurred during the period;

(e) amortization of actuarial gains and losses;

(f) the amount recognized as a result of a temporary deviation from the plan, determined in accordance with paragraph PS 3250.073;

(g) the change in a valuation allowance against the carrying amount of an **accrued benefit asset**, determined in accordance with paragraph PS 3250.050; less

(h) employee contributions made during the period.

.020 The retirement benefits interest expense is the net of:

(a) the interest cost on the accrued benefit obligation determined by applying the discount rate determined at the beginning of the period in accordance with paragraph PS 3250.044 to the average value of the accrued benefit obligation for the period; and

(b) the expected return on plan assets for a defined benefit plan, determined by applying the assumed rate of return on plan assets to the average market-related value of assets for the period.

.021 The retirement benefits expense and the retirement benefits interest expense would be disclosed separately in the notes to the financial statements. A separate disclosure is needed to ensure that the amount reported as the retirement benefit expense is not affected by the purely financial decision of a government to fund or not fund the plan.

Actuarial cost methods

.022 Accounting for retirement benefits on the basis of employee services reflects the fact that there is no obligation for an employee when hired and that an obligation for retirement benefits exists as the employee renders service. The accounting task is to determine how to attribute the cost of the total retirement benefits promised to each period of employee service.

.023 For defined benefit plans, there are two main groups of actuarial cost methods. They are **level cost methods** and **accrued benefit methods**. Under the level cost methods, retirement benefit expenses are computed in such a manner as to produce a total current period benefit cost that remains constant, either in absolute dollars or as a percentage

of salary, throughout an employee's service life. However, level cost methods are not recommended for accounting purposes because they do not reflect the cost of benefits earned by employees to the financial statement date.

.024 Under the accrued benefit methods, a distinct unit of retirement benefit is associated with each year of employee service rendered to the financial statement date. The actuarial present value of that unit of benefit is computed separately for the period during which it accrued. These methods are recommended because they reflect more directly the cost of retirement benefits earned by employees to the financial statement date.

.025 *An accrued benefit method should be used to attribute the cost of retirement benefits to the periods of employee service.* [SEPT. 2001]

.026 For certain **flat benefit retirement plans**, benefits vary only with periods of service rendered. For those plans, future salary and wage changes do not enter into the determination of the cost of retirement benefits earned to the financial statement date. For other defined benefit plans, such as **final pay retirement plans**, future salary and wage changes need to be incorporated into the cost of retirement benefits earned to the financial statement date because the benefit promise is based on future salary and wage levels. To estimate those levels, forecasts are needed of future inflation rates and of future salary increases. Similarly, for retirement medical plans, forecasts are needed of medical inflation rates.

.027 Accounting for the effect of future salary and wage changes ensures consistency when determining the present value of the cost of the retirement benefits earned to the financial statement date, i.e., the accrued benefit obligation. Because the discount rate used to determine that obligation includes an inflation component, for consistency the amount of the retirement benefits to be discounted must also include an inflation component. If only the discount rate used to determine the obligation includes an inflation component, then the accrued benefit obligation and expense would be understated significantly.

.028 One accrued benefit method that incorporates the effect of future salary and wage changes and attributes the value of retirement benefits to the years of employee service is the **projected benefit method prorated on services**. Under this method, generally an equal portion of the total estimated benefit, with salary projection for final pay plans and projection of medical inflation for retirement medical plans, is attributed to each year of service. The actuarial present value of the accrued retirement benefits is derived after the benefits are attributed to the years of service up to the financial statement date.

.029 *The projected benefit method prorated on services should be used to attribute the cost of retirement benefits to the periods of employee service.* [SEPT. 2001]

.030 When a retirement plan provides benefits that accrue in a non-uniform manner, the projected benefit method prorated on services may need to be adjusted to reflect the manner in which retirement benefits are earned by employees. For example, a pension plan formula may state that the pension benefit accrues at one percent of salary for the first 15 years and at two percent of salary for the final 20 years. In this circumstance, the prorating of the total estimated benefit to each accounting period would be adjusted to reflect the rates at which pension benefits are earned in that 35-year period.

.031 In some retirement plans, benefits promised in a contractual agreement or in legislation include inflation protection for current and future retirees and for former employees who have **vested** retirement benefits. For those plans, it is necessary to incorporate the impact of inflation protection in the determination of the cost of retirement benefits earned to the financial statement date.

.032 In other retirement plans, regular benefit increases for inflation protection may be provided even when such protection is not promised in a contractual agreement or in legislation. For those plans, careful analysis and professional judgment are needed to determine the substance of a government's obligation. If a regular pattern of benefit increases can be established over a reasonable period, it may be appropriate to incorporate the cost of such inflation protection in the cost of retirement benefits earned to the financial statement date and reported as an accrued benefit obligation.

Asset valuation

.033 The periodic valuation of plan assets is important because, to determine its retirement benefit liability and expense, a government needs to value the assets set aside for the purpose of meeting benefit payments.

.034 Most government plans require contributions from the employees as well as from the sponsoring government. Some governments place those contributions in a separate fund, which invests them in marketable assets. Those contributions and earnings are used to meet benefit payments to current and future retirees.

.035 When determining a government's retirement benefit liability and expense, plan assets would be valued at market-related values. Under this method, plan assets are recorded at market value or they are adjusted to market value over a period not to exceed five years. Values adjusted to market closely approximate current economic value in a manner that can minimize short-term fluctuations. Market-related values would be used because they are objective and verifiable. Once a basis of valuation is chosen it would be applied consistently.

.036 For some assets, such as real estate investments or non-marketable securities, market values are not readily available. For such assets, a method that approximates market can be used. For example, independent appraisals could be obtained, market values of similar properties could be reviewed, or future expected cash flows discounted at a market rate could be determined.

.037 *For a defined benefit plan, plan assets should be valued at market-related values.* [SEPT. 2001]

.038 In some cases governments issue non-marketable securities to their benefit funds on the condition that those securities are held in the fund to maturity. Market-related values for these assets may not be readily determinable. In such cases, non-marketable securities can be valued at cost.

Measurement date

.039 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and

as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Actuarial assumptions

.040 Accounting for retirement benefit obligations of defined benefit plans requires forecasts of future events, such as inflation rates, investment returns, interest rates, wage and salary increases, medical inflation and employee turnover and mortality. Such forecasts form the basis of actuarial assumptions.

.041 Each key actuarial assumption would be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation. The assumptions would take into account the expected long-term experience of the plan and the short-term forecast. Such an approach ensures that the reported accrued benefit obligation and expense recognize the long-term nature of retirement benefit promises as well as the experience of the plan expected in the short term. Assumptions about the long-term future, however, are not to be unduly influenced by the experience expected in the short term. At each actuarial valuation, assumptions need to be reassessed; they would be revised if expectations about the future change. All assumptions are based on the presumption that the plan will continue in effect in the absence of evidence to the contrary.

.042 *Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts.* [SEPT. 2001]

.043 One commonly used approach that meets this standard is the use of streamed rate assumptions. Under the streamed rate approach, the short-term forecast of fund asset earnings, for example, would reflect the rates of return that assets currently held in the fund will earn until their maturity. As those assets mature, assumptions about their expected earnings on reinvestment would move to the expected long-term rate. Similarly, there would be streamed rate assumptions for salary increases.

.044 The actuarial assumptions underlying the valuation of the retirement benefit liability and expense would be internally consistent. For example, when a government determines its discount rates by reference to its plan asset earnings, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the short-term forecast of rates of return on assets currently held in the fund. When a government determines its discount rates by reference to its cost of borrowing, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the specific rates of interest and the periods committed to by the government on the amounts borrowed.

.045 *Actuarial assumptions should be internally consistent.* [SEPT. 2001]

.046 Internally consistent assumptions about future inflation rates are particularly important because of the significant impact those rates have on the reported accrued benefit obligation and related expenses. The same assumptions about future inflation need to be used when forecasting future rates of return on fund assets, future costs of borrowing and future salary and wage increases, and when determining the appropriate discount rates. In addition, methods of developing actuarial assumptions need to be consistent over time.

.047 Measurement of the cost of future medical benefits requires assumptions about the level and frequency of future claims and the cost of meeting those claims. The level and frequency of claims are particularly sensitive to the age of employees (and their beneficiaries) and may be sensitive to other factors, such as gender and geographical location. A government estimates future medical costs on the basis of historical data about its own experience, supplemented when necessary by historical data from other entities, insurance enterprises, medical providers or other sources. Historical data is adjusted to reflect any differences in demographic mix of the population or when there is reliable evidence that historical trends will not continue.

.048 Certain medical claims may be covered by governmental programs under existing law or by other providers of health care benefits. Benefit coverage by governmental programs is assumed to continue as provided by the present law and by other providers pursuant to their present plans.

.049 When making assumptions about future events, a government would obtain expert assistance from internal or external sources. One source of expert assistance is the **actuary** carrying out the actuarial computations. Periodic assessments are needed to ensure that the assumptions continue to be relevant.

Limit on the carrying amount of an accrued benefit asset

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

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

.054 The adjusted benefit asset is then compared to the **expected future**

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

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

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

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

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

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

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

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

Actuarial gains and losses

.060 The periodic actuarial valuation of a government's obligation for

retirement benefits will usually determine that adjustments are required due to experience different from that assumed or to changes in actuarial assumptions. Adjustments are needed when the actual experience of the benefit plan is different than that expected. Adjustments due to changes in actuarial assumptions are needed when a government believes revised assumptions are necessary to reflect a relatively permanent change in expected experience or to reflect new information. Adjustments are inevitable because the actuarial valuation requires ongoing forecasts of uncertain future events.

.061 Actuarial gains and losses would be amortized over a reasonable future period because of their tentative nature and because further adjustments will likely be required in the future. A reasonable future period is the **expected average remaining service life of the related employee group**. Amortization may commence in the period following the determination of the adjustment. Actuarial gains and losses would be determined on a market value basis or a basis adjusted to market value, consistent with paragraph PS 3250.035.

.062 *Except in the circumstances in paragraph* PS 3250.068*,* PS 3250.071 *and* PS 3250.078*, actuarial gains and losses should be amortized to the liability or asset and the related expense in a systematic and rational manner over the expected average remaining service life of the related employee group.* [SEPT. 2001]

Prior period service costs arising from plan amendments

.063 A plan amendment occurs when a benefit plan is changed or initiated. In such circumstances, retroactive credit may be given to employees for services rendered previously and, as a result, **prior period service costs** are incurred. For example, if the benefit formula is changed from one percent to two percent of final pay per year of service, the extra one percent may be credited to employees for years of service prior to the change.

.064 Plan amendments include the inception of a new plan that grants retroactive credit for past service, an increase in benefits related to past service for active employees, or an increase in benefits for former employees already retired.

.065 The cost of plan amendments related to prior period employee services would be accounted for as an expense in the period of the plan amendment. This method is recommended because it ensures that, when a government provides retroactive credit to employees for past services, legislators, taxpayers and investors are provided a full accounting of the cost of that decision in the period the decision is made. Such an accounting ensures that the effect of that decision, as it relates to the cost of prior period services, is recognized as an expense in the period a liability is incurred. It also provides information needed to assess the extent to which future revenues are required by a government to pay for past transactions because all retirement benefit liabilities are accounted for in the financial statements.

.066 *The cost of plan amendments related to prior period employee services should be accounted for in the period of the plan amendment.* [SEPT. 2001]

.067 While all plan amendments related to prior period employee services are accounted for in the period of the plan amendment, the existence of the plan amendment may affect the recognition of actuarial gains, as

described in paragraph PS 3250.068.

.068 *In the period of a plan amendment related to prior period employee services that results in an increase in the accrued benefit obligation, if net unamortized actuarial gains exist, these should be recognized immediately, to a maximum of the prior period service cost, and offset against the prior period service cost in the statement of operations, with separate disclosure in the notes.* [SEPT. 2001]

.069 When a government makes a plan amendment related to prior period employee services and has net unamortized actuarial gains, it would recognize these net unamortized actuarial gains immediately in the statement of operations, to a maximum of the prior period service cost. Recognition would be applied first to the oldest net unamortized actuarial gains within a plan. These actuarial gains would be deducted from the prior period service cost in the statement of operations. The notes to the financial statements would disclose this information.

.070 A plan amendment may decrease, rather than increase, a government's accrued benefit obligation. A decrease in the accrued benefit obligation would be accounted for immediately in the period of the plan amendment. The existence of the plan amendment may affect the recognition of actuarial losses as described in paragraph PS 3250.071.

.071 *In the period of a plan amendment related to prior period employee services that results in a decrease in the accrued benefit obligation, if net unamortized actuarial losses exist, these should be recognized immediately, to a maximum of the decrease in the accrued benefit obligation. The net amount would be recognized in the statement of operations, with separate disclosure in the notes.* [SEPT. 2001]

.072 In the period of a plan amendment that decreases the accrued benefit obligation any net unamortized actuarial losses would be recognized immediately to a maximum of the decrease in the accrued benefit obligation. Recognition would be applied first to the oldest unamortized net actuarial losses within a plan.

Temporary deviation from the benefit plan

.073 A government may decide to deviate temporarily from the provisions of a benefit plan to increase or decrease the government's share of the benefit costs incurred in the current period or past periods. For example, a government may grant an employee contribution holiday as a temporary deviation from the normal terms of the benefit plan. A government would look to the substance of the temporary deviation to determine the most appropriate accounting.

Plan settlements and curtailments

.074 A **plan settlement** and a partial plan settlement consist of the discharge, in whole or in part, of a government's obligation existing under a retirement benefit plan. They are irrevocable events by which a government or a plan is relieved of the primary obligation to pay all or some of the benefits promised and is relieved of significant risks in relation to the obligation or the assets used to make settlement. When a full plan settlement occurs, a future actuarial valuation is not required because the government no longer has an obligation related to that plan. Because the cost of discharging the obligation may differ from the related liability recognized previously, a gain or loss may arise.

.075 A **plan curtailment** is an event that reduces significantly the expected

years of future service of present employees or eliminates, for a significant number of employees, the accrual of defined benefits for some or all of their future services. Plan curtailments include termination of a significant number of employees earlier than expected which may involve eliminating a government organization or program; they also include suspension of a plan so that a significant number of employees do not earn additional defined benefits for future services. When a plan curtailment occurs, future actuarial valuations are required because, even though the government's future obligations have been reduced, the government continues to have an obligation related to that plan.

.076 Generally, the act of settling or curtailing a retirement plan will result in a gain or loss because the actual cost of the settlement or curtailment will differ from the obligation recorded previously. Gains and losses determined upon a plan settlement or curtailment would be accounted for in the statement of operations in the period of the settlement or curtailment. This approach is recommended for plan settlements because the amount of the liability is known, it relates to services previously provided and it has been settled. Similarly, if a government settles only a part of a retirement plan obligation, the related gains and losses would be recognized immediately. This approach is also recommended for plan curtailments because the retirement benefit obligation is known with greater certainty, it relates to past employee services and the employees might no longer work for the government. For plan curtailments, the portion of the total gains and losses that would be accounted for would relate to the employees affected by the curtailment.

.077 In some circumstances, there will be unamortized actuarial gains and losses incurred prior to the plan settlement or curtailment. The net unamortized balances related to the obligation settled or to the employees affected by the curtailment would be recognized in the period of settlement or curtailment, and is included as part of the gain or loss arising on settlement or curtailment.

.078 *Gains and losses determined upon a plan settlement or curtailment should be accounted for in the period of the settlement or curtailment.* [SEPT. 2001]

Joint defined benefit plans

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

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

the definition of a joint defined benefit plan.

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]

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

Disclosure

.083 The notes and schedules integral to the financial statements would disclose the methods and judgments applied in accounting for accrued benefit obligations and expenses. Full disclosure is particularly important for retirement obligations because the measurements depend heavily upon judgments rather than objective evidence.

.084 *Financial statements should disclose:*

(a) a general description of retirement benefit plans, benefit formulae and funding policy, including a description of significant changes to retirement benefit plans during the period;

(b) the accrued benefit obligation at the end of the period, as determined by the actuarial valuation;

(c) the market value of plan assets at the beginning and the end of the period and, if different, the market-related value of plan assets at the beginning and the end of the period;

(d) the amount of retirement benefit liability or accrued benefit asset at the end of the period, indicating separately the amount of any valuation allowance determined in accordance with paragraph PS 3250.050*.*

(e) unamortized actuarial gains and losses and the periods of amortization;

(f) current period benefit cost;

(g) cost of plan amendments incurred during the period;

(h) net actuarial gains or losses recognized in the determination of the cost of plan amendments in accordance with paragraphs PS 3250.068 *and* PS 3250.071*;*

(i) other gains and losses on accrued benefit obligations arising during the period;

(j) other gains and losses on plan assets arising during the period;

(k) gains and losses arising from plan settlements and curtailments incurred during the period;

(l) amortization of actuarial gains and losses reflected in the current

year expense;

(m) the amount recognized as a result of a temporary deviation from the plan, determined in accordance with paragraph PS 3250.073*;*

(n) the change in a valuation allowance determined in accordance with paragraph PS 3250.050*;*

(o) the amount of contributions by employees during the period;

(p) the components of the retirement benefits interest expense for the period;

(q) the amount of contributions by the government during the period;

(r) the amount of benefits paid during the period;

(s) the expected return and actual return on plan assets during the period;

(t) assumptions about long-term inflation rates, expected rate of return on plan assets, assumed health care cost trends, rate of compensation increase (for pay-related plans) and discount rate; and

(u) the date of the most recent actuarial valuation performed for accounting purposes. [SEPT. 2001]

.085 Some of this disclosure information may be presented in reconciliations of the beginning and ending balances of the accrued benefit obligation and plan assets for the period, taking into account any unamortized actuarial gains or losses existing at the financial statement date.

.086 A reconciliation of the beginning and ending balances of the accrued benefit obligation would include the items disclosed in accordance with paragraph PS 3250.084(b), (i), (k) and (o)-(r). A reconciliation of the beginning and ending balance of plan assets for the period would include the items disclosed in accordance with paragraph PS 3250.084(c), (f)-(g), (j)-(k), (m), (o)-(p) and (r).

.087 *A government should provide these disclosures separately for plans that provide pension benefits and plans that provide retirement benefits other than pensions.* [SEPT. 2001]

.088 *A government that has aggregated disclosures for its defined benefit pension plans, or for its other defined benefit retirement plans, should provide the disclosures separately for the aggregate of plans with accrued benefit obligations in excess of plan assets.* [SEPT. 2001]

.089 The level of detail disclosed by governments would reflect the highly aggregated nature of financial statements. In deciding the level of detail to disclose, governments would consider the usefulness of the information to the reader in assessing the nature of, and the costs associated with, a government's retirement benefit plans. The level of disclosure would also consider the sensitivity of the information in relation to the government's financial position.

.090 The description of the significant benefit plans and benefit formulae might include the plan surplus or deficit at the end of the period, demographic information about the participants and whether the benefit obligation includes the cost of inflation protection. The description of the funding policy might include the major types of plan assets and the basis of their valuation. The extent to which the fund holds securities of the

sponsoring government would normally be disclosed.

.091 Governments are encouraged to provide additional disclosures about the significant actuarial assumptions underlying the reported amount of a government's accrued benefit obligation when the disclosures will enhance the financial statement users' understanding of that amount.

.092 A government may also choose to disclose a forecast of the cash required to pay its retirement benefit obligations in the short term, the medium term and the long term. If provided, such a forecast would include the amounts required in the next five years, and thereafter.

.093 *For joint defined benefit plans, in addition to the disclosures required in paragraphs* PS 3250.084 *government financial statements should disclose:*

(a) the significant accounting policies for joint plans;

(b) a description of the unique nature and terms of any joint plans;

(c) the government's share of the risks and benefits under the plans; and

(d) the total financial status of any joint plans. [SEPT. 2001]

.094 Users of government financial statements need an appreciation of the magnitude of the retirement benefit plans that governments jointly sponsor and the government's responsibility under the terms of any joint plans.

Defined contribution plans

.095 When a government establishes a defined contribution plan, it does not assume the actuarial and investment risks inherent in a defined benefit plan. The government typically agrees to contribute a certain amount in each period for services rendered by the employees and has no responsibility to make any further contributions. It is the employees who are at risk. This is generally because the amount of the benefit that will be payable to them is entirely dependent upon the amount of funds accumulated for each employee's account and the economic conditions prevailing at the retirement date (see paragraphs PS 3250.011-.014 for a further discussion of defined contribution plans).

Liability and expense

.096 For the most part, defined contribution plans do not present particular accounting problems. If the formula calls for government contributions on a regular predetermined basis and if those contributions have been made, then the expense recorded in the statement of operations is simply the required contribution of the accounting period. If the contributions have not been made as required, the retirement benefit expenses would include interest accrued during the period on any outstanding amounts payable to the fund. The liability for retirement benefits recorded in the statement of financial position would be the difference between the amount the government was required to contribute and the amount that was contributed to the financial statement date, including accumulated interest on any outstanding amounts payable to the fund at the financial statement date.

.097 *For defined contribution plans:*

(a) *the liability for retirement benefits should be the difference between the amount a government was required to contribute and the amount that was contributed by the financial statement date including accumulated interest on any outstanding amounts payable to the fund at the financial statement date;*

(b) *the retirement benefit liability should be accounted for in the statement of financial position;*

(c) *the expense for retirement benefits should be the amount of required contributions provided for employees' services rendered in the period. Interest accrued during the period on any outstanding amounts payable to the fund should be accounted for as a retirement benefit interest expense; and*

(d) *the retirement benefit expense and the retirement benefit interest expense should be accounted for in the statement of operations.* [SEPT. 2001]

.098 When a defined contribution plan is amended, a government may agree to make contributions in respect of past service. The cost of current and expected future years' contributions related to a past service plan amendment is recognized immediately in the period the decision is made to amend the plan.

.099 *For a defined contribution plan, the cost of current and expected future years' contributions related to a past service plan amendment should be accounted for in the period of the plan amendment.* [SEPT. 2001]

Disclosure

.100 *For defined contribution plans, financial statements should disclose:*

(a) *a general description of benefit plans, contribution formulae and funding policy;*

(b) *the expense recognized for the period; and*

(c) *a description of significant changes to benefit plans during the period.* [SEPT. 2001]

.101 The description of the significant retirement benefit plans and contribution formulae might include demographic information about the participants.

.102 The description of the funding policy might also include: the employee and government contributions during the accounting period; the major types of plan assets, the total amounts and the basis of their valuation; and the extent to which the fund holds securities of the sponsoring government.

.103 The description of significant changes to the plan or to the financing of the plan might also include which employee group(s) is affected and a description of the impact of such changes on current and future retirement benefit liabilities and related expenses.

.104 The level of detail disclosed by governments would reflect the highly aggregated nature of financial statements. In deciding the level of detail to disclose, governments would consider the usefulness of the information to the reader in assessing the nature of, and the costs associated with, a government's retirement benefit plans. The level of disclosure would also consider the sensitivity of the information in

relation to the government's financial position.

Multiemployer and multiple-employer benefit plans

Multiemployer plans

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

.106 The federal and most provincial governments sponsor defined benefit plans in which many public sector organizations participate. Many local governments participate in such multiemployer plans. When benefits are provided to employees through a multiemployer plan, the amount for which an individual government is obligated under the plan may not be quantified. Generally, a contribution rate is established for each period to ensure that the plan assets are adequate to cover the plan's future benefit payments.

.107 When a government sponsors a defined benefit multiemployer retirement benefit plan, it has the responsibility to ensure that the defined benefits promised to employees are met. In that circumstance the sponsoring government is at risk for future experience gains or losses and would account for its related obligation for the entire multiemployer plan as a defined benefit plan.

.108 *When a government sponsors a defined benefit multiemployer retirement plan, the government should follow the standards for defined benefit plans in accounting for its obligation for the plan.* [SEPT. 2001]

.109 Although a multiemployer plan may have the characteristics of a defined benefit plan, sufficient information to follow the standards for defined benefit plans is normally not available for each participating employer other than the sponsoring government. For this reason, a multiemployer plan is accounted for by each participating government following the standards for defined contribution plans.

.110 *When benefits are provided to employees through a multiemployer retirement benefit plan, each entity participating in the plan, other than the sponsoring government, should follow the standards for defined contribution plans.* [SEPT. 2001]

.111 *The government should disclose any available information about any surplus or deficit in a multiemployer plan, the basis used to determine the surplus or deficit and the implications, if any, for the government.* [SEPT. 2001]

Multiple-employer plans

.112 A **multiple-employer plan** is a defined benefit plan maintained by more than one entity that is not a multiemployer plan. In contrast to multiemployer plans, a multiple-employer plan maintains separate accounts for each entity so that contributions provide benefits only for employees of the contributing entity. In addition, multiple-employer plans are intended to allow participating entities, commonly in the same

industry, to pool their plan assets for investment purposes and to reduce the cost of plan administration. Multiple-employer plans may have features that allow participating entities to have different benefit formulae, with the entity's contributions to the plan based on the benefit formula selected by the entity.

.113 When benefits are provided to employees through a defined benefit multiple-employer plan, each government in the plan follows the standards on defined benefit plans and bases its accounting for plan assets on its proportionate interest in the assets of the multiple-employer plan.

.114 *When benefits are provided to employees through a defined benefit multiple-employer retirement plan, each entity in the plan should follow the standards for defined benefit plans.* [SEPT. 2001]

Transitional provisions

.115 When implementing this Section, governments may have an initial unrecorded liability.

.116 The initial unrecorded liability would be accounted for as a change in accounting policy applied retroactively. This method is recommended because it ensures that all liabilities incurred to the financial statement date are accounted for in the statement of financial position. Such an accounting is needed to help users of financial statements assess the impact those liabilities may have on:

(a) a government's future cash requirements from revenues and other sources;

(b) a government's ability to meet its financial obligations, both short-term and long-term; and

(c) a government's ability to maintain the level and quality of its services and to finance new programs.

.117 *This Section should be accounted for as a change in accounting policy applied retroactively.* [SEPT. 2001]

Timing of actuarial valuations

.118 Most governments do not have full actuarial valuations performed annually because of the magnitude of the information gathering and processing required. **Actuarial valuations for accounting purposes** would generally be done once every three years because of the financial importance of retirement benefit obligations. They would be done as close to the related financial statement date as is practical. In the years between valuations, an extrapolation would be used to compute the expected accrued benefit obligation and related expenses. Each year the government reviews matters such as changes to the plan, the actuarial assumptions, occurrence of settlements and curtailments, changes to the employee group and the rate of return on plan assets, and determines whether such matters necessitate any adjustments to the extrapolations. When the effect of any change is significant, a new valuation may be necessary.

.119 In the period a government implements this Section, it would need to assess whether a new actuarial valuation of its retirement benefit obligations is needed. A new valuation would be needed, for example, if the prior one is not current or is not prepared in accordance with this

Section.

Glossary

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

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

Actuarial assumptions are made as to the occurrence of a future event that will affect retirement benefit costs and obligations. They include assumptions about such matters as mortality, withdrawal, disability and retirement and about changes in compensation, interest on obligations and investment earnings.

Actuarial cost methods are used to determine the cost of providing retirement benefits and to allocate that cost to specific time periods. The two main families of actuarial valuation methods are:

Accrued benefit methods (also known as unit credit or single premium actuarial cost methods) — Under these methods a distinct unit of retirement benefit is associated with each year of credited service and the actuarial present value of that unit of benefit is separately computed for the period during which it is presumed to have accrued. Salary projection, when appropriate, is required.

Projected benefit method prorated on services — Under this accrued benefit method, generally an equal portion of the total estimated benefit (i.e., with salary projection, when appropriate) is attributed to each year of service. The actuarial present value of the accrued retirement benefits is derived after the benefits are attributed to the years of service up to the date of determination.

Level cost methods — Under these methods the retirement benefit cost assigned to any period is either the same dollar amount or the same percentage of compensation as any other period, and is a portion of the cost of the total prospective benefits of an employee group, either in absolute dollars or as a percentage of salary. (Entry age, attained age and aggregate actuarial cost methods are included in this family of methods.)

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

(a) experience different from that assumed; or

(b) changes in an actuarial assumption.

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

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

An **actuary** is a Fellow of the Canadian Institute of Actuaries.

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

A **contingency** is the result of an existing condition or situation involving uncertainty that will ultimately be resolved when one or more future events occur or fail to occur. Resolution of the uncertainty may confirm the acquisition of an asset or the reduction of a liability or the loss or impairment of an asset or the incurrence of a liability.

Contractual obligations are obligations of a government to others that will become liabilities when the terms of those contracts or agreements are met.

The **current period benefit cost** is the actuarial present value of benefits attributed to services rendered by employees in the period.

A **defined benefit plan** specifies either the benefits to be received by employees after retirement or the method for determining those benefits. The most commonly used defined benefit plans are:

Final pay plan — Bases benefits on an employee's length of service and compensation over a specified number of years (usually the years of an employee's highest earnings).

Flat benefit plan — Provides a specified benefit for each year of service rendered; the benefit earned in each period is usually fixed and determinable under the terms of the plan and the amount of benefits to be received varies only with the years of service rendered.

A **defined contribution plan** is one in which the employer's contributions are fixed, usually as a percentage of compensation, and allocated to specific individuals. The retirement benefit for each employee is the amount that can be provided at retirement based on the accumulated contributions made on that individual's behalf and investment earnings on those contributions.

The **expected average remaining service life (EARSL) of the related employee group** is the total number of years of future services expected to be rendered by that group divided by the number of employees in the group. The calculation of expected future services considers population decrements based on the actuarial assumptions but is not weighted by benefits or compensation.

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

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

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

Financial statements are summary financial statements published by a government that report on the financial position and changes in financial position of the government reporting entity. Such statements present aggregated information and serve as a means by which a government demonstrates its accountability for the financial affairs and resources entrusted to it.

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

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

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

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

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

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

Liabilities are present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits.

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

A **multiple-employer plan** is a defined benefit plan maintained by more than one entity that is not a multiemployer plan. In contrast to multiemployer plans, a multiple-employer plan maintains separate accounts for each entity so that contributions provide benefits only for employees of the contributing entity. In addition, multiple-employer plans are intended to allow participating entities, commonly in the same industry, to pool their plan assets for investment purposes and to reduce the cost of plan administration. Multiple-employer plans may have features that allow participating entities to have different benefit formulae, with the entity's contributions to the plan based on the benefit

formula selected by the entity.

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

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

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

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

A **plan curtailment** occurs when the expected years of future service to be rendered by the existing employee group are reduced significantly or when benefits will not be earned by employees for some or all future periods.

A **plan settlement** occurs when an employer legally discharges the obligation for accrued retirement benefits either by transferring assets directly to plan participants in exchange for their rights to retirement benefits or by purchasing annuity contracts in which a third party unconditionally undertakes to pay all accrued retirement benefits.

A **prior period service cost** is the increase in the accrued benefit obligation associated with past service benefit improvements.

The **retirement benefit expense** is the cost of the retirement benefits promised during the period in exchange for services rendered during the period.

The **retirement benefit interest expense** is the cost of financing an unfunded retirement benefit obligation during the period.

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

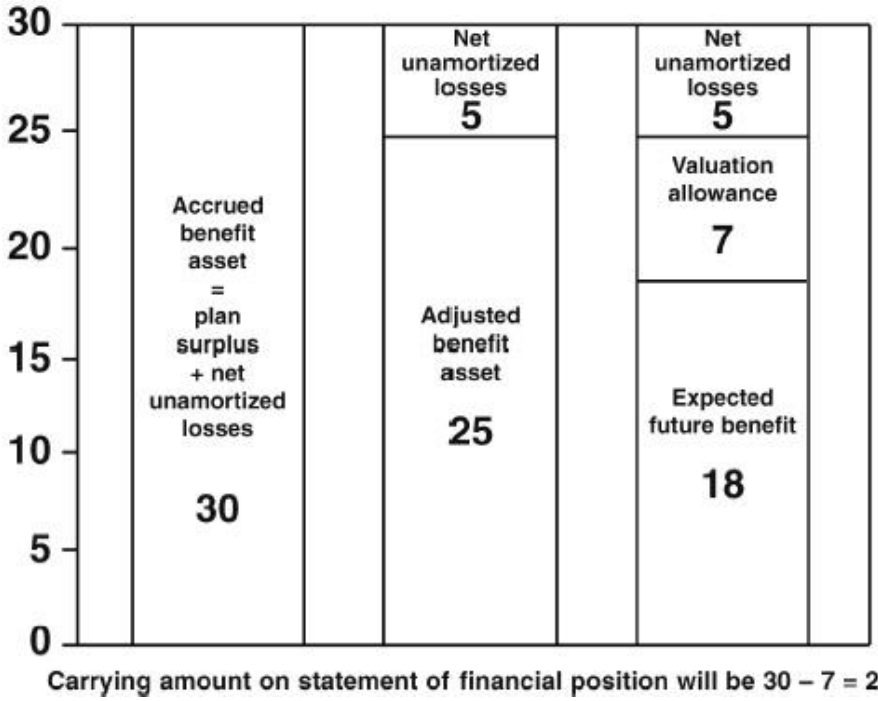
A **retirement benefit plan** is any arrangement (contractual or otherwise) by which a program is established to provide retirement income and other benefits to employees and/or retirees.

Retirement benefits are benefits expected to be provided after retirement to employees and their beneficiaries. These benefits include pension income, health care benefits, life insurance, and other miscellaneous benefits provided to employees after retirement.

Vesting is the recognition of the employees' rights to receive retirement benefits that are no longer conditional on the employees remaining in the service of the employer.

Appendix A — Limit on accrued benefit asset

Limit on accrued benefit asset



The carrying amount on the statement of financial position would be the accrued benefit asset of $30 less the valuation allowance of $7 for an amount of $23.

Appendix B — Illustrative examples

ILLUSTRATIVE EXAMPLES

The following examples have been prepared by CPA Canada staff to illustrate how the standards in Section PS 3250 might be implemented.

The examples are illustrative only and matters of principle relating to particular situations should be decided in the context of the Section. They are not intended to indicate preferred formats nor to prescribe standardized note disclosure, as variations in format and wording will be necessary to meet the requirements of differing circumstances.

For ease of presentation, selections are made from accounting alternatives permitted by the Section.

Example 1 — Defined benefit pension plan, assuming a separate pension fund is maintained

Example 2 — Defined benefit plan for retirement benefits other than pensions, assuming a separate fund is not maintained

Example 1 — Defined benefit pension plan, assuming a separate pension fund is maintained

The government sponsors contributory defined benefit pension plans for substantially all of its employees and for members of its Legislature. There are three main plans — the Public Service Plan, the Provincial Judges' Plan and the Elected Representatives' Plan. The Public Service and the Provincial Judges' plans provide for pensions equal to 1.5 percent of the average of the five highest years' salary for each year of service to a maximum of 35 years. The Elected Representatives' Plan provides for

pensions equal to four percent of the average of five years' session indemnities for each year of service to a maximum of 15 years. The plans do not provide inflation protection. The average age of the 45,000 active employees is 42. There are 5,000 former employees who are entitled to deferred pension benefits and 11,000 retirees now receiving benefits.

Each year employees contribute seven percent of their salary to a separate pension fund and the government contributes an equal amount. While the government and employees are required to contribute equal amounts into the pension fund, the government retains the full risk of the accrued benefit obligation. The pension fund invests monies from the contributions in securities of organizations external to the government reporting entity as well as investing in some non-marketable bonds of the government.

At the beginning of fiscal year 20X1, an actuarial valuation of the government's employee pension obligations was done for accounting purposes using the projected benefit method prorated on services. The liability for pensions recorded in the statement of financial position was $400 million. For purposes of this example it is assumed that there were no unamortized actuarial gains or losses at that time.

Key actuarial assumptions used in the valuation were based on the government's best estimates. Those assumptions involve forecasts of expected future inflation rates, investment returns, wage and salary increases, and employee turnover and mortality. A second actuarial valuation for accounting purposes was performed at the end of fiscal year 20X3. During the second valuation, the actuarial assumptions included in the first one were reviewed and no changes were considered necessary.

During fiscal 20X4, a plan amendment was made to the Public Service Plan increasing the benefits from 1.5 percent to two percent of the average of the five highest years' salary for each year of service to a maximum of 35 years. The plan amendment was effective March 31, 20X4 and relates to both future and past services. The government is responsible for funding the pension liability of $25 million related to past services over the next 12 years. The increase in current period benefit costs due to rendering of service for fiscal 20X5 was $1.5 million.

	April 1, 20X0	March 31, 20X3
Accrued benefit obligation	$1.5 billion	$2.2 billion
Pension fund asset	$1.1 billion	$1.8 billion
Pension liability recorded in the statement of financial position	$ .4 billion	$ .4 billion
	========	========
Expected average remaining service life of related employee groups (EARSL)		12 years
Plan amendment March 31, 20X4		$25,000

Expected current period benefit cost:		
20X1	$200 million	
20X2	$220 million	
20X3	$240 million	
20X4		$240 million
20X5		$250 million
20X5 related to plan amendment		$1.5 million
20X6		$260 million

Expected rates of return	8%
Expected salary escalations	5%
Expected inflation rates	3%

The following amounts related to other pension experience incurred throughout the period:

($ millions)	20X1	20X2	20X3	20X4
Employee funding contributions	110	115	120	126
Government funding contributions:				
— related to current service	110	115	120	126
Benefit payments to retirees	105	109	115	119

Exhibit I — Interest during the year on the average pension liability outstanding during the year

($ thousands)	20X1	20X2	20X3	20X4
Interest on expected average accrued benefit obligation:				
Accrued benefit obligation — opening balance (a)	1,500,000	1,718,800	1,971,744	2,200,000
Add: Current period benefit cost (b)	100,000	110,000	120,000	120,000
Deduct: Benefit payments (b)	(52,500)	(54,500)	(57,500)	(59,500)
Average accrued benefit obligation	1,547,500	1,774,300	2,034,244	2,260,500
Interest at 8% on average accrued benefit obligation	123,800	141,944	162,740	180,840

Expected earnings on average pension fund assets:				
Pension fund assets — opening balance (a)	1,100,000	1,417,600	1,598,048	1,800,000
Add: Employee and government funding contributions (b)	110,000	115,000	120,000	126,000
Deduct: Benefit payments (b)	(52,500)	(54,500)	(57,500)	(59,500)
Average pension fund assets	1,157,500	1,478,100	1,660,548	1,866,500
Expected earnings on average pension fund assets at 8%	92,600	118,248	132,844	149,320
Total interest during the period on the average pension liability outstanding during the period (c)	31,200	23,696	29,896	31,520

(a) In the period of an actuarial valuation, the opening balance of the accrued benefit obligation is the actuarially determined amounts (opening balances 20X1 and 20X4). In the periods between valuations (20X2 and 20X3), the opening balance is equal to the expected closing balance for the previous year as determined in Exhibit II. The opening balance of pension fund assets is the actual amount reported in the financial records of the fund.

(b) Accrued, or assumed to take place, evenly throughout the year, therefore interest is accrued on one-half of the total.

(c) Interest during the year on average pension liability outstanding during the year = 8% of [(average accrued benefit obligation) – (average pension fund assets)].

Exhibit II — Expected closing balance of accrued benefit obligation

($ thousands)	20X1	20X2	20X3	20X4
Accrued benefit obligation — opening balance	1,500,000	1,718,800	1,971,744	2,200,000
Add: Current period benefit cost	200,000	220,000	240,000	240,000
Increase due to plan amendment	—	—	—	25,000
Interest accrued (Exhibit I)	123,800	141,944	162,740	180,840
Deduct: Benefit payments	(105,000)	(109,000)	(115,000)	(119,000)
Expected closing balance	1,718,800	1,971,744	2,259,484	2,526,840

Exhibit III — Expected closing balance of pension fund

assets

($ thousands)	20X1	20X2	20X3	20X4
Pension fund assets — opening balance (actual)	1,100,000	1,417,600	1,598,048	1,800,000
Add: Employee and government funding and contributions	220,000	230,000	240,000	252,000
Expected earnings (Exhibit I)	92,600	118,248	132,844	149,320
Deduct: Benefit payments	(105,000)	(109,000)	(115,000)	(119,000)
Expected closing balance	1,307,600	1,656,848	1,855,892	2,082,320

Exhibit IV — Amortization of actuarial gains / losses on accrued benefit obligation

($ thousands)	20X1	20X2	20X3	20X4
Expected closing balance of accrued benefit obligation at March 31 (Exhibit II)	N/A	N/A	2,259,484	N/A
Actual accrued benefit obligation (per the March 31, 20X3 actuarial valuation)			2,200,000	
Actuarial gain			59,484	
EARSL			12 years	
Annual amortization over EARSL			4,957	

(a) A straight-line method is used to amortize actuarial gains and losses over the expected average remaining service life of the related employee groups. Amortization commences in the year following the effective date of the related actuarial valuation.

Exhibit V — Amortization of actuarial gains / losses on pension fund asset earnings

($ thousands)	20X1	20X2	20X3	20X4
Expected closing balance of pension fund assets at March 31 (Exhibit III)	1,307,600	1,656,848	1,855,892	2,082,320
Actual pension fund assets	1,417,600	1,598,048	1,800,000	2,142,320
Actuarial gain (loss)	110,000	(58,800)	(55,892)	60,000
EARSL	12 years	12 years	12 years	12 years
Annual amortization over EARSL	9,167	(4,900)	(4,658)	5,000

Exhibit VI — Unamortized actuarial gains and losses

($ thousands)	20X1	20X2	20X3	20X4
Unamortized actuarial gains and losses — opening balance	—	110,000	42,033	41,358
Actuarial gains (losses) due to:				
— accrued benefit obligation (Exhibit IV)	—	—	59,484	—
— earnings on pension fund assets (Exhibit V)	110,000	(58,800)	(55,892)	60,000
Amortization recorded during the year:				
— accrued benefit obligation (Exhibit IV)	—	—	—	(4,957)
— earnings on pension fund assets (Exhibit V)	—	(9,167)	(4,267)	391
— recognition of net unamortized actuarial gains as an offset to prior period service cost (a)	—	—	—	(25,000)
Unamortized actuarial gains and losses — closing balance	110,000	42,033	41,358	71,792

(a) When the cost of a plan amendment that improves a benefit related to prior service is offset against net actuarial gains, the cost is offset first against the oldest gains. Additionally, it is only offset against gains in the Public Service Plan.

Exhibit VII — Liability recorded in the statement of financial position

($ thousands)	20X1	20X2	20X3	20X4
Accrued benefit obligation — closing balance (a) (Exhibit II)	1,718,800	1,971,744	2,200,000	2,526,840
Deduct: Pension fund assets — closing balance (Exhibit III)	(1,417,600)	(1,598,048)	(1,800,000)	(2,142,320)
Unamortized actuarial gains / losses (Exhibit VI)	110,000	42,033	41,358	71,792
Pension liability	411,200	415,729	441,358	456,312

(a) In the period of an actuarial valuation, this is the actuarially determined amount (closing balance 20X3). In the periods between valuations, this is an expected closing balance.

Exhibit VIII — Expenses recorded in the statement of

operations

($ thousands)	20X1	20X2	20X3	20X4
Pension expense:				
Current period benefit cost	200,000	220,000	240,000	240,000
Prior period cost of plan amendment incurred during the year	—	—	—	25,000
Recognition of unamortized net actuarial gains	—	—	—	(25,000)
Amortization of actuarial gains / losses (Exhibit VI)	—	(9,167)	(4,267)	(4,566)
	200,000	210,833	235,733	235,434
Less: Employee contributions	(110,000)	(115,000)	(120,000)	(126,000)
Pension expense	90,000	95,833	115,733	109,434
Pension interest expense:				
Interest during year on the average pension liability outstanding during the year (Exhibit I)	31,200	23,696	29,896	31,520
Total pension-related expenses	121,200	119,529	145,629	140,954

Exhibit IX — Non-cash items recorded in the statement of cash flow

($ thousands)	20X1	20X2	20X3	20X4
Pension liability:				
— beginning of year (Exhibit VII)	400,000	411,200	415,729	441,358
— end of year (Exhibit VII)	411,200	415,729	441,358	456,312
Increase in pension liability	11,200	4,529	25,629	14,954

Financial Statement Disclosure

Illustrative Note to the Financial Statements

The government sponsors contributory defined benefit pension plans for substantially all of its employees and for members of its Legislature. There are three main plans — the Public Service Plan, the Provincial Judges' Plan and the Elected Representatives' Plan. The plans provide pensions based on length of service and final average earnings. They do

not provide for inflation protection. The average age of the 45,000 active employees covered by the plans is 42. There are 5,000 former employees who are entitled to deferred pension benefits. At present, the plans provide benefits for 11,000 retirees; benefit payments were $119 million in 20X4 and $115 million in 20X3.

Employees make contributions equal to seven percent of their salary and the government contributes an equal amount. In 20X4, total contributions for current year's service were $252 million (20X3 — $240 million). Total benefit payments to retirees during the year were $119 million (20X3 — $115 million). A separate pension fund is maintained. Pension fund assets are invested primarily in marketable investments of organizations external to the government reporting entity, with some invested in non-marketable bonds of the government. The pension liability at March 31 includes the following components:

($ thousands)	20X4	20X3
Accrued benefit obligation	2,526,840	2,200,000
Pension fund assets:		
Marketable securities	(1,942,320)	(1,610,000)
Government bonds	(200,000)	(190,000)
	384,520	400,000
Unamortized actuarial gains / losses	71,792	41,358
Pension liability	456,312	441,358

Actuarial valuations for accounting purposes are performed triennially using the projected benefit method prorated on services. The most recent actuarial report was prepared at March 31, 20X3. The accrued benefit obligation shown for 20X4 is based on an extrapolation of that 20X3 valuation. There is a net unamortized actuarial gain to be amortized on a straight-line basis over the expected average remaining service life of the related employee groups (12 years).

The actuarial valuation was based on a number of assumptions about future events, such as inflation rates, interest rates, wage and salary increases and employee turnover and mortality. The assumptions used reflect the government's best estimates. The expected inflation rate is three percent. The discount rate used to determine the accrued benefit obligation is eight percent.

Pension fund assets are valued at market values. The expected rate of return on plan assets is eight percent. The actual return on plan assets was 8.6 percent. Plan assets include government bonds valued at an estimated market value of $200 million (20X3 — $190 million).

The total expenses related to pensions include the following components:

($ thousands)	20X4	20X3
Current period benefit cost	240,000	240,000
Prior period cost of plan amendment	25,000	—

Recognition of net unamortized actuarial gains	(25,000)	—
Amortization of actuarial gains / losses	(4,566)	(4,267)
	235,434	235,733
Less: Employee contributions	(126,000)	(120,000)
Pension expense	109,434	115,733
Interest cost on the average accrued benefit obligation	180,840	162,740
Expected return on average pension plan assets	(149,320)	(132,844)
Pension interest expense	31,520	29,896
Total expenses related to pensions	140,954	145,629

The pension expense is included in the statement of operations as a component of program expenses. The pension interest expense is included in the public debt interest expense.

On March 31, 20X4, a plan amendment was made to the Public Service Plan increasing the rate at which pension benefits accrue. The amendment relates to both future and past service. The benefit accrual of $25 million is based on an actuarial valuation of the increase in the accrued benefit obligation due to past service. The government intends to fund this amount over a 12-year period ($1 million in 20X4).

Statement of Financial Position (excerpts)

As at March 31 ($ thousands)	20X4	20X3
Liabilities		
Accounts payable	x	x
Accrued liabilities	x	x
Borrowings		
Treasury bills	x	x
From other governments	x	x
Bonds payable to pension fund (note)	200,000	190,000
Other	x	x
Pension liability (note)	456,312	441,358
Total liabilities	x	x
Excess of liabilities over financial assets	x	x

Statement of Operations (excerpts)

For the year ended March 31 ($ thousands)		20X4	20X3
Expenses			
Health	(includes pension expense)	x	x
Education ...etc.		x	x
Public debt interest (includes pension interest expense)		x	x
		x	x
		=====	=====

Example 2 — Other retirement benefits plan

The government provides certain retiree health and life insurance benefits to its employees. The plan is unfunded and requires no contribution from employees.

In 20X3 the government adopted accrual accounting for the benefit plan. Prior to that date the government recognized benefit expenses equal to its payments for the actual costs incurred by the retirees and no liability for retirement benefits other than pensions was recorded in the statement of financial position.

At the beginning of fiscal year 20X3, an actuarial valuation of the government's obligations for retirement benefits other than pensions was done for accounting purposes using the projected benefit method prorated on services. Key actuarial assumptions used in the valuation were based on the government's best estimates. Those assumptions involve forecasts of expected future inflation rates, cost of long-term debt, employee mortality and medical costs. A second actuarial valuation for accounting purposes was performed at the end of fiscal year 20X5. During the second valuation, the actuarial assumptions included in the first one were reviewed and no changes were considered necessary.

($ thousands)	April 1, 20X2	March 31, 20X5
Accrued benefit obligation	100,000	150,000
Expected average remaining service life of related employee groups (EARSL)	12 years	
Plan amendment September 30, 20X5		10,000
Expected current period benefit cost:		
20X3	3,500	
20X4	3,800	

20X5	4,000	
20X6		4,000
20X6 related to plan amendment		500
20X7		5,200
20X8		5,400

Expected cost of long-term debt	8%	
Expected salary escalations	5.5%	
Expected medical inflation rates	10%	
Expected inflation rates	5.5%	

Benefit payments to retirees	20X3	2,500
	20X4	2,800
	20X5	2,900
	20X6	3,100

Exhibit I — Interest during the year on the average liability for retirement benefits other than pensions outstanding during the year

($ thousands)	20X3	20X4	20X5	20X6
Interest on expected average accrued benefit obligation:				
Accrued benefit obligation — opening balance (a)	100,000	109,040	118,803	150,000
Add: Current period benefit cost (b)	1,750	1,900	2,000	2,125
Increase in accrued benefit obligation due to plan amendment (c)	—	—	—	5,000
Deduct: Benefit payments (b)	(1,250)	(1,400)	(1,450)	(1,550)
Average accrued benefit obligation	100,500	109,540	119,353	155,575
	======	======	======	======
Interest at 8% on average accrued benefit obligation (d)	8,040	8,763	9,548	12,446

(a) In the period of an actuarial valuation, the opening balance of the accrued benefit obligation is the actuarially determined amounts (opening balances 20X3 and 20X6). In the periods between valuations (20X4 and 20X5), the opening balance is equal to the

expected closing balance for the previous year.

(b) Accrued, or assumed to take place, evenly throughout the year, therefore interest is accrued on one-half of the total.

(c) Since the plan amendment was effective mid-year, interest is earned for one-half of the year on the increase in accrued benefit obligation due to past service = ½ (10,000). Similarly, interest is earned on the increase in the current period benefit cost following the plan amendment. The average current period benefit cost in 20X6 is, therefore, = ½ (4,000) + ¼ (500).

(d) Interest during the year on average liability outstanding during the year = 8% of average accrued benefit obligation.

Exhibit II — Expected closing balance of accrued benefit obligation

($ thousands)	20X3	20X4	20X5	20X6
Accrued benefit obligation — opening balance	100,000	109,040	118,803	150,000
Add: Current period benefit cost	3,500	3,800	4,000	4,500
Increase due to plan amendment	—	—	—	10,000
Interest accrued (Exhibit I)	8,040	8,763	9,548	12,446
Deduct: Benefit payments	(2,500)	(2,800)	(2,900)	(3,100)
Expected closing balance	109,040	118,803	129,451	173,846

Exhibit III — Amortization of actuarial gains / losses on accrued benefit obligation

($ thousands)	20X3	20X4	20X5	20X6
Expected closing balance of accrued benefit obligation at March 31 (Exhibit II)	N/A	N/A	129,451	N/A
Actual accrued benefit obligation (per the March 31, 20X5 actuarial valuation)			150,000	
Actuarial gain (loss)			(20,549)	
EARSL			12 years	
Annual amortization over EARSL			(1,712)	

(a) A straight-line method is used to amortize actuarial gains and losses over the expected average remaining service life of the related employee groups. Amortization commences in the year following the effective date of the related actuarial valuation.

Exhibit IV — Unamortized actuarial gains and losses

($ thousands)	20X3	20X4	20X5	20X6
Unamortized actuarial gains and losses — opening balance	N/A	N/A	—	(20,549)
Actuarial gains (losses) due to:				
— accrued benefit obligation (Exhibit III)			(20,549)	—
Amortization recorded during the year:				
— accrued benefit obligation (Exhibit III)			—	1,712
— recognition of net unamortized actuarial gains as an offset to prior period service cost			—	—
			(20,549)	(18,837)

Exhibit V — Liability for retirement benefits recorded in the statement of financial position

($ thousands)	20X3	20X4	20X5	20X6
Accrued benefit obligation — closing balance (a) (Exhibit II)	109,040	118,803	150,000	173,846
Unamortized actuarial gains / losses (Exhibit IV)	—	—	(20,549)	(18,837)
Liability for retirement benefits	109,040	118,803	129,451	155,009

(a) In the period of an actuarial valuation, this is the actuarially determined amount (closing balance 20X5). In the periods between valuations, this is an expected closing balance.

Exhibit VI — Expenses recorded in the statement of operations

($ thousands)	20X3	20X4	20X5	20X6
Retirement benefit expense:				
Current period benefit cost	3,500	3,800	4,000	4,500
Prior period cost of plan amendment incurred during the year	—	—	—	10,000
Recognition of unamortized net actuarial gains	—	—	—	—

Amortization of actuarial gains / losses (Exhibit III)	x	x	x	1,712
Retirement benefit expense	3,500	3,800	4,000	16,212
Retirement benefit interest expense (Exhibit I)	8,040	8,763	9,548	12,446
Total expenses related to retirement benefits	11,540	12,563	13,548	28,658

Financial Statement Disclosure

Illustrative Note to the Financial Statements

The government sponsors a defined benefit plan for retirement benefits other than pensions for substantially all of its employees. The plan provides extended health and dental as well as life insurance to employees.

Total benefit payments to retirees during the year were $3.1 million (20X5 — $2.9 million). The plan is unfunded and requires no contribution from employees. The retirement benefit liability at March 31 includes the following components:

($ thousands)	20X6	20X5
Accrued benefit obligation	173,846	150,000
Unamortized actuarial gains / losses	(18,837)	(20,459)
Retirement benefit liability	155,009	129,451

Actuarial valuations for accounting purposes are performed triennially using the projected benefit method prorated on services. The most recent actuarial report was prepared at March 31, 20X5. The accrued benefit obligation shown for 20X6 is based on an extrapolation of that 20X5 valuation. There is a net unamortized actuarial loss to be amortized on a straight-line basis over the expected average remaining service life of the related employee groups (12 years).

The actuarial valuation was based on a number of assumptions about future events, such as inflation rates, interest rates, medical inflation rates, wage and salary increases, and employee turnover and mortality. The assumptions used reflect the government's best estimates. The expected inflation rate is 5.5 percent. The discount rate used to determine the accrued benefit obligation is eight percent.

The total expenses related to retirement benefits other than pensions include the following components:

($ thousands)	20X6	20X5
Current period benefit cost	4,500	4,000
Prior period cost of plan amendment	10,000	—

Amortization of actuarial gains / losses	1,712	—
Retirement benefit expense	16,212	4,000
Retirement benefit interest expense	12,446	9,548
Total expenses related to retirement benefits	28,658	13,548

The retirement benefit expense is included in the statement of operations as a component of program expenses. The retirement benefit interest expense is included in the public debt interest expense.

On September 30, 20X5, a plan amendment was made to the plan increasing the rate at which retirement benefits accrue. The amendment relates to both future and past service. The benefit accrual of $10 million is based on an actuarial valuation of the increase in the accrued benefit obligation due to past service.

Statement of Financial Position (excerpts)

As at March 31 ($ thousands)	20X6	20X5
Liabilities		
Accounts payable	x	x
Accrued liabilities	x	x
Borrowings		
Treasury bills	x	x
From other governments	x	x
Other	x	x
Retirement benefit liability (note)	155,009	129,451
Total liabilities	x	x
Excess of liabilities over financial assets (a)	x	x

(a) The opening balance of the excess of liabilities over financial assets in 20X3 has been restated to reflect a change in accounting policy for employee retirement benefit obligations applied retroactively. The effect of this restatement is as follows:

($ thousands)	
Excess of liabilities over financial assets — beginning of year:	
As previously reported	x
Adjustments due to change in accounting policy applied retroactively	100,000
As restated	x

Excess of expenses over revenues during the year	x
Excess of liabilities over financial assets — end of year	x
	=====

Statement of Operations (excerpts)

For the year ended March 31 ($ thousands)		20X6	20X5
Expenses			
Health	(includes retirement benefit expense)	x	x
Education ...etc.		x	x
Public debt interest (includes retirement benefit interest expense)		x	x
		x	x
		=====	=====

Go To Document ID: PS 3250
Last Modified Date:08 Dec 2016

FW_ Pension - PWC.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Pension - PWC
Date: Wednesday, October 05, 2016 14:06:15

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: October 5, 2016 12:59 PM
To: Virani, Shyrose (TBS)
Subject: Re: Pension - PWC

Hi Shyrose,

To date I have $16,000 in our WIPs based on time incurred to dates at the rate in our engagement letter.

It would be a good time to send an interim bill, so I will get that arranged also.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 10/04/2016 03:23 PM
Subject: Pension - PWC

Hi Lucy

We are forecasting our budget and would like to know how much monies have already been spent as of last Friday (Sep 30th) Please advise asap.

Thanks
Shyrose

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FW_ Pension Asset - additional advice.rtf

From: Donaldson, Mark (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Pension Asset - additional advice
Date: Friday, June 22, 2018 09:22:49

Just in case ....

-----Original Message-----
From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: May 14, 2018 3:56 PM
To: Donaldson, Mark (TBS) <Mark.Donaldson@ontario.ca>
Subject: Automatic reply: Pension Asset - additional advice

I am out of the office with periodic access to email and voicemail until 17 May 2018. If you need immediate assistance please contact my assistant Sarah Anderton at 416 943 3143 or sarah.anderton@ca.ey.com

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FW_ Pension Ceiling Discussion with the Auditor General .rtf

From: Virani, Shyrose (TBS) []
To: Pomykacz, Rob (MOF) [Robert.Pomykacz@ontario.ca]; Killoch, Alex (MOF) [Alex.Killoch@ontario.ca]; Paul, Joshua (EDU) [Joshua.Paul@ontario.ca]
Subject: FW: Pension Ceiling Discussion with the Auditor General
Date: Wednesday, September 21, 2016 10:18:14

-----Original Appointment-----
From: Veinot, Cindy (TBS)
Sent: September 21, 2016 10:07 AM
To: Veinot, Cindy (TBS); Petsche, Nadine (TBS); bill.pelow@auditor.on.ca; david.catarino@auditor.on.ca; benjamin.leung@auditor.on.ca; susan.klein@auditor.on.ca; rebecca.yosipovich@auditor.on.ca; bonnie.lysyk@auditor.on.ca; christine.wu@auditor.on.ca; mcolley@deloitte.ca; kdanyluk@deloitte.ca; Raymond, Martin (CA - Montreal)
Subject: Pension Ceiling Discussion with the Auditor General
When: September 21, 2016 4:15 PM-6:00 PM (UTC-05:00) Eastern Time (US & Canada).
Where: 7 Queen's Park Cres., Frost Building South 2nd Floor - ADM Boardroom or teleconference available (see details below)

In person: Please check in with security and call Mary at (416) 327-2727. Thank you.

Teleconference details:

Dial In: (416) 212-8013

Long Distance: 1-866-633-1033

Access Code: 4950903

Chair passcode: 1705 (Cindy moderator)

FW_ Pension paper.rtf

From: Virani, Shyrose (TBS) []
To: Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]
Subject: FW: Pension paper
Date: Tuesday, August 28, 2018 15:54:54
Attachment 1: 20180823150724654.pdf
Attachment 2: Draft Pension Asset Position Paper November 14 PwC clean.docx

---

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: August 24, 2018 10:09 AM
To: Virani, Shyrose (TBS) <Shyrose.Virani@ontario.ca>
Subject: Re: Pension paper

Hi Shyrose,

This was the latest version of the paper that I worked on. As it's a management paper, I don't know whether it was "finalized" or changed after this version, as this version is a still marked as draft.
It would be management's responsibility to finalize the paper and remove the Draft references, when comfortable with the content.

Hope this helps,

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Virani, Shyrose (TBS)" <Shyrose.Virani@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA

Date: 08/24/2018 08:58 AM
Subject: Pension paper

Hi Lucy:

Thank you for returning my call. Basically I am looking for the above paper in final version. Would you be able to provide it to me?

Thanks
Shyrose

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20180823150724654.pdf

Position paper for Ontario Teachers' Pension Plan

Preamble

This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP.

As described in PSAS, a pension asset arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. Contributions reflect the funding objectives of the plan. The benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (or plan surplus for accounting purposes) in OTPP is an asset to the province and it is suitable to reflect it in the financial results.

The OAG disagrees with this position. The OAG 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 Ontario Teachers' Federation (OTF) with respect to how the surplus would be utilized such that it would provide a benefit to the Province, a pension asset in the Public Accounts is not appropriate.

Ontario had followed the same pension accounting treatment for all of the past 14 years. This had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals. There has been no change to the relevant PSAS (i.e. RETIREMENT BENEFIT, Section PS 3250) over the past 14 years.

A regulation was filed to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The regulation is time-limited and legislates the accounting for pension assets of its two jointly-sponsored pension plans (OTPP and

OPSEUPP) for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The impact of the change resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to reflect the Auditor General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1.

The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the Ontario Teachers' Federation represented by its Executive (the "OTF") (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;

---

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
a. It provides defined benefits.
b. The defined benefits are contributory benefits.
c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners Agreement (FMP);
f) The Ontario Teachers' Pension Plan; and
g) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA 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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5] The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (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, in practice there has been 50/50 cost sharing of the normal contribution cost under the OTPP since the OTPP became jointly sponsored (and

Commented [CV1]: Let's discuss this next section – its new to me – was it in one of the legal opinions?

Yes, per the Osler September 20, 2016 letter – pages 7 and 8 – included in this section as we discuss that OTPP qualifies as a JSPP

Also – I'm confused by the footnotes below – 3. And 4. And then 2.3.4.?

The characteristics of a JSPP in footnote 1 includes 4 parts which were the first series of 1, 2, 3 and 4 – I have changed to a, b, c and d

Commented [CV2]: Does this have any impact on the JSPP status of the plan

I believe it is consistent with the characteristics of a JSPP- characteristic c

LD – I think there are a number of ways to interpret this clause It could be argued that the clause is there to ensure that there is sufficient money from a liquidity perspective. This does not necessarily negate the broader agreement to share on an equitable basis – i.e. it's not clear if this injection by the Province would be balanced by the OTF in some other form – one might argue that the rest of the arrangement (partner's agreement) would require it to.
The TPA does require that the assets of the pension fund should be maintained at a level that is reasonably sufficient to meet the liabilities. Therefore, if this requirement has been met then the requirements of subsection 5(3) would only be for liquidity/short term in nature and not for long term funding.

I can see how one might also argue that it indicates that residual risk is with the Province – for example, does this clause kick in when the pension plan has no more active members and runs out of assets to pay for the liabilities then is the Province on the hook. Again – the rest of the Plan's terms would indicate that this should not happen, While "should not" might not be the same as "cannot" it could be countered that the majority of the funding risk is not with the province, because the other requirements in the Partners' Agreement require shared funding.
However this would likely be a matter of interpreting the arrangement as a whole.

I don't know what the original thinking by mgt/OAG was when this was agreed upon to be a JDBP, but the above would be my guess as to how it was considered.

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).
[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).

for the majority of periods of time since the inception of the plan in 1917). [7] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Currently, the Sponsors are required to mutually agree upon how any plan deficits are to be addressed. [8] 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.

Commented [CV3]: Not sure what we are referring re: the use of also

Section 3.11 of the FMP discusses options available to the partners to eliminate any deficit in the plan (i.e. change benefits, contributions, or both)

Joint governance and cost sharing form two of the core features of the OTPP. Consistent with the equal sharing of risk permitted under a JSPP, 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.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix E. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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):

---

[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/101791209401-l5e47lc2b-23f1-44e6-b5cld22e3e50dbc3lHow+ Contribution+Rates*HaverEvolved.pdf As noted above, for the period from January l, 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%/11.20lo versus l0.4yo/l2Vo, 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.

[8] See, for example, Section 3.09 and 3.11 of the FMP.

Draft Pension Asset Position Paper November 14 PwC clean.pdf

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DRAFT

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DRAFT

Position paper for Ontario Teachers' Pension Plan

DRAFT

1.0 Preamble

This document addresses the accounting for the net pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

2.0 Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed on an appropriate application of Public Sector Accounting Standards (PSAS) to net pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP. This position paper addresses the analysis for OTPP. A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, as well as HOOPP and CAAT.

This position paper addresses the following three questions in relation to the accounting for OTPP:

1. For accounting purposes, what type of pension plan is OTPP (i.e. how should OTPP be classified under Public Sector Accounting Standards (PSAS))?
2. As a result of the classification, how should the Province of Ontario account for the pension surplus of OTPP in the Public Accounts?
3. How should the pension asset of OTPP be measured in the Public Accounts of the Province of Ontario?

3.0 Conclusions

The following conclusions were reached regarding each of the above questions:

1. Classification of OTPP - The Province has concluded that OTPP meets the definition of a joint defined benefit plan as the Province and Ontario Teachers' Federation are shared sponsors of the plan. The Teachers' Pension Act, the Partners' Agreement and the plan text for OTPP collectively set out this shared control and equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a joint defined benefit plan in RETIREMENT BENEFITS, Section PS 3250 in PSAS. The classification of OTPP as a joint defined benefit plan for accounting purposes has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

2. Recognition of a pension asset for a joint defined benefit plan - The Province has concluded that PSAS (Section PS 3250) supports the recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets be subject to unilateral control. Shared control is relevant and appropriate for a situation involving a joint defined benefit plan. The Province's share of OTPP's pension surplus meets the definition of an accrued benefit asset under Section PS 3250 which requires the Province to recognize its portion of the plan (50% for OTPP).
3. Measurement of a pension asset - The Province has concluded that the attributes of the joint defined benefit plan arrangements for the OTPP entitle the Province to access its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surpluses to reduce contributions in the future. The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of those models to date no valuation allowance appears to be required and the OTPP pension assets should be recorded on the books of the Province. The Province recognizes that professional judgement must be applied in deriving an estimate of a potential valuation allowance under Section PS 3250.

4.0 Background Information

4.1 Accrued benefit asset

As described in PSAS, an accrued benefit asset (net pension asset) arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. An Accrued Benefit Asset (AcBA) includes the effect of net unamortized experience gains or losses. Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation. OTPP currently has net unamortized experience gains. The following illustration reflects the compilation of the net pension asset (accrued benefit asset) reported on the Province's books for the OTPP.

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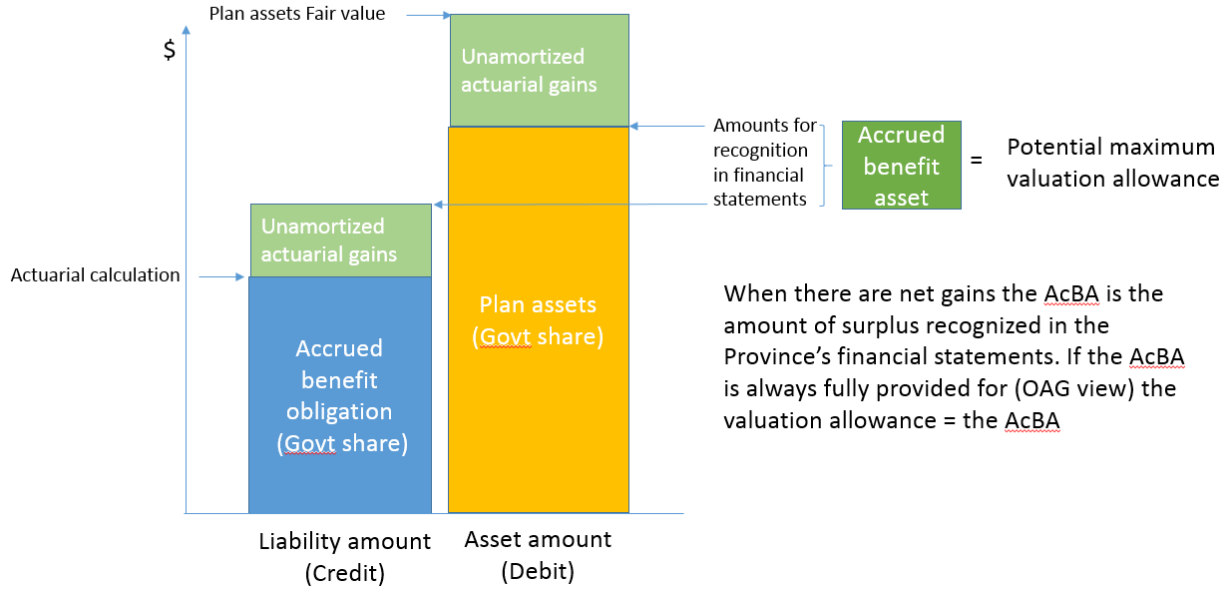
An Accrued Benefit Asset (AcBA) occurs when there is a plan surplus, including the effect of net unamortized experience gains or losses. OTPP currently has net unamortized experience gains.
Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation



It is important to note that contributions to the plan are based on funding objectives of the plan. In contrast, benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the net asset balance (plan surplus for accounting purposes) in OTPP is an asset to the Province and it is appropriate to reflect it in the financial results in accordance with PSAS. The Province has also concluded that no valuation allowance under PSAS is required against the asset as at March 31, 2016.

The OAG disagrees with the Province's position. Specifically, the OAG has indicated that the Province does not have the legally enforceable right to unilaterally access the assets of the plan, and as such that the Province does not control the assets which the OAG interprets PSAS as requiring. Further, the OAG considers the lack of an enforceable agreement at year-end with the Ontario Teachers' Federation (OTF as the joint sponsor of the plan) that would provide for lower contributions in the future as requiring that a full asset valuation allowance be taken against the net asset under PSAS.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. RETIREMENT BENEFITS, Section PS 3250 of the PSA Handbook, addresses the accounting of obligations for employee retirement benefits in government financial statements. Since 2001, there have been no consequential changes to Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years. The pension liability (asset) and expense reported by the Province of Ontario for OTPP over the period is reflected in Appendix A. Unqualified audit reports have been received for each of the years from the

OAG on the Public Accounts. The pension accounting initially adopted by the Province for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals for the prior years.

In light of the contrasting views on interpretation of PS 3250 to the Province's jointly sponsored pension plans, a regulation was necessary to allow the public service to sign-off on the impact of the OAG's view on accounting for net pension assets in Ontario's 2015-16 financial statements. The regulation is time-limited and legislates the accounting for net pension assets of its two jointly-sponsored pension plans (OTPP and OPSEUPP) for 2015-16 in a manner that is consistent with the interpretation proposed by the Auditor General. The change in accounting treatment for 2015-16 resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the 2015-16 annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's interpretation, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to reflect the Auditor General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt and would have only been appropriate if the government had agreed with the Auditor General's interpretation of PSAS which would have acknowledged errors in the prior year's comparative results.

4.2 Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1. The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the OTF (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
a. It provides defined benefits.
b. The defined benefits are contributory benefits.
c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners' Agreement (FMP); and
f) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA contains limitations on the contributions that the Province (and other participating employers) may make under 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 TPA the Province is required to make additional contributions to OTPP in the event that there are insufficient assets to make required payments out of the plan in any

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).

particular year. [5] This clause has been interpreted as a short term solvency protection clause, rather than a clause that transfers substantive residual risk to the Province, as the rest of the arrangement is structured such that the risk of these payments is minimal and the risks of the long term funding of the plan must still be equitably shared. The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (although, as noted above, solvency funding is not required under OTPP). Notwithstanding that subsection 5(1.1) of OTPP provides a cap on the Province's normal cost contribution obligation, rather than requiring 50/50 cost sharing, in practice there has been 50/50 cost sharing of the normal contribution cost under OTPP since OTPP became jointly sponsored (and for the majority of periods of time since the inception of the plan in 1917). [7] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Joint governance and cost sharing form two of the core features of OTPP. Consistent with the equal sharing of risk permitted under a JSPP, there is a requirement for decisions relating to plan design and plan amendments to be made jointly by the sponsors. In this regard, the Partner's Agreement requires the sponsors to negotiate and agree upon decisions relating to surplus or deficit utilization, which currently is outlined in the FMP. [8] The FMP indicates that deficits (or surpluses) may be addressed through increases (decreases) to the contribution rates, lowering (increasing) the amount of indexation and/or other decreases (increases) in benefits. While not binding upon the sponsors, as the sponsors can change the FMP at any time, any changes are required to have the mutual consent of both sponsors. Accordingly, the sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the sponsors are included in appendix B. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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

[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).
[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1d22e3e50dbc3/How+ Contribution+Rates+Have+Evolved.pdf As noted above, for the period from January l, 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%/11.20% 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.
[8] See, for example, Section 3.09 and 3.11 of the FMP.

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 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 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 funding surpluses that may arise under the plan.

4. Negotiations on the use of the surplus occur as specified in the Partners' Agreement. The Partner's Agreement requires that any actuarial funding valuation submitted to the pension regulators must be "actuarially balanced" (Section 57 of the Partners' Agreement). This must occur at least once every three years, but can occur every year if the partners agree. If a preliminary funding valuation shows a funding surplus or deficit then the joint sponsors must negotiate how this surplus or deficit is to be resolved prior to filing the funding valuation.

4.3 Accounting for OTPP by the Province

Since fiscal year 2001-2002, the Province has recorded a net pension asset for OTPP on the Statement of Financial Position in accordance with Section PS 3250. A net pension asset has arisen because the government's share (50%) of the total contributions to OTPP plus recognized investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense (see illustrative examples in Appendix J). The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

The various valuations prepared for the OTPP – i.e. those for the Province's public accounts, those for the funding valuation and those for the OTPP stand-alone financial statements, can create confusion when assessing the Province's accounting. Therefore, this next section sets out the differences in those valuations.

With regards to any comparisons between surplus or deficit amounts reported in the Province's financial statements verses OTPP's financial statements or funding reports, it is important to acknowledge the different objectives of funding and accounting for a pension plan which are also explicitly addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.*

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Section PS 3250 paragraph .051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: “Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…”

OTPP’s most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website (https://www.otpp.com/home). The Province’s relative portion of this surplus would be $6.6 billion. OTPP’s published stand-alone financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015, for which the Province’s portion would be a deficit of $900 million. The following background helps to clarify the reasons for these different results. OTPP’s financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook (“Part IV”), which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the net surplus or deficit for funding purposes.

Accounting for employee future benefits requires the use of assumptions and methodologies to calculate both the obligation incurred to date and the value of the assets already set aside to meet those obligations. Accounting frameworks differ in standards that must be applied in determining appropriate assumptions and methodologies. Further, the assumptions and methodologies used in developing a “funding valuation” on a going concern basis also differ from those required by accounting standards. These differences result in a number of different valuations for the same plan, depending on the purpose of the valuation and can be affected by certain choices made between acceptable options within each framework. A summary of the main differences between the methodologies used to calculate a going concern funding valuation, OTPP’s accounting valuation and the Province’s accounting valuation is shown in Appendix D.

Specifically, the discount rate used to value the obligations of the plan has a significant impact on the overall position of the plan. A lower discount rate results in a higher liability and a higher discount rate results in a lower liability, all else being equal. Put another way, a higher estimate of the time-value of money results in the value the promises made today that will be paid out in the future cheaper. OTPP uses a discount rate based on corporate/government bond rates in its financial statements, as permitted by Part IV. The Province uses a discount rate based on the expected asset return, as permitted by PSAS. The rationale for using a corporate or government bond approach is that a pension promise is akin to a bond as it is a promise to pay a series of cash flows in the future regardless of what the asset returns actually are (which could be higher or lower than expected). The rationale for using an asset return approach is that it represents the amount of contributions that, combined with investment returns, should be sufficient to pay the promised benefits, particularly as pension plans will often invest in higher risk/higher return assets then simple corporate bonds. Both a discount rate based on the expected asset return and one based on corporate/government bonds are “best estimate” rates; they must both be based on management’s best estimate of the applicable discount rate. In both cases the estimates must be supportable. The difference results not from one being more “right” or “wrong” relative to the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.

Typically the funding discount rate used for the funding valuation falls between the bond discount rate and the expected asset return, but it differs in that it does not purport to be the "best estimate" of the discount rate, rather it is designed to indicate the contributions that are required to fund the promised benefits with an additional conservative margin for adverse deviations. Note that over the long term the difference between funding valuations and accounting valuations would diminish as the impact of the discount rate unwinds and the asset valuation methods converge.

In practice, the discount rates used in the financial statements of government sponsored and joint defined benefit pension plans prepared under Part IV of the CPA Canada Handbook (Section 4600) use diverse methodologies. For example, in Alberta there are seven plans which prepare their financial statements under Part IV with reference to IFRS (same framework as OTPP). Of these none use a government bond discount rate and all use a discount rate calculated with some reference to a rate of return on invested assets, which may include factors for expenses, diversification and rebalancing. The analysis of a number of government sponsored plans is included as Appendix E. The analysis demonstrates that in their stand-alone financial statements, a significant number of government sponsored plans use a discount rate aligned to an asset investment return rather than a bond discount rate. OTPP is actually in the minority of plans that choose to use the rate required by IFRS, resulting in a lower discount rate and higher liability for financial reporting purposes.

The above analysis explains how different discount rates impact the net surplus/deficit reported on OTPP's financial statements, OTPP's funding reports and the Province's financial statements. The fact that OTPP reports a deficit on its financial statements, or that the 50% of the net surplus reported by OTPP for funding purposes is lower than the surplus reported on the government's financial statements under PSAS does not impact the net pension asset amount or pension expense reported by the Province for OTPP.

To further clarify, that there is a deficit reported in OTPP's stand-alone financial statements while the Province of Ontario calculates a surplus under PSAS requirements does not mean that there is no accounting surplus and therefore no reportable asset for the Province. In fact, **if** OTPP had chosen (as an acceptable accounting policy choice) to use a discount rate more consistent with its counterparts in other jurisdictions (see Appendix E) such as a discount rate based on an expected asset return which would be closer to that used by the Province, it would eliminate much of the existing difference between the reported net surplus/deficit amounts in OTPP's stand-alone financial statements and the Province's share of OTPP reported for accounting purposes in the Province's Public Accounts.

4.4 Applicability of PS 3250 as primary source of GAAP

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150 prescribes that, in developing and applying accounting policies, all primary sources of GAAP should be applied (Section PS 1150 paragraph .04). Primary sources of GAAP are Sections PS 1201-PS 3510, Public Sector Guidelines and appendices and illustrative material to those pronouncements. Only when there are no primary sources of generally accepted accounting principles (GAAP) that relate to the transactions or events under consideration, or more specific guidance is needed (Section PS 1150 paragraph .05), does an entity

consider other primary sources of GAAP dealing with similar issues and also the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 (issued January 2003). Section PS 1000 is not, however, a "primary source of GAAP" under the PSA Handbook.

The primary sources of GAAP specific to the accounting for pension assets is RETIREMENT BENEFITS, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, also titled Section PS 3250).

Other primary sources of GAAP that deal with similar issues might also be considered where additional interpretation or guidance may be required. For the issues dealt with in this paper - recognition and measurement of a joint defined benefit plan - this could include standards that relate to shared control, as OTPP is a joint defined benefit plan, standards that relate to the definition of an asset and standards that relate to measurement uncertainty:

- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015, effective from April 1, 2017)
- CONTINGENT ASSETS, Section 3320 (issued in June 2015, effective from April 1, 2017)
- MEASUREMENT UNCERTAINTY, Section PS 2130 (issued in April 2005)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 and CONTINGENT ASSETS, Section PS 3320 which are more recent and will be effective in for periods beginning on or after April 1, 2017. Section PS 3210 provides additional guidance on the various components of the existing asset definition found in Section PS 1000; it does not change the definition.

5.0 Question 1 – Classification of a pension asset

The analysis below addresses whether the Province's share of the pension surplus in OTPP, calculated in accordance with PSAS under Section PS 3250, represents a reportable asset to the Province of Ontario in the Public Accounts.

5.1 RETIREMENT BENEFITS PSAS 3250

The focus of the following analysis is on the accounting requirements in RETIREMENT BENEFITS, Section PS 3250 as this standard is a primary source of GAAP which specifically addresses the accounting for pension assets. The following highlights some key concepts and guidance contained in this standard.

5.1.1 Section PS 3250 – Purpose and Scope

The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250.003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

5.1.2 PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*
>
> *(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;*
>
> *(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and*

> *(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.*
>
> *The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.*

Additional guidance on identifying joint defined benefit plans (JDBPs) is in Section PS 3250 paragraphs .79 to .80 which similarly highlight the importance of both shared control and shared risks and rewards in a JDBP as follows:

> *.079 Governments may participate jointly in defined benefit plans where the government shares the risks and rewards jointly with plan participants, represented by a sponsor or sponsors. Joint defined benefit plans are governed by a formal agreement between the sponsors, which establishes that the sponsors have shared control over the plan. A governing board is generally appointed by the joint sponsors with equal representation and a mutually agreed-upon chair.*
>
> *.080 A government would consider the characteristics of the plan to determine whether it meets the definition of a joint defined benefit plan. In a joint defined benefit plan, funding contributions are shared mutually between the government and the plan members. The sponsors have control over decisions related to the administration of the plan and the level of benefits and contributions on an ongoing basis based on the terms of the contractual agreement. The sponsors share, on an equitable basis, the significant risks associated with the benefit plan. Risk would not be considered to be equitably shared in an arrangement where the government and the joint sponsors fund the plan equally but where the government retains the full risk of the accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.*

It should be noted that the definition of a JDBP under Section PS 3250 is not the same as the definition of a JSPP under the PBA, although there are some overlapping concepts between the two. A JDBP is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. The Province has concluded that OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. OTPP is a contractual arrangement between the Province and OTF in which:

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

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 10(1)3 of the TPA for example).

The TPA, the Partners' Agreement and the plan text collectively set out this shared control and that the Province of Ontario has an equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a JDBP.

The classification of OTPP as a JDBP for accounting purposes [and a JSPP under the PBA] by the Office of the Provincial Controller has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

5.2 Conclusion on classification

The Province has concluded that OTPP meets the definition of a joint defined benefit plan as the Province and Ontario Teachers' Federation are shared sponsors of the plan. The Teachers' Pension Act, the Partners' Agreement and the plan text for OTPP collectively set out this shared control and equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a joint defined benefit plan in RETIREMENT BENEFITS, Section PS 3250 in PSAS. The classification of OTPP as a joint defined benefit plan for accounting purposes has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

6.0 Question 2 – Recognition of a pension asset for a JDBP

6.1 Standards in the PSA Handbook

RETIREMENT BENEFITS, Section PS 3250 paragraphs .081 to .082 provide guidance on the accounting for a JDBP in the financial statements of the government sponsor. As OTPP meets the definition of a JDBP for the reasons noted above, the relevant guidance for the Province for purposes of reporting retirement benefits in the Public Accounts includes:

> *.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]*
>
> *.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially*

> *curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.*

Section PS 3250 paragraph .081 clearly states that "The government should account for its portion of the plan in accordance with the standards for defined benefit plans". It is clear from this that only the government's portion of the plan is included in the government's financial statements consistent with the requirements of Section PS 3250 (recognition) and the measurement of that portion is based on the requirements of Section PS 3250 (measurement). It is also then clear that the requirements of the standard for recognition and measurement, including the Limit of the Carrying Amount of an Accrued Benefit Asset guidance, are designed to be applied to a shared control situation and not only to situations where there is unilateral control. If it was intended that no pension asset could be recognized because the asset was subject to shared control and not unilateral control Section PS 3250 paragraph .081 would have made this clear. This paper discusses the question of measurement separately in Question 3.

The balance sheet recognition guidance for retirement benefits is stated in Section PS 3250 paragraphs .016 to .017:

> *.016 The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date. [SEPT. 2001]*
>
> *.017 The components of the retirement benefit liability are:*
>
> > *(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;*
> >
> > *(b) plan assets, if any; and*
> >
> > *(c) unamortized actuarial gains and losses.*

As OTPP is a funded plan there are plan assets that are recognized as part of the retirement benefit liability. When plan assets and the net impact of unamortized actuarial gains and losses exceed the accrued benefit obligation then there is an "Accrued benefit asset" (ABA). An ABA is defined in Section PS 3250 as follows:

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

Accordingly, the portion of the government's plan to be recognized includes their share of the accrued benefit obligation and also their share of the plan assets. In the case of the Province's portion of OTPP there is no uncertainty regarding the *existence* of an ABA for the government's portion of the plan; the

ABA is calculated by reference to accrued benefit obligation and plan assets, both determined based on the best estimate assumptions and the methodologies required by with Section PS 3250 for these items. As noted above an ABA is defined as the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance). For a jointly sponsored plan, this is the government's accumulated cash contributions less the government's share of the current and prior years' benefit expenses that are attributable to the government under the JDBP. The Province's portion of OTPP resulted in an ABA of $10.1 billion as at March 31, 2016. There is no uncertainty regarding the occurrence of the cash contributions made (and the interest earned thereon) measured in accordance with Section PS 3250 and the existence of the government's obligation. As Section PS 3250 paragraph .080 *requires* a government to account for its portion of the plan in accordance with the standards for defined benefit plans, this would include the recognition of any asset that meets the definition of an ABA under the standard.

Further, Section PS 3250 paragraph .050 refers to the presentation of the ABA; this amount is presented in the financial statements, net of any valuation allowance. This indicates that an ABA should be recognized in the financial statements, but measured in reference to the limit on the carrying amount of the asset - essentially a measurement requirement rather than a recognition requirement, as the limit could result in an ABA being measured at anything from $nil to its full amount. Note that the *measurement* of any net asset is subject to guidance in Section PS 3250 paragraphs .050-.059 and is discussed later in this paper.

To recognize only their share of the liability and not their share of the plan assets, or to recognize only a net liability (when the accrued benefit obligation exceeds plan assets) but never a net asset (when plan assets exceeds the accrued benefit obligation, subject to the valuation allowance guidance discussed in the Measurement section below), would indicate that the Province does not share equitably in the risks and rewards of OTPP because they bear only the risk of increased liabilities without being able to bear any rewards of investment returns on the plan assets and under this interpretation the plan would not therefore be a JDBP.

6.2 Concept of Shared Control and Asset Recognition

Included in the definition of a JDBP is the concept of shared control. Points (b) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of shared control resulting in a recognition of an asset could on the surface appear to conflict with the definition of an asset under FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210, as part of the definition of an asset under Section PS 1000 would suggest that the government must control the economic resource and access to the future economic benefits. Since shared control does not equate to control, there is a need to consider whether the recognition of any asset under PS 3250 is appropriate where there is only shared control.

The Province's position is that PSAS does not preclude asset recognition for assets under shared control and specifically for plan assets of JDBPs for the following reasons:

- As discussed above GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity. Section PS 3250 is a primary source of GAAP for dealing specifically with JDBPs and, as noted above, requires the government to account for their portion of the plan – both the accrued benefit obligation and plan assets in accordance with Section PS 3250. As such, reference to Section PS 3250 is sufficient to indicate that the recognition criteria are met for JDBP assets, no further source of PSAS guidance need be considered.

- Similarly, if other primary sources of GAAP are considered then it is relevant to consider GOVERNMENT PARTNERSHIPS, Section PS 3060 which also includes the concept of shared control. Under Section PS 3060, shared control is sufficient for asset recognition.

- The concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. With the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that the Public Sector Accounting Board (PSAB) did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

- The Province's reporting of a pension asset for the JDBP is therefore consistent with these primary sources of GAAP, subject to measurement guidance including impairment considerations.

The similarities between the definitions of a JDBP and a government partnership under PSAS are demonstrated in Appendix F to this paper, and further support Section PS 3060 as being a relevant primary source of GAAP dealing with similar circumstances, should it be considered necessary to go outside of the requirements of Section PS 3250 to look for further clarification and guidance on recognition.

Under Section PS 3060 a critical condition for a Government partnership is shared control. Section PS 3060 explicitly acknowledges that under shared control "none of the partners is in a position to exercise unilateral control over the government partnership" (Section PS 3060 paragraph .20), yet the accounting model required by Section PS 3060 for non- GBPs[9] is that of proportionate consolidation which is the recognition of a pro rata share of assets, liabilities, revenues and expenses of the partnership. JDBPs (or pension plans in general) are not specifically excluded from the scope of Section PS 3060 (Section PS

[9] Government business partnerships (GBPs) are accounted for under the modified equity method rather than proportionate consolidation.

3060 paragraph .05 lists a number of exclusions from its scope and pension plans are not noted), however some may interpret that they are excluded from the scope of Section PS 3060 on the basis that control is shared with employees rather than with a party outside of the reporting entity (Section PS 3060 paragraph .06 footnote 3). The Province of Ontario and OTF, which represents employees of the Province (Teachers), share control of OTPP. This interpretation indicates that such plans are excluded because of a closer relationship between the government and the other party than normally exists for government partnerships. Even when an independent third party shares control, Section PS 3060 still requires the recognition of a share in an asset subject to shared control, indicating that the PSAS framework does not require unilateral control in order to support asset recognition when there is shared control. It would not be appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3060 for proportionate consolidation, and similarly it is not appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3250 to account for the government's portion of a JDBP. In other words, Section PS 3250 is a primary source of GAAP and provides sufficient and complete guidance on how to account for assets related to JDBPs.

6.3 Concept of Contingent Asset

CONTINGENT ASSETS, Section PS 3320, provides guidance on the disclosure of contingent assets in a government's financial statements. It characterizes a contingent asset as one where there is uncertainty as to the existence of an asset (Section PS 3320 paragraph .04). It is the Province's position that the existence of the pension asset is not uncertain – there is an accrued benefit asset calculated in accordance with Section PS 3250 as noted above that is based on past transactions, being the impact of cumulative contributions and benefit expense. The fact that shared control exists with regards to access to the assets of the plan does not create additional uncertainty that would impact asset recognition under PSAS. The Province anticipates that in a broad sense, any OTPP surplus would be shared in an "equitable manner" under the terms of the arrangement, and this is enabled through the ability to negotiate the utilization of the surplus including the ability to prevent the utilization of the surplus in a manner that does not benefit the Province. This expectation is further supported by past history of surplus utilization (see Appendix G). The method, extent and timing during which the Province will obtain the expected future benefits (contributions reductions vs increase in benefits) is not certain. However Section PS 3320 also states "The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset. For example, even though there may be measurement uncertainty related to income tax receivable, there is nothing uncertain about the fact that this asset exists. Any uncertainty is related solely to the amount thereof" (Section PS 3320 paragraph .07). Based on past history of surplus utilization for OTPP and based on the constating documents, expected future benefits for the Government are present. The uncertainty as with many types of assets relates to measurement uncertainty which will be discussed below.

6.4 Conclusion on recognition

Therefore the Province has concluded that PSAS supports the recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets must be subject to unilateral control. The Province's share of OTPP's pension surplus meets the definition of an Accrued Benefit Asset under Section PS 3250. The measurement of that accrued benefit asset is determined by reference to the guidance in Section PS 3250 regarding the Limit on the Carrying Amount of an Accrued Benefit Asset, discussed in Question 3 of this position paper.

7.0 Question 3 – Measurement of a pension asset

7.1 Standards in the PSA Handbook

Section PS 3250 addresses how to measure a pension asset. This is a two-step process for OTPP. Firstly the accrued plan obligation (a Credit) and the plan assets (a Debit) are measured in accordance with the standard, and adjusted for any unamortized actuarial gains or losses (a Debit for gains not yet realized, a Credit for losses not yet realized). This measurement results in a retirement benefit liability when it is a net liability (a Credit) amount or an accrued benefit asset when it is a net asset (a Debit) amount. When the resulting amount is an asset, the standard requires a second step to test that the asset is not impaired. It should be noted that impairment testing in some form is required for all assets recognized under PSAS standards except those carried at fair value, although the methodology of impairment tests will vary depending on the nature of the asset. The amount that is tested is the "adjusted benefit asset". When there are net unamortized gains the ABA is equal to the adjusted benefit asset. When there are net unamortized losses the ABA is reduced by those net unamortized losses to calculate the adjusted benefit asset. A graphical illustration of the calculation of the Accrued Benefit Asset (AcBA) and the Adjusted Benefit Asset (AdBA) are shown in appendix C. Section PS 3250 paragraphs .052 to .059 go on to explain what the standard means by expected future benefit and how a government may benefit from the ABA or adjusted benefit asset. Note that for OTPP the accrued benefit asset equals the adjusted benefit asset as there are net unamortized actuarial gains.

Section PS 3250 paragraphs .050-.059 are included here for completeness and ease of reference:

> ***Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)***
>
> *.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]*

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

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

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

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

.055 The objective of the standard in Section PS 3250 paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

calculate this present value is the expected rate of return on plan assets used to determine the benefit expense in the period.

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

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

Section 3250 paragraph .052 states that a government may benefit from an ABA by either i) withdrawing surplus assets from the plan or ii) by taking a contribution holiday or receiving a refund of contributions. This is an explanatory paragraph on how a government may benefit from an ABA and why a valuation allowance may be needed, rather than detailing the test to be applied. Part of this justification is to note that that an ABA may be impaired when "the government is not entitled to benefit from [the ABA] fully". Examples of when a government may not be entitled to benefit from the ABA fully are given, such as a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

Section PS 3250 paragraph .059 gives additional guidance to apply when an entity contemplates realizing future benefits <u>through a surplus withdrawal</u>: "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal". This introduces the concept of a legally enforceable right but only in the context of a government's withdrawal of surplus and <u>not in the context of contribution holidays</u>. If the standard setters had intended legal enforceability

to be the test throughout the standard, they would not have raised it only in the context of a withdrawal of surplus, but as a more fundamental notion in the guidance on expected future benefit. [10]

It is acknowledged that the Province does not have a unilateral legal right to reduce its contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to shared control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Section 3250 paragraph .052 does not state that being "entitled to benefit" means having a legally enforceable right as at the reporting date to take contribution holidays. When considering the ability to realize expected future benefits under Section PS 3250 paragraph .052, the Province's legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability which is not explicitly required by the standard to support recognition and measurement of JDBP pension assets. Specifically, the amount of pension asset that gets recorded needs to take into account considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a pension asset in the Public Accounts. Pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". Expected does not equate to certainty or the absence of uncertainty (Section PS 3250 paragraph .056).

Under the Plan and Partners' Agreement, if funding surpluses occur the partners are required to negotiate the use of the funding surplus (at least once every three years) and the Province is entitled to negotiate a reduction in contributions in respect of its share of the surplus. Under the Partners' Agreement any funding surplus must be dealt with (which includes the option of parking the surplus in the contingency reserve) so that the funding valuation becomes actuarially balanced. *In other words when there is a funding surplus over a certain range the "status quo" cannot be maintained, the surplus must be reduced by a combination of reductions in contributions, increases in benefits or withdrawals of surplus*. This is confirmed by the Partners' Agreement Section 57 that requires an actuarially balanced valuation to be prepared at least once every three years, allowing for a contingency reserve, combined with the FMP which sets out the framework for determining when a surplus or deficit outside of agreed upon ranges are met and action must be taken. While the Province might choose to accept an increase in member benefits rather than to reduce funding, any such decision is at the Province's discretion since the OTF cannot force the Province to increase benefits instead of reducing contributions. In other words

[10] Per page 10 of the October 2, 2016 dated letter from Deloitte LLP addressed to Ms. Karen Hughes, Associate Deputy Minister, Treasury Board Secretariat

it is at the Province's discretion whether to address the actuarial balancing requirements by allowing its portion of the surplus to be utilized through increased benefits. The OTF equally has the right to not agree to reduced contributions from the Province, but they do not have the right to force an inequitable sharing of the surplus. Therefore, the Province is entitled to negotiate their share of the JDBP which may include taking contribution holidays in future negotiations and can effectively use their power in negotiations to benefit from the ABA. The joint partners do have the ability to renegotiate all aspects of the partners' agreement including the FMP. However all changes require the agreement of both parties and as such the Province can veto any changes to the agreement. Note that while the negotiations are based on funding surplus amounts rather than accounting surplus amounts, any differences would be captured in the mechanics of the calculation of the expected future benefit rather than precluding an ability to benefit from any of the accounting surplus.

Further, Section PS 3250 paragraph .055 indicates "The objective of the standard in Section PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Many generally accepted accounting frameworks use "expected" in a number of principles and it is typically used in the probabilistic sense – something is expected when it is probable at some level, it does not equate to certainty. The Province has an expectation that they will benefit fully from the ABA by exercising their current rights under the plan arrangements to negotiate the use of current and future surpluses in the form of contribution holidays. This position is supported by the review of the constating documents and past history of negotiations that indicate[11]:

1. The TPA prohibits the total amount of the contributions payable by the Province (and other participating employers) from exceeding the amount of contributions paid by or on behalf of active members in respect of credited service for the year[12] (subject to certain exceptions for payment of a solvency deficiency and where there are insufficient cash and liquid assets in the fund). 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.
2. 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 (refer to Appendix G for a history of surplus utilization for OTPP). 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.

[11] Per pages 3 to 6 of the September 20, 2016 dated letter from Osler, Hoskin & Harcourt LLP addressed to Len Hatzis and Paul Kaufman, Treasury Board Secretariat Legal Services
[12] TPA, subsection 5(1.1)

3. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right[13])[14], and the requirement to negotiate and agree (or in the absence of agreement, mediate and/or arbitrate) presents the Sponsors with an equal opportunity to benefit from surplus utilization.
4. One could argue that the obligation to bargain in "good faith" found in the Partners' Agreement (section 74) 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. Under the plan, contributions are generally borne equally by the Province and the employees. Employees benefit economically from both an increase in benefits and from a reduction of contributions. The Province benefits economically directly from a reduction in contributions. This makes it reasonable that at least some contribution reductions would be agreed to by the joint sponsors as a highly unequal weighting towards increases in benefits would not balance the interests of taxpayers and teachers therefore may be unlikely to be a reasonable outcome of “good faith” negotiations between the Province and the OTF.

   This is further supported by the historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses, and therefore, which should also be considered. In respect of conditional indexing, reduced indexation for current retirees was matched by an increase in payments by the Province for the first 50% of the indexation reduction. As the sponsors agreed to utilize the funding surplus to partially restore indexation, this restoration of indexation resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.98B for the 2015 change, and $1.68B for the 2014 change). This demonstrates that historically and over the long term an equitable sharing of the deficits and surpluses has resulted in changes in the Province’s contributions, even when there are decreases or increases to benefits for employees.

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, a mediator may be chosen by agreement of the sponsors (section 77 of the Partners’ Agreement). If the sponsors do not accept the report of the mediator, an arbitration board will be appointed (section 84 of the Partners’ Agreement). The arbitration board would consist 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

[13] The OTF Call Right is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising the government initiated Freeze period. Part of a previously agreed upon arrangement to ensure equitable sharing of the risks and rewards over the long term of the plan, it is not a general unilateral right to utilize future surpluses beyond the recovery of the specific funding shortfalls.
[14] FMP, section 6.03

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).

Based on the above analysis, the Province believes that the uncertainties around how and when to utilize a surplus in the OTPP do not result in an inability or lack of entitlement to utilize the surplus in accordance with Section PS 3250 paragraph .052.

7.2 Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250 paragraphs .053 to .058 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where actual realization of the benefit would be reflected in a reduction in future contributions. A valuation allowance is recorded against the pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province calculated the expected future benefit as the sum of:

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

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

Each of these is discussed separately.

7.3 Considerations re: withdrawal of the surplus (Section PS 3250 paragraph .056 (b))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph .059 indicates “The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal.”

The TPA for OTPP does not specify a method for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution. The Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

The Province's position is that there is no amount of expected future benefit included in respect of withdrawable plan surplus.

7.4 Considerations re: reduced future contributions (Section PS 3250 paragraph .056 (a))

Section PS 3250 paragraph .056(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per Section PS 3250 paragraph.081 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

Section PS 3250 paragraph .055 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the pension asset value to be recorded in the accounts. For example, if the pension asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the pension asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. It is therefore relatively straightforward and is typically calculated based on the Province's share of the current service cost reported in the actuarial valuation taken into perpetuity unless there is evidence to indicate the workforce will significant diminish over time (for example a closed plan).

The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for

judgment in the above calculation is in this second part of the calculation. Note that consistent with the calculation of the expected future accruals for service, no amounts are considered for employee contributions as these relate to the OTF's portion of the plan. The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (Section PS 3250 paragraph .056(a)). There is no further guidance in Section PS 3250 as to how the calculation of minimum required contributions should be performed and what restrictions or parameters should be factored into this calculation. Typically for defined benefit plans minimum contributions include those that are required by the pension regulator to be made for funding. However, minimum contributions regardless of any surplus, may be required by plan text, legislation or other agreements with employees. For OTPP a key element of judgment is determining what contributions are required by the current plan arrangements "regardless of any surplus". The constating agreements for OTPP require that the parties negotiate every 3 years as a minimum, and when there is a funding surplus.

Determining the number of years of contributions to include should involve an assessment of the facts and circumstances of the plan and should consider uncertainty. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the contractual agreements between the sponsors that provide for the sharing of risks and benefits and specifically in respect of assessing the minimum contributions required by the plan agreements (there is no minimum contributions stipulated in the Plan text, legislation or Partners' Agreement) including the following:

- One view of minimum contributions might be that the agreed upon level of contributions are the minimum contributions until they are altered in the plan text. As this can only happen with agreement from OTF it cannot be assumed that changes will be made and therefore that the contribution formula as stated in the current agreements will continue in perpetuity. This view provides the most conservative view of minimum payments. However as the current contribution amounts are greater than the government's share of the annual current service cost for the existing workforce this indicates that continued contributions at this rate will result in ever increasing surpluses. Extrapolating the surpluses, at a certain point other requirements that are currently incorporated into the plan text, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan will apply to reduce the contributions. The effect of these caps on contributions would have to be estimated but cannot be ignored as they form part of the current contribution arrangements. Modelling could be performed to develop expectations as to when these CRA limits could be expected to be reached assuming no changes in the contribution levels. As is the most conservative view (highest minimum contributions) the impact of this has been considered, as discussed below.
- An alternative view of the minimum contributions required by the plan is that there is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'. On this basis it could be

argued that any agreed upon contribution levels are mandatory for only a three year period, after which the contributions must be renegotiated to stay the same, increase or decrease, such that the stated contribution level in the plan text constitute minimum payments for only three years. It should be noted that the plan text requires an actuarially balanced funding valuation, so to the extent that a funding deficit currently existed a contribution holiday (contributions lower than the annual cost of the plan) could not be negotiated. However because the funding situation at the time of future negotiations is not known it could be argued that no amount is a fixed "minimum contribution" in this context, because all of the contribution amount is subject to future changes in funding and negotiation by the joint sponsors.

- Other views of what the minimum contributions are would fall between these two views, such as that the current funding level is set to ensure that there is no funding deficit over a 11 year period and after that changes in contributions would be negotiated. This view has been used in calculating the actuarial calculation of the asset ceiling as noted in the table below.
- Another consideration might be the specific framework within the Funding Management Plan for OTPP which contemplates specified funding zones and expectations regarding possible contribution reductions by the sponsors. Informed stochastic modelling would be necessary to estimate when the different funding zones will be reached and probability of contribution reductions may be increased.
- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to use some of the funding surplus to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change, $1.98B for the 2015 change, and $1.68B for the 2014 change).

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (Section PS 2130 paragraph .03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in Section PS 2130 paragraph .13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

As part of the 2015/16 Public Accounts audit, the Office of the Provincial Controller engaged external consultants to conduct asset ceiling tests to assess the requirement for a valuation allowance against the $10.1 billion of net pension assets reported by the Province for OTPP . The results of those reports are summarized in Table 1 below.

Table 1: Summary of Asset Ceiling Models performed for OTPP

Model Assumptions	Expected Future Benefit or Asset Ceiling ($ Billions)	Results
1. There is no minimum employer contribution under the plan/legislation that is required if a surplus is present.	$44.6	There is no reduction in the expected future benefit (EFB) as at March 31, 2016.
2. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of the current funding report. Contribution requirements are $1.7B per year for 2015, 2016 and 2017.	$41.2	The minimum contribution requirement applies to the current period of the funding report and until a new report is completed. EFB is reduced for 2 years by $1.7B at March 31, 2016.
3. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of contribution requirement (i.e. 11 years through 2026) not just for the period of the current funding report.	$29.3	Uses a period to 2026 (11 year period) based on the funding report special contribution requirement. The EFB at March 31, 2016 is reduced by $15.3B.
4. The surplus is never used until the time it reaches the Income Tax Act (ITA) threshold. Once attained, the excess surplus is used at 50% for employees and 50% for the Province to reduce contributions in the following years.	$23.2	The ITA surplus limit is reached at the end of 2025, leading to forced contribution reductions from 2026. EFB is reduced by $21.4B at March 31, 2016
5. Every year, 50% of current	$12.9	The ITA surplus limit is reached at

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year surplus is applied to improve member benefits and the remaining 50% of the current year surplus is retained and continues to accrue. Once the ITA threshold is attained, the excess surplus is used 50%-50% to reduce contributions by employees and the Province.		the end of 2041 leading to forced contribution reductions from 2042. EFB is reduced by minimum $31.7B at March 31, 2016.

Note: Models above made no assumption on any value of the surplus withdrawal.

In all 5 models above, the expected future benefit (EFB) for OTPP is greater than the accrued pension asset of OTPP of $10.1 billion, at March 31, 2016. Even under the most conservative model (number 5 above) under which 50% of the current year surplus is applied to improve member benefits while the remaining 50% is retained and continues to accrue a return on assets until the Income Tax Act (IITA) surplus threshold is reached, the EFB of $12.9 billion is greater than the accrued pension asset of $10.1 billion. As such no valuation allowance was required and reported for OTPP as of March 31, 2016.

For purposes of OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

In addition to the above calculations, the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan should also be considered. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that no valuation allowance is required.

The determination of the minimum contribution levels required as input to the calculation of the expected future benefit involves significant judgements, estimation and assumptions about future funding surplus levels. These judgements, estimates and assumptions should be made on a consistent basis with best estimates used in developing the accrued benefit obligations and plan asset amounts. Regardless of the need to apply judgements, estimates and assumptions for the calculation, this does not imply that no asset can be recognized or that it cannot be reliably measured. In fact, pension plans,

by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". From the Province's perspective, 'expected' does not equate to 'certainty' or the absence of uncertainty.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (Section PS 3250 paragraph .042) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (Section PS 3250 paragraph .041). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. Section PS 3250 paragraph .057 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on plan assets, which is one of the acceptable references suggested on Section PS 3250 paragraph .044.

The OAG and the Province differ in their interpretation regarding whether it needs to be "expected" that the Province will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in Section PS3250 paragraph .059. The Province considers that it needs to be expected that future economic benefits are to be obtained reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to benefit from a plan surplus.

7.5 Other guidance in the PSA Handbook on measurement

MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe would be a useful addition to the financial statements. Section PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would*

be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.

.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.

The estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the net pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is an acceptable alternative under PSAB and consistent with rates followed by other senior Canadian governments. Actual historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets reported in the Public Accounts. Appendix J includes a comparison of the OTPP funding rate assumptions, the Provincial discount rate for OTPP and the actual performance of OTPP from 2005 to 2016. Historical rates of return on plan assets have supported the past discount rates used by the Province in relation to OTPP.

7.6 Impact of valuation allowance

The current Auditor General's view challenges previous interpretations of the Provincial Controller and former Auditor Generals regarding the interpretation and application of Section PS 3250 to those JDBPs where the government is a joint sponsor. The impact of the OAG's view is that no net pension asset should be recognized in the Province's Public Accounts for JDBPs until the joint sponsors agree to a change in the plan text to provide for unilateral authority to the Province to access surplus or reduce future contributions or the sponsors enter into an agreement by year-end enabling the government to take a contribution holiday. In the absence of meeting either the criteria set out by the Auditor General, any ABA would therefore be fully provided for through a valuation allowance, impacting each year's

statement of operations by the amount by which the asset would otherwise increase in value. These results are counterintuitive with pension expense being higher in years in which increased funding is made and also higher when poor investment returns create actuarial losses that have not yet been amortized into the statement of operations. These examples are illustrated in Appendix C.

For information purposes, refer to Appendix H for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting for OTPP compared with following the Province's interpretation of the PSAS. Of particular note is the impact in 2008 when the deficit would have been lower by $3 billion in a year when pension asset values fell significantly because of the financial crisis.

7.7 Comparability of Ontario's accounting to other Provinces defined benefit plans

Not all of the jurisdictions noted in this comparative overview have joint defined benefit plans. Furthermore, the specific terms and conditions of any jurisdiction's plans will determine the appropriate accounting under PSAS. This information is provided for reference purposes only and has no direct impact on the Province's accounting treatment for OTPP or other defined benefit plans on the Province's financial reports.

The Province of British Columbia does have a jointly sponsored pension plan. Appendix I provides details from a legal opinion prepared by lawyers, Koskie Minsky which compared access to the pension surplus of OTPP relative to JDBPs in British Columbia. The Province of British Columbia does not report a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

The Province of Manitoba has a multi-employer defined benefit plan for their healthcare employees. The Province neither records the net pension liability or the net pension asset on their financial statements as the Province is not a direct sponsor of the plan. The Province of Manitoba appropriately reduces the accrued benefit asset to nil in accordance with Section PS 3250 paragraph .050 as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

The Province of Nova Scotia's Public Service Superannuation Plan transitioned to a joint governance structure in April 1, 2013. Due to the wording of the legislation, the Province has determined it no longer has any residual liability for the plan, and therefore has no entitlements to its assets. The legislation and funding policy alleviated the Province from any responsibility to fund shortfalls or to benefit from fund surpluses. As a result, the Province no longer records a net pension asset or liability in their financial statements. The Province of Nova Scotia therefore appropriately reduces the accrued

benefit asset to nil in accordance with Section PS 3250 paragraph .050 as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

Quebec has two joint sponsored plans: Government and Public Employees Retirement Plan, and Pension Plan Management Plan. These plans are structured such that employee and employer contributions are in separate funds. Currently both of these plans are in net pension liability positions.

In New Brunswick, the target benefit pension plans are governed by an Agreement and Declaration of Trust which restricts the Province's access to the plan assets. On this basis, the Province records the value of the plan net assets as nil when these plans are in a net asset position. These plans are shared risk plans that are governed by a Board of Trustees to which the Province has appointed one-half of the members. The Plans are jointly funded by employees and the Province. These target benefit plans target retirement benefits as opposed to guaranteeing them. Two of the four target benefit plans are in a net asset position, where a full allowance is taken by the Province against the net pension asset. The Province of New Brunswick appropriately reduces the accrued benefit asset to nil in accordance with Section PS 3250 paragraph .050 (there is no specific guidance on target benefit plans in PSAS) as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

As noted above, the constating documents for pension plans in other provinces are different than those of OTPP, therefore caution should be exercised when trying to compare accounting among the jurisdictions, or others.

7.8 Conclusion on measurement

As discussed, there is significant professional judgement and estimation in determining how to measure the valuation allowance under Section PS 3250, including the determination of the minimum contributions required by the current plan arrangements. It is the Province's position that the attributes of the JDBP arrangements for the OTPP entitle the Province to access its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surplus through reduced contributions.

The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of various actuarial assessments for the asset ceiling test date, no valuation allowance appears to be required and the OTPP pension assets should continue to be recorded on the books of the Province.

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Appendix A – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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' Pension Act and to the Partners' Agreement and Funding Management Policy in order to determine how ongoing surplus is dealt with under the OTPP.
Teachers' Pension Act (TPA)
Paragraph 10(1)3 of the TPA 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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners (sponsors) can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners (sponsors) in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the PBA, appointing the OTTP Board, and defining the role of the Board. Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the sponsors to the OTPP have the authority to utilize ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years to comply with the PBA.

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Paragraph 57 requires a valuation prepared for filing with the Superintendent of Financial Services to be actuarially balanced so that the present value of benefits and costs to be paid out of the fund (plus any contingency reserve) be equal to the present value of sponsor contributions. An actuarial valuation for funding purposes of the pension fund shall be prepared by the Board's actuary as at the 1st day of January and filed annually with the Superintendent of Financial Services, unless the partners jointly agree to instruct the Board not to file the valuation. The partners shall establish a committee to deal with accounting matters relating to joint pension plan sponsorship and agree to contact the Public Sector Accounting Board to raise issues of concern to the partners.

Paragraphs 58 to 60 indicate the actions to be taken based on the preliminary results of a valuation prepared for filing with the Financial Services Commission of Ontario. If the valuation indicates a need to increase the contribution rate, the partners need to meet as soon as possible to discuss how to adjust for that need on an equally shared basis. If the valuation indicates the contribution rate can be decreased, the actuarial gain can be applied to reduce the payments required to liquidate any unamortized balance of a solvency deficiency.

The process governing the use of ongoing surpluses by the sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

If the sponsors cannot agree on the changes required to the Plan, a mediator is appointed to assist the sponsors in coming up with an agreement. The mediator is responsible for submitting a report to the sponsors on his or her views on the positions of the partners and provide a recommendation to the sponsors. If the sponsors do not accept the mediator's report, the arbitration process will begin and an arbitration board will be appointed. The board will consist of 3 people, with each partner selecting one

representative and two appointees will select the final member who is an umpire. Paragraph 94 of the Partners' Agreement indicates that the report created by the arbitration board will be implemented.

Paragraph 92 sets some parameters for the arbitration, including part (c), which sets out that the parameters that the award of the arbitration will provide that the contributions from the Minister and employers be equal to those of the members.

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.

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

Funding Management Policy (FMP)

The FMP is an appendix to the Partners' Agreement that speaks to how the Plan should be funded and how surpluses should be utilized by both parties. The protocol for the use of a surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP. The FMP sets out a complex series of considerations surrounding funding management and the use of any excess of assets over liabilities. The FMP sets out a number of "funding zones", depending on the level of funding in the Plan. The following three are most relevant to addressing surpluses:

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the sponsors are unable to agree the mediation process set out in the

Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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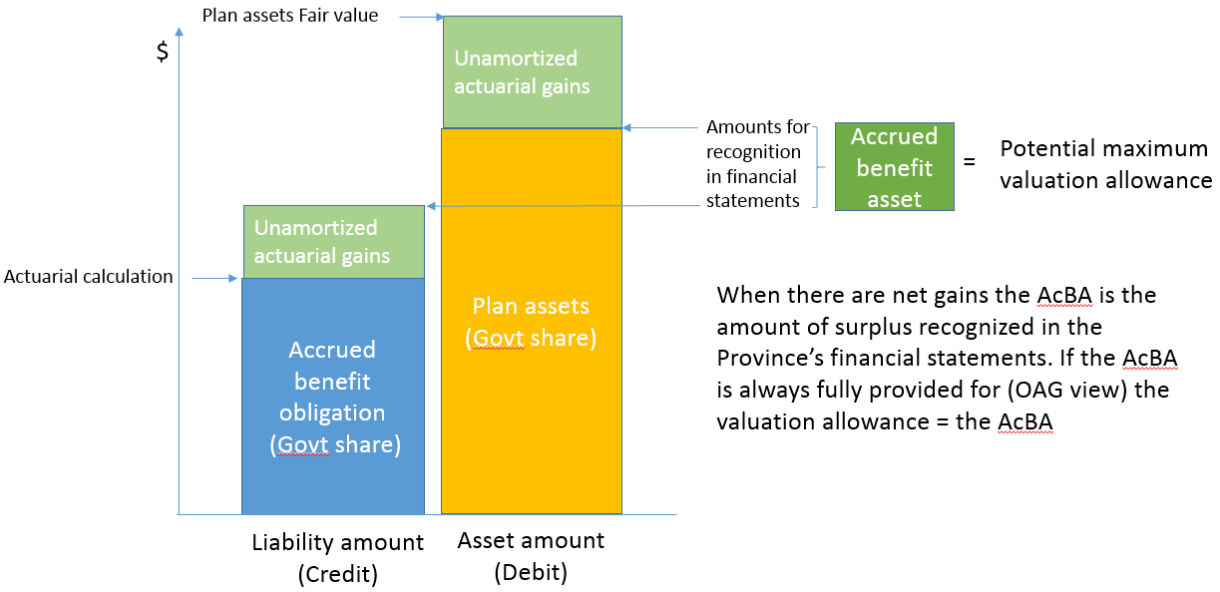
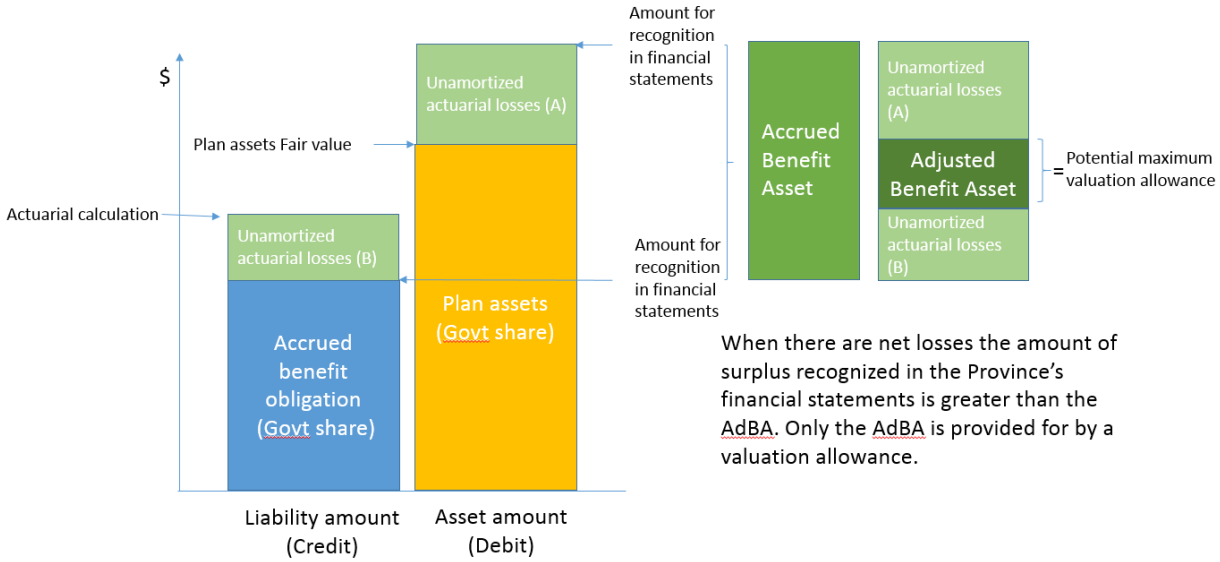
Appendix C – Overview of a Valuation Allowance on Pension Assets

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



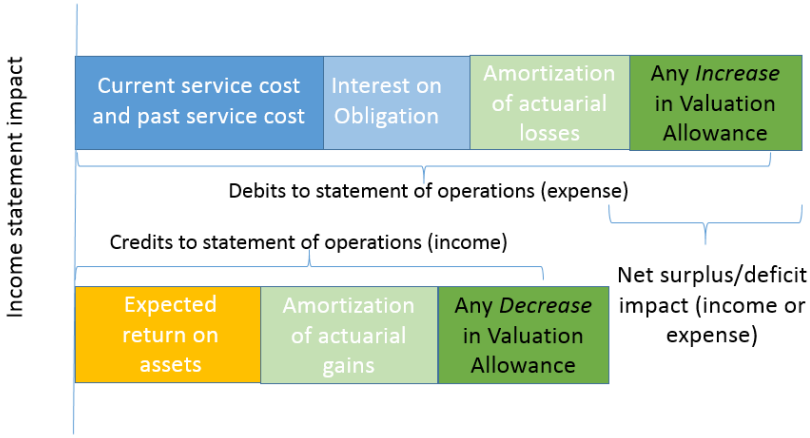
An Adjusted Benefit Asset (AdBA) is required when there are unamortized losses



Components of Expense

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

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



Changes in the Accrued Benefit Asset

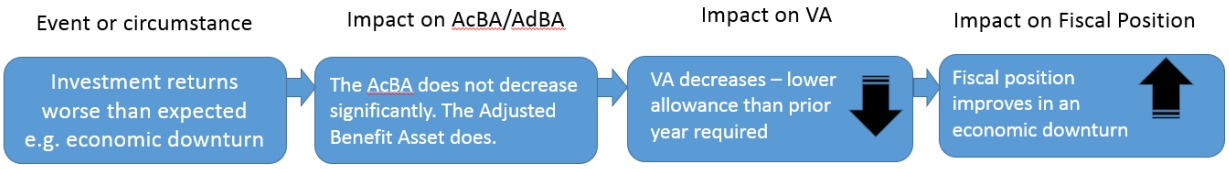
Changes in the AcBA may occur for a number of reasons. Where changes result in an increase in the AcBA without expectation of future benefit, such changes would result in a change in the valuation allowance (VA) to effectively reduce the AcBA to zero. In this situation, the following impacts on the statement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

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

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

Changes in the Accrued Benefit Asset

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



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

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

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

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

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

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

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Appendix D – Summary of different valuation methodologies for pension valuations

The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV of the CPA Canada Handbook – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits and to provide information on the financial position of the plan as of the valuation date on a funding basis in accordance with the Pension Benefits Act, the Income Tax Act as well as generally accepted actuarial practice.	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits, pension obligations and the financial position of the plan as of the valuation date in accordance with Part IV of the CPA Canada Handbook (Part I of the CPA Canada Handbook (i.e. IFRS) is referred to where Part IV is silent).	Measure and report the obligation for employee retirement benefits, attribute the costs of those benefits to the periods in which the related services are rendered and to provide information on the financial position of the plan in accordance with PSAS.
Actuarial cost method	Modified aggregate method (level cost method)	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	PSAS allows choice regarding the valuing of plan assets at market-related value. Market -related values, are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied

	moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values For funding valuation, the plan uses the actuarial value of assets which are the market value of assets adjusted for investment gains / losses spread over a period of 3 years.		consistently. The Province has chosen to value OTPP's plan assets by adjusting to market value over a period of 5 years in accordance with PSAS.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate. For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work	Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. OTPP follows Part I (IAS 19) which requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on	Not specified. However two methods are specifically acknowledged in PSAS – a) discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing. [15] The Province of Ontario uses a discount rate for OTPP determined by reference to the expected long-term

[15] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

	For the purpose of the funding valuation, the plan uses a discount rate which is based on market related rates averaged over a period of 36 months. The discount rate used in the most recent funding valuation for OTPP as at January 1, 2015 was 4.85%.	bonds issued by the Province of Ontario. As illustrated in Appendix E, this is inconsistent with other Provincial pension plans in Canada which use as a discount rate, the long-term rate of return on plan assets. The discount rate used by OTPP in their December 31, 2015 financial statements was 3.25%.	return on plan assets. The discount rate used by the Province to account for OTPP in their March 31, 2016 financial statements was 6.25%. This is the long-term rate of return on plan assets which is in accordance with PSAS.
Independent verification		OTPP's financial statements are audited by Deloitte LLP.	The Province's financial statements are audited by the OAG.
Underlying population data	All valuations use consistent underlying data of the population covered by the plan (membership data as at August 30 of the prior year projected to the valuation date is used].		
Inflation rate	All valuations treat inflation in a consistent manner (on a best estimate basis). Best estimate assumptions are derived based on the best estimate of future events. Best estimates of inflation by the Province may be different from those of the OTPP Board, even though they are both best estimate assumptions. In developing its best estimate assumptions, the Province references a broad range of available data, including the best estimate from the OTPP Board.		
Demographic assumptions	Valuations use consistent demographic assumptions (best estimate by the OTPP Board).		Under PSAS, the Province is not required to prescribe demographic assumptions.
Other economic assumptions	The OTPP Board develops its own salary escalation assumption to be used for both the funding and the Board's financial statement valuation. Economic assumptions other than the discount rate, inflation rate and salary assumptions are determined by the Board. These are the same for funding valuation and the Board's financial statement valuation.		The Province prescribes the future salary escalation rates. The Province develops this assumption by referencing the outcome of the most recent collective agreements as

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		well as compensation policies issued from time to time by the government and the historic increases granted.

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Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	ON 1	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	ON 2	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	ON 3	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	ON 4	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	ON 5	5.95%	LT return on plan assets
Alberta					
Teachers' Post-1992 Pension Plan	6.80%	LT return on plan assets	AB 1	7.00%	LT return on plan assets
Universities Academic Pension Plan	6.00%	LT return on plan assets	AB 2	5.95%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)					
Local Authorities Pension Plan	5.60%	LT return on plan assets	AB 3	5.60%	LT return on plan assets
Public Service Pension Plan	6.00%	LT return on plan assets	AB 4	6.00%	LT return on plan assets
Management Employees Pension Plan	6.10%	LT return on plan assets	AB 5	6.10%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.40%	LT return on plan assets	AB 6	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.00%	LT return on plan assets	AB 7	6.00%	LT return on plan assets
Special Forces Pension Plan	5.90%	LT return on plan assets	AB 8	5.90%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan					
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.50%	LT return on plan assets	SK 1	6.50%	LT return on plan assets
British Columbia					
Public Service Pension Plan	6.50%	LT return on plan assets	BC 1	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	BC 2	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	BC 3	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	BC 4	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec					
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	QC 1	6.40%	LT return on plan assets less inflation
Newfoundland					
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	NF 1	5.80%	LT return on plan assets
Nova Scotia					
Nova Scotia Public Service Superannuation Plan (PSSP)	6.70%	LT return on plan assets	NS 1	6.15%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	NS 2	6.25%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba					
Civil Service Superannuation Plan	6.00%	LT return on plan assets	MB 1	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.25%	LT return on plan assets	MB 2	6.00%	LT return on plan assets
New Brunswick					
Provincial Court Act and Provincial Court Judges Pension Act (JUDGE)	6.15%	LT return on plan assets		No individual financial statements	
Pension Plan for Management Employees of New Brunswick School Districts (Sch-Mgt)	6.05%	LT return on plan assets		No individual financial statements	
Pension Plan for General Labour, Trades and Services Employees of New Brunswick School Districts (GLTS)	6.05%	LT return on plan assets		No individual financial statements	
Pension Plan for Full-Time CUPE 2745 Employees fo New Brunswick School Districts (CUPE 2745)	6.05%	LT return on plan assets		No individual financial statements	

7

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
New Brunswick					
NHMgt, NH-G&S, NH-N&P (i.e NH Nursing Home)	6.20%	LT return on plan assets		No individual financial statements	
CUPE Employees of New Brunswick Hospital (shared risk)	5.45%	LT return on plan assets		No individual financial statements	
Certain Bargaining Employees of New Brunswick (shared risk)	5.70%	LT return on plan assets		No individual financial statements	
Public Service Shared Risk Pension Plan	6.00%	LT return on plan assets		No individual financial statements	
New Brunswick Teachers' Pension Plan (shared risk)	6.15%	LT return on plan assets		No individual financial statements	

8

Appendix F – Comparison of definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, Section PS 3060 paragraph .06. Section PS 3060 was introduced into the Public Sector Accounting (PSA) Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the

			definition of a JDBP focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a JDBP are similar.

While similar in concept and wording, the definition of a JDBP is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including JDBPs.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from 1990 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	Contributions by teachers increased by 1 percentage point (from 7.9% to 8.9%) effective January 1, 1990 per legislation.	Legislated an increase in matching contributions (from 7.9% to 8.9%) effective January 1, 1990 and responsibility to finance the initial unfunded liability through a series of special payments	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	$0

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			reduce the value of remaining special payments	
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	

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).

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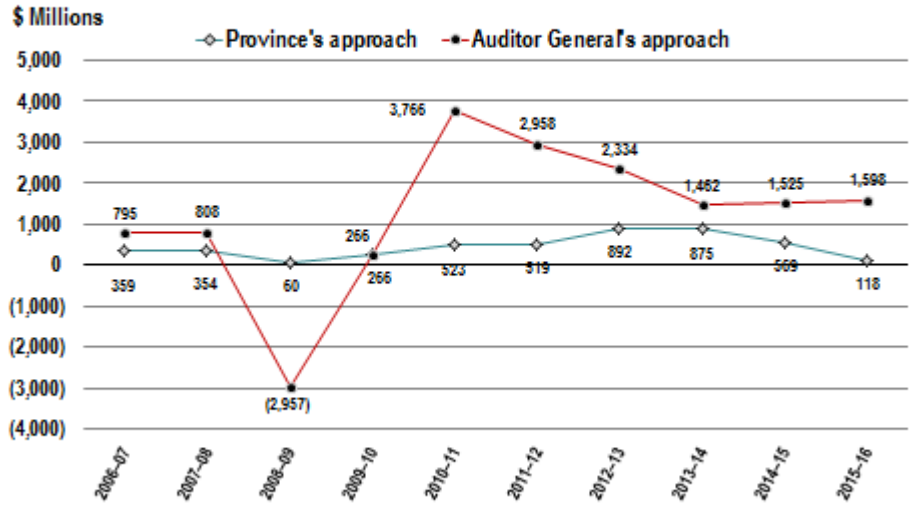
Appendix H - Illustrative impact of 100% valuation allowance on OTPP on key indicators for prior 10 years

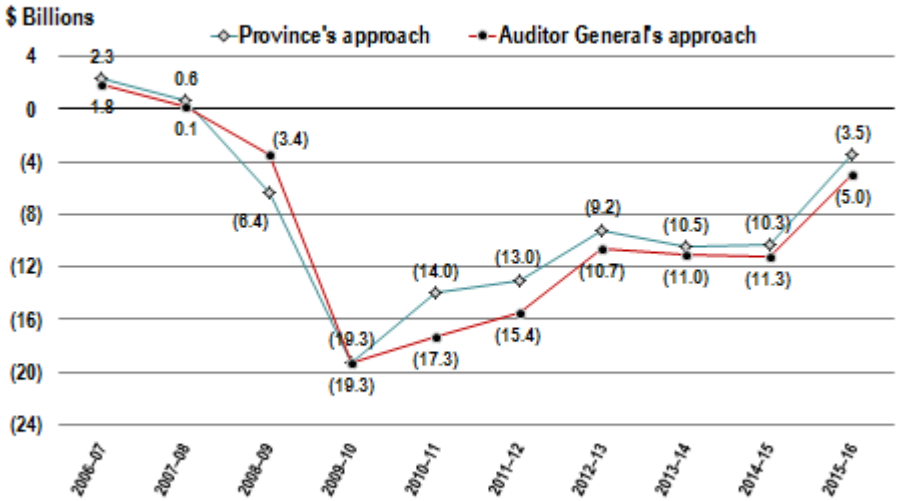
OTPP expense comparison — 10-year

Chart 1



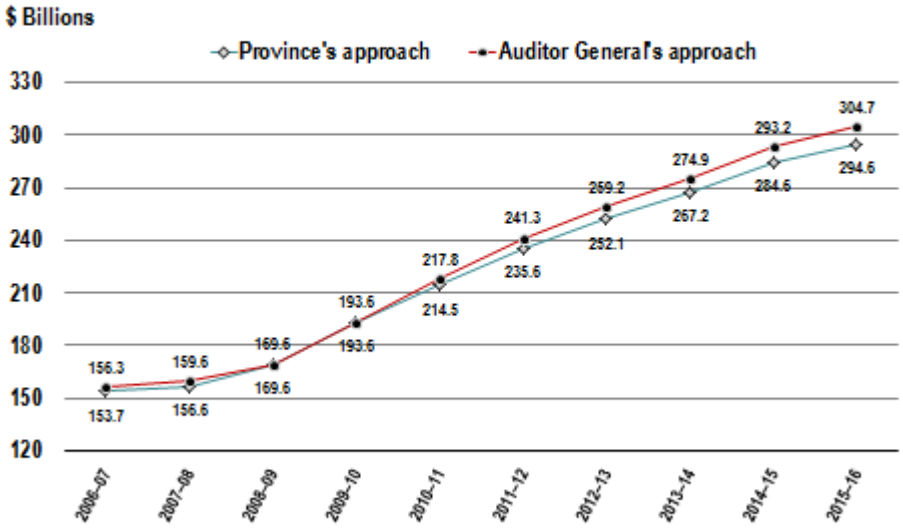
Surplus/(deficit) comparison — 10-year

Chart 2



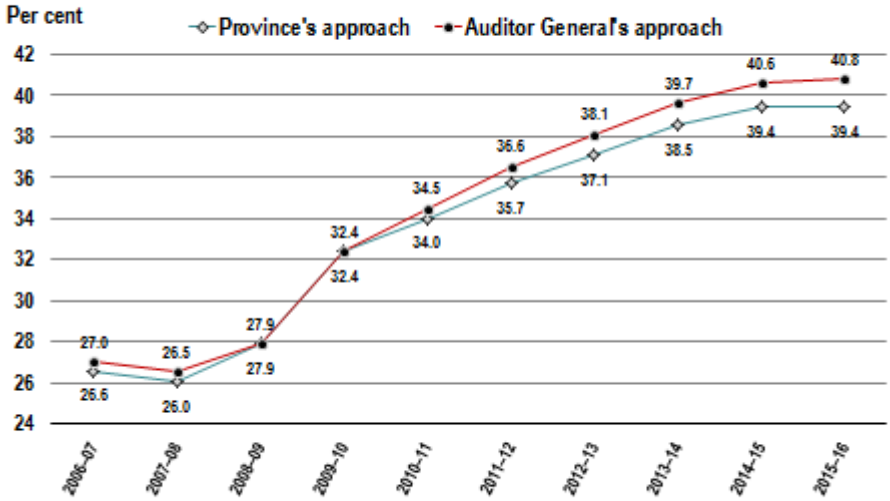
Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year

Chart 4



Appendix I – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the

event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan (''PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[16] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[16] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

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Appendix J – Summary of OTPP Funding Rate Assumptions and Provincial Discount Rates vs. Actual Performance

Ontario Teacher's Pension Plan
Rate Comparison

	OTPP Annual Performance	OTPP Filed Discount Rate *	Province Economic Assumption for Nominal Return
2005	17.2%	6.48%	7.00%
2006	13.2%		7.00%
2007	4.5%		6.75%
2008	-18.0%	5.65%	6.75%
2009	13.0%	5.00%	6.75%
2010	14.3%		6.75%
2011	11.2%	5.40%	6.75%
2012	13.0%	5.30%	6.75%
2013	10.9%		6.75%
2014	11.8%	4.95%	6.75%
2015	13.0%	4.85%	6.50%
2016	n/a	n/a	6.25%

* The plan does not file a valuation annually. Under the Pension Benefits Act, plans must file at least every three years

Ontario Teacher's Pension Plan
Plan Performance

2015	13.0%
2014	11.8%
4 - Year	12.2%
10- year	8.2%
Inception	10.3%

DRAFT

FW_ Proposal - RFS NUMBER _ TBS-OTB-OPCD-22.rtf

From: Donaldson, Mark (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Proposal - RFS NUMBER : TBS-OTB-OPCD-22
Date: Friday, November 03, 2017 15:09:34
Attachment 1: image001.png
Attachment 2: Deloitte_Ontario_TBS_OTB_OPCD_22 - Tecnical Proposal.pdf
Attachment 3: Deloitte_Ontario_TBS_OTB_OPCD_22 - Pricing Proposal.pdf

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From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: November 3, 2017 2:57 PM
To: Donaldson, Mark (TBS)
Subject: Proposal - RFS NUMBER : TBS-OTB-OPCD-22

Mr. Donaldson

You will find attached our technical proposal and separately our pricing proposal to provide pension and non-pension benefit advice.

We have structured our technical proposal in order to cover the various criteria of the RFS while the pricing proposal is provided separately as per the RFS requirement in the provided form.

Should you have any question, you can contact me directly.

We look forward to the possibility of working with the Treasury Board Secretariat (Office of the Provincial Controller) in this important mandate.

Have a nice weekend

Regards

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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Public Sector Pension and Non-Pension Benefit - Management Consulting Services

Technical Proposal to serve the Ontario Government

Technical proposal
Reference: RFS TBS-OTB-OPCD-22

Closing date: Friday, November 3, 2017

Proponent and contact information

Deloitte LLP
1190, avenue des Canadiens-de-Montréal
Montréal, Québec H3B 0M7
Canada

Contact: Martin Raymond
Email: maraymond@deloitte.ca
Tel: (514) 393-7367

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We will:

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- **understand** your business and what is important to you
- **provide** value and build trust through technical competence and consistent results
- **demonstrate** professionalism through effective interaction and communications
- provide a **no surprises** experience

Deloitte LLP
1190, avenue des Canadiens-de-
Montréal, QC H3B 0M7
Canada
Tel: (514) 393-7367
www.deloitte.ca

November 3, 2017

Private

Email delivery

Attention of Mark Donaldson
Director, Treasury Board Secretariat
Office of the Provincial Controller Division

Re: Actuarial Services – RFS TBS-OTB-OPCD-22 (technical proposal)

Deloitte is pleased to submit this technical proposal to provide actuarial services to the Office of the Provincial Controller Division (the "OPCD") about pension and non-pension benefit management consulting services. As you will see from our proposal, professionals at Deloitte possess relevant experience and have conducted similar engagements for a variety of clients, including public sector. Should we be the successful bidder, we are also able to draw upon an experienced team who not only understands actuarial services, but also appreciates the challenges and complexities associated with the communication issues of actuarial results and accounting complexities. Deloitte being highly involved in pension and non-pension benefit plans audit, the OPCD will have access to individuals that have significant expertise in understanding the market practice on accounting for these benefits and have specialized views on interpretation of accounting standards.

If you have any questions with respect to the information contained within this proposal, please do not hesitate to contact us. We look forward to working with the OPCD on this important initiative.

For ease of presentation and to maintain the format of the submission in line with the RFS requirement, we note that after an executive summary, the next 2 sections include the completed Submission form and a summary of the Scope of services. The other sections will cover the required Schedules, pricing (A) being provided in a separate document and the resume / references for our team members (B). We have added other Schedules to answer the Experience and Qualifications aspects of the Evaluation criteria.

Sincerely,

Martin Raymond
Partner

Deloitte LLP

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Executive summary

Deloitte is delighted to have this opportunity to propose actuarial services to the OPCD with regards to pension and non-pension benefit management consulting services. We believe that our firm is an ideal choice to serve you.

> We surpass the mandatory requirements

Deloitte, one of Canada's leading professional services firms, provides audit, tax, consulting, and financial advisory services through more than 8,000 people in 56 offices, including a key office in the Toronto area.

Deloitte actuarial group has an extensive experience in performing and reviewing actuarial accounting valuations for pension and non-pension benefit plans. We serve a various range of clients, including many municipal clients or other public sector entities.

> We have the experience and skills to provide an outstanding service

Our team is built up of actuaries and they have a continuous access to highly qualified accountants that will provide the OPCD with work of high-quality. Their experience in pension and benefit accounting under PSAS and their profile will ensure that the work will be performed in timely manner in accordance with professional standards. All the team members are familiar with the recommendations contained in PSAS for pension accounting.

> We have a clear understanding of the process and requirements to perform accounting valuations

As we provide similar services to a various range of clients on a continuous basis, we have a good understanding of the issues and a comprehensive view of the market practice. We do review actuarial calculations, we do perform actuarial calculations for other clients, we perform review and selection of best estimate assumptions in a large number of cases so we are involved in all of the steps that are required by the activities listed in the RFS.

> We offer a wide range of value added services to our clients

As actuarial consultants, we focus on listening to clients and designing specific solutions to achieve targeted results. We do not restrict ourselves to regular traditional approaches but try to define the most efficient one that applies to the client. In every task, we will tailor our level of involvement to your requirements and internal resources. We will advise you, and work in partnership with you, to achieve your objectives.

We value personalized approach and use open dialogue as much as possible. Our team will work with you in suggesting creative opportunities that add value to their consulting assignments. Our professionals are used in their day-to-day job to perform reviews and build valuation models. They will be in great position to support the specific needs as they come up.

Our group has a unique balance in that it does work on providing consulting services, with also other work coming from audit support. This situation provides the group with both the consulting aspect and creativity along with the vision of rigorous application from auditing. This balance is important to develop better consultants that will provide services in line with today's highly regulated environment.

> We regularly provide similar services to satisfied clients

Deloitte takes pride in developing relations based on communication and trust. Our knowledge and understanding of the pension and non-pension benefits allowed us to thrive on the financial services market. Here is a list of public sector clients that Deloitte serves or have served recently:

- City of Montreal
- NB Government
- OTPP
- Quebec Municipal Ministry
- City of Laval
- City of St-John (NB)
- Office of the Auditor General of Canada
- Revenu Québec

Submission form

Request for Services Number: **TBS-OTB-OPCD-22**

To: HER MAJESTY THE QUEEN in right of Ontario as represented by President of Treasury Board Secretariat

1. Vendor Information

(a) The full legal name of the Vendor is: **Deloitte LLP**

(b) Please identify any other relevant name under which the Vendor conducts business:

Deloitte S.E.N.C.R.L./s.r.l
Deloitte Inc.

(c) The Vendor's address, telephone and facsimile numbers are:
Bay Adelaide Centre, East Tower
22 Adelaide Street West, Suite 200
Toronto, ON M5H 0A9

Tel: 416-601-6150
Fax: 416-601-6151

(d) The name and title of the Vendor's Representative:
Martin Raymond, Partner

(e) The mailing address, phone number and e-mail address of the Vendor's Representative:

1190 Avenue des Canadiens-de-Montréal,
Montréal, Quebec
Canada
H3B 0M7
Tel: 514-393-7367
Fax: 514-390-4104
Email: maraymond@deloitte.ca

(f) State the name, address, telephone and facsimile numbers and e-mail address of the Company Security Officer (CSO) for the Vendor:

Cara Warburton
Bay Adelaide Centre, East Tower
22 Adelaide Street West, Suite 200
Toronto, ON M5H 0A9
Tel: 416-601-5763
Fax: 416-601-6151
E-mail: cawarburton@deloitte.ca

(g) State the name and title of each of the individuals that the Vendor is proposing for this Project:

Names	**Titles**
Martin Raymond	Partner
Trevor Gary	Senior
Matt Colley	Senior Manager

2. Submission Requirements and Accuracy of Information

The Vendor accepts the terms and conditions set out in the RFS. While this submission is provided for evaluation purposes only and is not legally binding before the execution of a SOW, I confirm that the information provided is accurate.

3. Certificate(s) of Insurance

As required in Article 32.4 – Proof of Insurance in the Master Agreement, please identify the status of the Vendor's Certificate(s) of Insurance by placing a check mark (√) in one (1) of the following three (3) boxes:

☒ a) the Vendor has previously submitted a Certificate of Insurance to MGCS, which has been approved

☐ b) the Vendor has included its Certificate of Insurance with this RFS submission (that will be subject to approval by MGCS) prior to the Client issuing a SOW

☐ c) the Vendor agrees to submit a Certificate of Insurance (that will be subject to approval by MGCS) prior to the Client issuing a SOW

4. Conflict of Interest

The Vendor must complete the following:

(a) If the box below is left blank, the Vendor will be deemed to declare that: (1) there was no Conflict of Interest in preparing its submission; and (2) there is no foreseeable Conflict of Interest in the Vendor or any of its Personnel performing the contractual obligations contemplated in the Request for Services.

(b) Otherwise, if the statement below applies, check the box.

☐ **The Vendor declares that there is an actual or potential Conflict of Interest relating to the preparation of its submission, and/or the Vendor foresees an actual or potential Conflict of Interest in it and/or its Personnel performing the contractual obligations contemplated in the Request for Services.**

(c) If the Vendor declares an actual or potential Conflict of Interest by marking the box above, the Vendor must set out below details of the actual or potential Conflict of Interest:
N/A

(d) The following individuals, as employees, advisors, or in any other capacity (i) participated in the preparation of our submission; **AND** (ii were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:
Job Classification (of last position with OPS):
Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):
Last Date of Employment with OPS:
Name of Last Supervisor with OPS:
Brief Description of Individual's Job Functions (at last position with OPS):

Brief Description of Nature of Individual's Participation in Preparation of Submission:

(e) The following are individuals that: (i) are proposed to be assigned by the Vendor to perform work under the SOW; **AND** (ii) were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:
Job Classification (of last position with OPS):
Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):
Last Date of Employment with OPS:
Name of Last Supervisor with OPS:
Brief Description of Individual's Job Functions (at last position with OPS):

(f) We agree that, upon request, we shall provide the Client with a Conflict of Interest Declaration from each individual identified above in the form prescribed by the Client.

5. Schedules

This submission includes the following Schedules:

Schedule A (Pricing Schedule) – provided in a separate document as required
Schedule B (Resumes and references)
Schedule C (Similar projects and working with Governments)
Schedule D (Reports for public pension related initiative)
Schedule E (Ceiling test and sensitivity analysis scenarios)
Schedule F (Methodology and implementation plan)

Deloitte LLP
I acknowledge that providing my name on the line below in electronic form will constitute a signature for the purposes of the *Electronic Commerce Act, 2000*, S.O. 2000, c. 17.

I have authority to bind the Vendor.

Per:

Signature:

Name: Martin Raymond
Title: Partner
Date: November 3, 2017

Scope of services

Treasury Board Secretariat, Office of the Provincial Controller (OPCD) requires accounting/actuarial services to support the preparation/review of pension and non-pension benefit expense/liability numbers of various pension plans where Province is sole owner and joint sponsor. The Province reports these numbers in various public documents (i.e. Fall Economic Statements, Budget, Pre-election Report and Public Accounts) and consultant requires to review these numbers/accounting and to make sure that numbers/accounting prepared by the OPCD met with requirements with Public Sector Accounting Standards.

Scope of the services

The Services and Deliverables to be provided by the Vendor will include the following:

- Working with management of the Office of the Provincial Controller's Accounting Policy and Financial Reporting Branch (APFRB), the provider will provide actuarial/accounting services related to the following possible areas:
  - Review the economic assumptions (i.e. management best estimates) used for the accounting valuations of the pension plans and non-pension benefits reported by the Province.
  - Review the actual and forecast numbers prepared by APFR staffs for the Province's various pension and non-pension benefits. Including assessing the reasonableness and completeness of assumptions used by APFRB staff in the models, including any sensitivity analysis as required.
  - Provide recommendations, if any, on improvements in the pension and non-pension benefits accounting models currently used to by APFRB.
  - Perform ceiling test requirements in accordance with PS3250.50 to PS3250.59 for all sole sponsor or joint sponsor pension plans that are in an accrued benefit asset position.
  - Provide advice on any accounting issues related to pension and non-pension benefits, as required.
  - Participate in discussions with internal and external stakeholders, as required.

- The Vendor will participate in meetings as necessary to support the engagement objectives.

Based on the RFS, it is estimated that 150 hours of effort over the term of the agreement to be split equally between the following resources for the deliverables of this project:

- One (1) Senior Consultant / Project Lead
- One (1) Intermediate Consultant / Sr. Analyst

The work is expected to start December 4, 2017 and end June 15, 2019.

The successful candidate must demonstrate experience/expertise:

- Understanding and experience with government financial reporting objectives of transparency and accountability, including an in-depth understanding of public sector accounting standards
- With Public Sector Accounting Standards (PSAB), especially as related to pension and non-pension actuarial valuation.
- Working with a variety of Public Sector stakeholders in appropriate accounting and measurement under PSAB.
- With Ontario government's protocols regarding document confidentiality.

Schedule A – Pricing

As per the RFS requirement, the pricing proposal has been provided in a separate file named:
Deloitte_Ontario_TBS_OTB_OPCD_22 – Pricing Proposal

Schedule B – Resumes and References

Based on the RFS requirement:

- Vendors are expected to submit a resume for each consultant proposed in the Submission Form - please include the resumes as Schedule B to your Submission Form

  NOTE : resumes are included in this Section

- For each proposed consultant, Vendors are expected to submit the consultant's most current project(s), and submit references (include name, title, organization and telephone number) whom the Client may contact for the purpose of conducting reference checks

  NOTE : some projects are presented and references are included in this Section

- Vendors are expected to demonstrate in their submission that each proposed consultant has the knowledge, experience and all other qualifications for the proposed Role, and will be able to provide the requested services

  NOTE : the description found in this Section will show the qualification of our proposed team

- Vendors must provide the Client with the opportunity to interview each proposed consultant, and must not charge the Client in connection with any interview

  NOTE : we confirm that interview with our proposed team is available as needed

- Vendors must identify all subcontractors that they propose to use, and must also identify which consultant(s) is provided by which subcontractor

  NOTE : we will not use any subcontractors, all services required will be provided by Deloitte professionals

Proposed Team

As you will see from this section, our proposed team does have the necessary qualification, skills and experience to deliver the needed activities related to this mandate. Considering that the focus of the work will be related to pension and non-pension benefit plans accounting results and work will include some technical application of elements such as asset ceiling, we have included 2 actuaries in the Submission form that have both deep actuarial and accounting knowledge, experience and expertise. One member is fully qualified Fellow.

Having worked in large actuarial consulting firms and also being within Deloitte, our group has built the deep key accounting knowledge to provide them with the overall skills to deliver the actuarial/accounting work that the OPCD is looking for.

The Project Lead that will handle OPCD work is Martin Raymond (partner), the leading consulting actuary for pension and non-pension benefit plans at Deloitte. In his work, Martin will be supported by Trevor Gary (senior). Martin joined Deloitte in October 2011 to lead the actuarial pension and benefit practice. Since then,

his group has been supporting Deloitte auditors with all regards related to pension and benefits. He is also responsible for any specific consulting pension and benefit services on non-audit Deloitte clients.

In their everyday work, Martin and Trevor have access to some specific personnel of Deloitte that do have very deep pension and benefit accounting expertise. Although not expected to be involved, the availability of the other resources makes it of additional value to the OPCD should any complex accounting issue come up. If required, their involvement is likely to be more for sound-boarding support or validation of approach. Matt Colley will be one subject matter expert that may have some implication in supporting our 2 actuaries. Matt is already involved in some other advice support to the Ontario government. His understanding of the OPCD environment, structure and strategy will ensure that we always provide the optimal approach in working with the OPCD. His involvement with Ontario Government for many years will be helpful to the team for any protocol or process considerations. The RFS mentions confidentiality of documents.

Both Martin and Trevor have worked previously with the OPCD on specific pension accounting matters and therefore are familiar with the approach and the communication / discussion process. They will use this experience to ensure that the implementation is performed on solid basis and that we keep open communication ongoing for the period of the project. Matt though his extensive experience will give an additional source of knowledge to ensure adequate steps are taken by our team.

Since Martin and Trevor are identified as the 2 main members of the team to work on deliverables (Project Lead and Senior Analyst) we have provided more details for experience and references for these 2. For Matt, we provided the resume but if needed, additional references will be available on demand.

Proposed resources		
Name of Individual	**Level**	**Description of role**
Martin Raymond (Project Lead)	Partner, Actuarial Services	As the account manager, Martin will be responsible for relation with the OPCD. He will be the reference person for any strategic issue and will ensure that high-quality services be provided. He will work in collaboration with Trevor on the delivery of documents and advice. He will be responsible for the timeliness and quality of services performed, as well as ensuring that OPCD expectations are met or exceeded. His vast experience in both accounting and actuarial fields will provide all the expertise that will be needed for the activities to be performed. Considering the extensive knowledge that Martin has in public sector accounting for pension and non-pension benefit plans, he will drive the orientation of the analysis and advice.
Trevor Gary (Senior Analyst)	Senior, Actuarial Services	Trevor will be responsible to prepare along with Martin the documentation needed on the account. He will be involved in any data and calculations that may be required. He will be a day-to-day contact for data, questions and follow-ups. He will participate in most of the communications with the OPCD. Trevor and Martin will meet on regular basis to provide status updates and agree to the required steps. During the implementation, his role will be to lead the information gathering and prepare initial documentation.
Matt Colley (subject matter expert on Ontario processes and protocols)	Senior Manager, Audit	Matt is a Deloitte professional that is highly familiar with the Ontario processes and protocols. Based on his experience, he will support, as needed the proposed team on adhoc basis. He will help ensure approach taken is optimal considering the Ontario government practices. Considering he also has knowledge in pension accounting, he may serve as needed for sound boarding in accounting issues that may be faced during the mandate.

Shown expertise of the proposed team

Within the resumes of the proposed team, you will find more specific expertise for both Martin and Trevor. The following paragraphs are meant to show the extent of the work that both Martin and Trevor are involved on a regular basis. The proposed team works significantly with PS3250 and PS3255 annually as well as other pension and non-pension benefit plans accounting standards. The team has worked in all aspects of a valuation required for accounting purposes, namely:

- Review of membership data and sufficient information to support extrapolation purposes
- Selection and review of management best estimate assumptions for economic and demographic factors
- Prepare models needed for selection of assumptions
- Determine the approach to define the accounting discount rate
- Prepare the asset (liability) on the balance sheet and reconcile year change, explaining gains and losses
- Perform accounting valuations and apply actuarial valuation methodology mandated by PS3250 and PS3255
- Prepare the year expense and reconcile year change
- Apply asset ceiling test when asset shown on the balance sheet
- Prepare sensitivity analysis to key parameters
- Prepare actuarial report with the required content for accounting disclosures
- Answer auditor questions, including Auditor Generals

The pension actuarial group do perform annually more than 150 audits on different standard basis. Among these we are involved in 15 to 20 comprehensive audit reviews of public sectors. Sitting in an accounting firm and being employee benefit accounting specialists, we are always searching through the applicable accounting standards to assess if work is performed in accordance with the requirements of those standards. This is definitively one key advantage that our professionals do have to support our clients in that we know the details of the standards along with the detailed actuarial calculations. We also have access internally to very highly specialized experts (accountants) that are very familiar with how a standard has been developed. Sometimes it is important to understand the spirit of the standard to determine what is acceptable or not and not just the wording of a paragraph of the standard.

As you will see from some experiences we have detailed, our team has been involved in very complex key actuarial and accounting issues, such as application of public sector to Shared risk plan model in New Brunswick. In performing this work, our team demonstrated a high level of knowledge of the accounting standards to define how it would apply to the specific plan model and how the actuarial calculations are performed. This is one proof of the high familiarity that we do have with the standards and not only the public sector but also with other standards.

We need to design and run valuation models for a large number of our audit files. Above this audit part, we also perform a number of specific actuarial valuation reports prepared for accounting purposes to help entities in the preparation of their financial statements. We are therefore involved with many different clients in steps starting from data gathering through accounting valuation results calculation and all the way to audit of results and financial reporting.

Considering the large number of clients we worked with, we are exposed to best practices, which makes us very familiar with the evolution of the public standards and the actuarial work performed.

Our team is really connected to future public sector changes as Martin Raymond is involved in the CPA Task Force working on PS 3250 and PS 3255 review since 2016.

We perform a significant number of actuarial mandates for public sector in valuation services and also in audit services. As an illustration, here is a list of high-profile public sector clients for which we have been involved in recent years:

- City of Montreal
- NB Government
- OTPP
- Quebec Municipal Ministry
- City of Laval
- City of St-John (NB)
- Office of the Auditor General of Canada
- Revenu Québec

Resumes and references

Following are the resumes of the proposed team along with references and specific relevant experience for Martin and Trevor the main resources identified to provide the deliverables.

Martin Raymond, FSA, FCIA

Partner – Audit & Advisory
Actuarial, Rewards and Analytics

Profile

For 23 years, Martin has been with the Consulting practice as a specialist in pension plans. He is also an expert in retirement and benefits accounting, having served as the national specialist in this area for a large actuarial consulting firm. This experience has provided him with the skills to serve a diverse clientele and to handle complex accounting and financial disclosure issues.

As a partner in the actuarial department, Martin is responsible for managing and supervising the work related to Canadian pension plans and benefits for Audit teams but also for general consulting. Additionally, he is also actively involved in answering questions related to the application of pension accounting and pension legislation while assisting the firm's decision-making process in these areas.

His role includes follow-up on changes in accounting standards and best practices. Over the years, he developed different tools required to perform calculations and ensured integrity of work in accordance with the standards. He was also highly involved in training, both internally and to the firm's clients. His expertise was used many times in resolving clients' issues for accounting treatment of special events and also situations that demanded specific accounting interpretations.

Along with his responsibility as national specialist on accounting, Martin also served as general consultant for clients on actuarial issues. His work encompassed looking at funding and accounting projections along with optimizing strategies. He also helped employers in negotiation support to identify possible plan design changes and evaluating the costs. He supported employers in selecting actuarial assumptions and reviewed work of more junior staff to assess reasonableness of results. He was responsible for quality of services offered along with satisfaction of clients.

His skills as communicator has made him highly appreciated by clients, pension plan members and fellow colleagues. He takes pride in translating complex issues into accessible actuarial and accounting concepts for people less familiar with these matters. For pension and benefit arrangements to be appreciated by members, it needs to be well understood. This represents in many cases the challenge for today's plan sponsors and Martin would surely be an addition to this mandate.

Professional affiliations/Certifications

- Fellow of the Society of Actuaries (FSA since 1998)
- Fellow of the Canadian Institute of Actuaries (FICA since 1998)

Education

- B.Math. (actuarial science) – Université de Montréal

Other activities

- Speaker at the Canadian Institute in 2001-2002 on termination of plans
- Instructor at the AGFMQ (Quebec association of municipal financial managers) in benefits programs accounting in a municipal setting in 2006
- Member of the CIA (Canadian Institute of Actuaries) Task Force on Pension and Post-retirement Benefit Accounting Discount Rates (2009 to the present)
- Speaker at the Canadian Institute of Actuaries' pension seminar in 2012.
- Member of the CPA Task force on review of Public Sector accounting standards (2016 and forward)

Knowledge / experience and current / recent projects

His expertise in the pension accounting field has been recognized by clients, fellow actuaries and also by participation through accounting specific working groups. Of particular interest for this specific mandate, we note that Martin is part of the CPA Task Force on employee benefits that is reviewing the standards (PS3250 and PS3255) to determine if and to what extent changes might be made to these standards to reflect the evolution in accounting practice since their initial implementation. Some issues that are to be looked at include deferral of actuarial gains and losses, discount rate selection, shared risk plan (SRP) treatment and multi-employer plans. Since a number of these elements are of interest to public sector entities, having someone that is involved in the discussions will provide great insight for the OPCD to understand the issues, the discussion elements and the possible outcomes. Some of these possible changes might be included part of the analysis and sensibility work in order to get a complete perspective of what might eventually come up and affect the public sector accounting for pension and non-pension benefits.

Martin has also worked with numerous public sector clients either as a consultant providing full valuation services but also through the auditing role of ensuring that accounting was performed in conformity with the accounting standards. His involvement in all types of employee benefit accounting standards (US, IFRS, ASPE, PSAS) has provided him with a broad view of the possible issues that come up and the likely ways of addressing them.

He is also recognized by the Québec municipalities Ministry as a key person involved in number of complex actuarial / accounting issues that have come up on pension and benefit accounting since the Québec municipalities have transitioned to public sector accounting in 2007. This implication is still ongoing on regular occasions when specific situations come up that need insights on the appropriate treatment. He has been involved in a number of areas that demanded accounting and actuarial expertise since that date, including:

- Impact of 2007 transition on municipalities financial statements
- Treatment of funded and non funded plans
- Selection of discount rate based on cost of borrowing
- Treatment of asset ceiling
- Use of reliefs for taxation purposes for various elements (past service costs, asset ceiling, non funded plans)
- Special approach used after the 2008 financial crisis to alleviate the taxation requirements
- Review of changes in pension plan legislation specific to municipalities and define the appropriate treatments.

He also has worked closely with the federal OAG on a number of pension and non-pension audit supports for which his collaborative approach along with his understanding of issues and ease to communicate have been greatly appreciated by the OAG personnel. The reporting format of the information, the illustrations provided on complex issues and the deep knowledge of both actuarial work and accounting understanding have been part of the successes of all the mandates performed.

Along with the Québec Ministry support and the OAG audit supports described as current projects, for which we do provide references, it should be noted that another main area that shows expertise relates to his involvement with the Government of NB and City of St John (NB) on Shared Risk Plan (SRP) accounting treatment. This is a very complex actuarial and accounting area that is still being regularly discussed with actuarial firms and accounting standard setters. The main elements that were part of the activities are:

- Review of the SRP legislation
- Review of plan provisions and funding policy
- Review of actuarial valuation reports on SRP

- Review of stochastic projection results to meet the risk management criteria
- Review of the accounting standards to define the defined benefit / defined contribution classification for accounting treatment
- Review the selection of assumption process as some benefits are conditional on plan situation
- Review of the joint defined benefit accounting provisions
- Meetings / discussions with clients and their actuaries
- Work in collaboration with the actuaries to define the appropriate calculations
- Review valuation numbers, accounting figures and confirm it is performed in accordance with accounting standards

All through these 2 SRP mandates, Martin was highly involved in helping understanding the standards to define the appropriate actuarial valuation approach, working in collaboration to find appropriate solutions and providing along the way the knowledge enhancements that the various parties needed to appreciate the issues and understand the solutions.

References

We authorize the OPCD to verify information provided to confirm client satisfaction and demonstrated success.

Relevant project #1 – Office of the Auditor General	
Years of work	2016 and 2017
Description of Contract	The Office of the Auditor General provides an allotment of sick leave days per month of service to its employee. The unused sick days given in a year may be carried forward to future years. This type of benefit requires an actuarial valuation to determine the defined benefit obligation and the expense of each fiscal year under PSAS. • Review plan provisions and prepare a summary • Review data and prepare a summary • Recommend appropriate assumptions • Perform a detailed calculation of the liability of the OAG for sick leave benefits accumulated by its employees as of year-end; • Determine the related components to be disclosed in the financial statements, I.e. the benefit costs, the interest cost, and the actuarial loss or gain for the year; • Estimate the benefit costs for the following year; • Perform a sensitivity analysis on the following assumptions: discount rate, annual rate of increase in salary, retirement age and use of accumulated sick leave. • Prepare a report in accordance with standards of practice of the Canadian Institute of Actuaries (CIA) and with PSAS (PS 3255)
Contact Person	Shawn Audette
Telephone and Email	(613) 952-0213 ext: 5290 shawn.audette@oag-bvg.gc.ca

Relevant project #2 – City of Montréal	
Year of work	1997 to 2017
Description of Contract	Numerous cities on the island of Montreal merged in recent years into the City of Montreal. With these mergers came also the application of public sector accounting to municipalities in Quebec. As such, the City was faced with more than 40 pension and benefit plans to account for. Martin was involved over 5 years into preparing accounting results for the various plans and harmonizing communications for the City representatives. Communications to the management was also crucial and Martin was involved in many key employer meetings. His work also included treatment of many special events and also ensuring that work was in accordance with accounting requirements. He supported the setup of an accounting document that follow-up the quarterly evolution of the expense and the explanation of changes. The document also showed the expected expense over a 5-yr period in stochastic modelling. More recently, Martin is involved in the review of the accounting results of the pension plans. This includes the reconciliation of the results, the review of the assumptions, the impact of the changes in assumptions, the impact of changes in legislation and many more audit procedures related to employee benefits accounted under PS 3250 and PS 3255.
Contact Person	Jacques Marleau
Telephone and Email	(514) 872-3155 jmarleau@ville.montreal.qc.ca

Relevant project #3 – City of St John (NB)	
Year of work	2016
Description of Contract	Accounting of a pension plan under the Shared-Risk Plan model, a complex new pension framework in New-Brunswick. Define the accounting treatment under PS 3250: • Review plan provisions • Review legislation • Identify key accounting standards provisions • Discuss with Entity and actuary about the valuation of the obligation and accounting results • Work some illustrations and calculations to help the client through the process Define an acceptable approach within the accounting framework.
Contact Person	Hilary Nguyen
Telephone and Email	(506) 648-3713 hilary.nguyen@saintjohn.ca

Relevant project #4 – Québec Ministry of municipalities	
Year of work	1997 to 2017
Description of Contract	Public standards accounting is applicable to Québec municipalities since 1997. Martin involvement with the Ministry has been of different natures • Identify key accounting provisions that apply to pension plans • Review the impact on the municipalities financial statements • Identify some relief options to manage taxation level • Discuss the impact of the 2008 crisis on municipalities and identify the options / treatments to offer some tax management relief to the municipalities • Look more recently at the major changes in pension legislation that affected municipalities and identify the appropriate accounting treatment • On number of occasions be an expert / sound boarding resource for the Ministry on issues that come up
Contact Person	Yvon Bouchard
Telephone and Email	(418) 691-2015 (extension 3812) yvon.bouchard@mamot.gouv.qc.ca

Relevant project #5 – Revenu Québec	
Years of work	2016 and 2017
Description of Contract	Revenu Québec provides an allotment of sick leave days per month of service to its employee. The unused sick days given in a year may be carried forward to future years. This type of benefit requires an actuarial valuation to determine the defined benefit obligation and the expense of each fiscal year under PSAS. • Review plan provisions and prepare a summary • Review data and prepare a summary • Recommend appropriate assumptions • Perform a detailed calculation of the liability for sick leave benefits accumulated by its employees as of year-end; • Determine the related components to be disclosed in the financial statements, I.e. the benefit costs, the interest cost, and the actuarial loss or gain for the year; • Estimate the benefit costs for the following year; • Prepare a report in accordance with standards of practice of the Canadian Institute of Actuaries (CIA) and with PSAS (PS 3255)
Contact Person	Anne Rousseau
Telephone and Email	(418) 652-5127 anne.rousseau@revenuquebec.ca

Trevor Gary

Senior – Audit & Advisory
Actuarial, Rewards & Analytics

Profile

Trevor joined Deloitte's Actuarial, Rewards & Analytics Team from McMaster University where he completed his B.Sc. Mathematical Science and B.A. Economics. In the Audit practise, he actively leads on 50+ pension plan audits under various accounting standards. This included: review of accounting schedules, disclosures, and assumptions, audit planning for the pension plan, and liaising with clients and their consulting actuary to resolve pension related issues.

In the Advisory practice, Trevor acts as the main point of contact for Pension Due Diligence related to M&A/Transactions, he continues to actively pursue opportunities in the de-risking space including Buy-Outs, DB to DC conversion, and Plan Design, and has experience providing support for plans with a foreign domicile including the US, UK, and Switzerland.

Trevor's 'historical' Actuarial experience at Deloitte has included work on actuarial valuations, annual client regulatory filings, benefit calculations including Family Law Value calculations, and providing client support in regards to following Canadian Pension Regulation. Trevor has worked on plans under each of the 11 pension regulators in Canada.

Education
BA, McMaster University, 2012
B.Sc., McMaster University, 2013

Training
Trevor is close to completion of his Associate of the Society of Actuaries (A.S.A.) designation.

Awards
- 1st place - 2014 Actuarial National Student Association (ASNA) Case Study Competition
- 2012 Vanier Cup Champion

Knowledge / experience and current / recent projects

Trevor has been involved over recent years in a large number of audit supports on the different accounting standards. Over all of these mandates, Trevor's work did cover the full array of the accounting support:

- Review of assumptions used and confirm they are reasonable
- Ensure the methodologies applied are in accordance with the accounting standards
- Question management on accounting choices made
- Explain the major changes occurring during a year
- Detail the main gains and losses
- Compute the expense and balance sheet entry
- Review content of financial statements notes and comment on it
- Provide sensitivity and extrapolation results
- Review asset ceiling calculations and determine the economic future benefit calculation

In one of its main audit assignment he was involved in a very large pension plan in recalculating specific member benefit obligation by analysing plan provisions, applying the accounting methodology, perform the projection and determine obligation and current service cost. He did prepare an actuarial report covering the methodology, data and calculations results to compare with the actuary calculation.

He has also been recently involved in a very large accounting work with the OAG that covered 7 pension and employee benefit plans. The work specifically covered an array of the accounting valuation activities such as review of best estimate assumptions, review of sensitivities, and projection of results leading to a formal reporting going out to external user (the OAG). The documentation prepared by Trevor was received with high level of satisfaction and showed his level of professionalism and his commitment to quality work.

References

We authorize the OPCD to verify information provided to confirm client satisfaction and demonstrated success.

Relevant project #1 – Canada Post Corporation (OAG support)	
Year of work	2016 and 2017
Description of Contract	Trevor, along with Martin supported the OAG in reviewing the actuary's work and ensure work performed in accordance with the accounting standards and actuarial practice. Activities covered: • Review of assumptions • Review main changes occurring during the year • Review main elements of gains and losses (explain the source and calculate independent assessment) • Comment on content of report and disclosures • Validate sensitivity disclosures • Prepare a formal report for external use to be sent to the OAG • Prepare knowledge transfer to the OAG on some complex accounting and actuarial elements Deloitte did receive a very good feedback from the OAG on work performed and communication between OAG and Deloitte
Contact Person	Patrick Charbonneau
Telephone and Email	(613) 952-0213 (extension 2226) Patrick.charbonneau@oag-bvg.gc.ca

Relevant project #2 – Ontario Teachers' Pension Plan (OTPP)	
Year of work	2015 - 2017
Description of Contract	Applying the calculation requirements defined under accounting standards to perform independent assessment of member obligation result • Review plan provisions • Define appropriate benefit calculation • Apply legislation limits • Apply assumptions to the calculation • Discuss with the actuary some may results obtain to validate some aspects of the calculation • Compare results with the actuary calculation • Prepare a report defining our approach and key observations / results Objective was to ensure adequate obligation reported based on the accounting requirements.
Contact Person	Mary Cover
Telephone and Email	(416) 730-2976 mary_cover@otpp.com

Matt Colley, CPA, CA

Senior Manager
Assurance and Advisory

Profile

Matt is a Senior Manager in the Audit Advisory Practice in Toronto, which focuses on Accounting Advisory, Transaction Consultation, Finance Transformation, and Audit Analytic services. Matt has over 12 years of public accounting experience and has been exposed to a variety of engagements and cross functional teams. Matt joined Deloitte in 2004 and spent the majority of his initial years with the firm performing attest services mainly in the public sector organizations. Matt currently advises Public Sector and Private Sector organizations on complex accounting matters, as well as systems and process improvements. From 2012 to 2014, Matt was seconded to Deloitte's National Office to assist audit practitioners with complex accounting issues and to audit practitioners prepare their clients for new accounting standards that were being developed under IFRS, ASPE, Accounting Standards for Not for Profit Organizations and Public Sector Accounting Standards, including helping many clients with the adoptions of PS 3450.

Through his experience in auditing and advising many different types of public sector organizations, Matt has been exposed to various public sector accounting and regulatory issues. In addition to providing complex accounting advice to public sector organizations, Matt is currently supports clients in finance transformation initiatives and helping organizations elevate the profile and efficiency of their finance function.

Relevant Experience

Provincial Ministry of Finance Complex Accounting Support: 2015 - Current: Matt is Deloitte's lead senior manager on engagement to advise management on a large complex transaction on a Government Business Enterprise. This engagement required Deloitte to work with the client to understand the transaction being proposed and to provide guidance to relevant stakeholders on the accounting implications of the transaction. Deloitte worked with management and various professional advisors to inform decision makers about the implications of the proposed transaction and to help the client document their analysis and conclusions. Deloitte also assisted the client in presenting the client's analysis and views to the Auditor General. This engagement required extensive research across all parts of the CPA Canada Handbook (Not-for-Profit, Public Sector, Private Company, and Public Reporting Issuers) to support the conclusions reached by management.

Provincial Review of the Implementation of a New Accounting Standard (PS 3260) - 2015: Deloitte was engaged to advise the internal audit function within a Provincial government on the complexities of implementing a new accounting standard on contaminated sites. Matt was the lead senior manager on the engagement which involved helping internal audit provide recommendations to identified ministries and a central agency on how to deal with complex issues associated with implementing the accounting standard and providing support to various ministries on how to improve their internal controls and documentation around the implementation of the accounting standard. The engagement also involved assisting management and internal audit in developing a position paper on how to treat certain complex issues resulting from the implementation of PS 3260 that was used in discussions with the auditor general.

Provincial Government Business Enterprise Complex Accounting Support - 2013- Current: Matt is the lead senior manager on a Deloitte engagement to advise Provincial Government Business Enterprise on complex accounting issues resulting from new transactions, and challenges with adopting new accounting standards under IFRS around employee benefits, revenue, and leases. Deloitte supports this client by providing updates on changes in accounting standards and by working with the client to develop analysis on the impact of new standards and proposed transactions.

Community involvement

- Board Member and Finance Committee Member – 2015: The Meighen Health Centre
- Finance Committee Member – 2009 – 2015: The Change Foundation
- Board Member and Treasurer– 2003 – 2009: Intrada Brass

Education / Professional designations / Industry Conferences

- Bachelor of Business Administration, University of Toronto (2004)
- Chartered Professional Accountant, Chartered Accountant (2007)

Schedule C – Similar Projects and Working with Governments

Each Vendor should provide in its proposal:

- A description of the proponent's current or past experience with similar projects, with examples of successful outcomes, anticipated challenges, and corresponding mitigation strategies that the Vendor would employ.
- Provide a description of the proponent's experience and previous pension actuarial experience with the Ontario Government or other senior Canadian Governments and provide specific examples of how that experience would assist the proponent with the deliverables of this initiative.

Similar projects

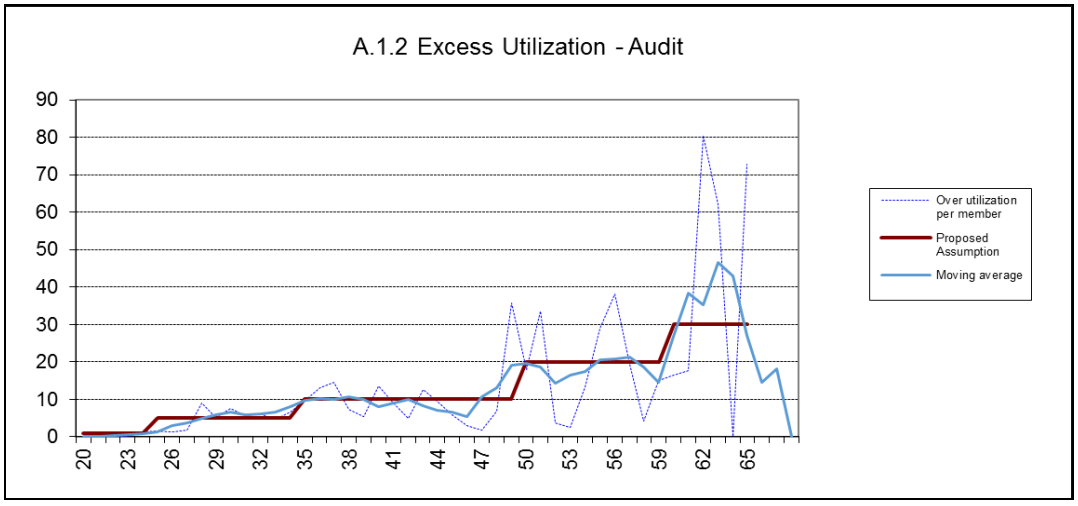
Number of similar projects were performed by Deloitte over recent years covered actuarial valuations for accounting purposes and also complex accounting issues. Some of these have already been described in the Schedule B of team members to show their expertise. Some examples are described below.

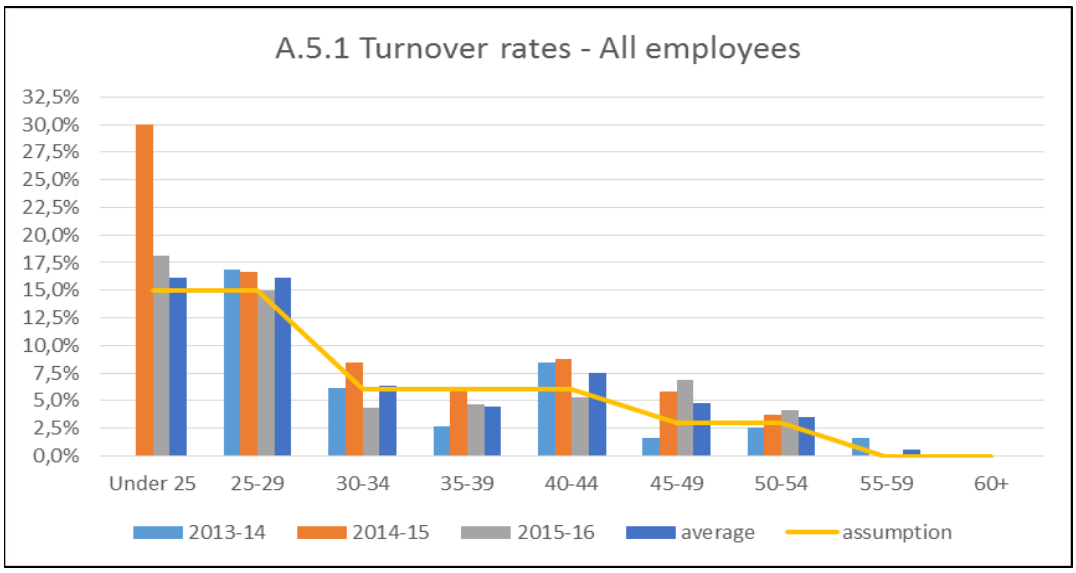
Under PSAS for one specific client, Martin and Deloitte provided various accounting advice over many years. Success was measured in that the client was satisfied and so was the Auditor General. Work was performed on accounting standards compliant basis and we did find practical approaches to prepare some elements of accounting calculation in an environment of multiple plans. Challenge was mostly around getting some harmonized approach to the multiple plans that were present (more than 40 at some point). Determining the main goals, identifying the material elements were crucial and helped mitigate the multiple plans situation. We were able to focus on the main ones that represented the biggest piece of the obligation. The other challenge was the level of knowledge of the various parties relating to accounting requirement. To overcome this, Martin was involved in number of training sessions to really provide a solid basis for the different key persons that would be involved. Throughout the years of engagement, Martin also used his communication skills and illustrative approach to help the client and the Auditor General to get familiar with the pension accounting and get a comprehensive understanding of the calculations performed. On every occasion, he found a way to increase the appreciation of the actuarial concepts / accounting standards and the required work. Complex elements that came up and needed to be explained and dealt with included; asset ceiling calculation and its non-intuitive effect, market-related value of asset methodology, discount rate for non funded plans, use of the available information to determine how to make some available results accounting compliant (time and cost savings).

Under IFRS, for 3 main clients of Deloitte, we did have asset ceiling consideration this year due mainly to the plans being closed to new entrants. Asset ceiling is a very complex application under IFRS that encompass minimum funding requirement calculations and determination of economic future benefits. Letters of credit could also be used to avoid minimum funding requirement effect. So a large number of pieces come into play in the calculations performed. Success of our work was measured by raising issues around the asset presented on the balance sheet, making the clients aware of the complexity of this and getting them understanding our approach and therefore limits on balance sheet asset. The main challenge we had was to get the actuaries to view the arguments we had on this issue and have them agree at least to some extent to our views. In order to overcome this challenge, we held some calls with the actuarial firm and we did have the client also listening to these calls, and provide their inputs. Having all interested parties included in the discussion proved to be a good way to mitigate that and avoid simple back and forth emails from actuary to actuary. We also did validate some of our position elements with other colleagues in various firms (actuarial and accounting) to understand the practice for some components of asset ceiling and get a broader view of the flexibility that exists and boundaries applied.

One other main success we can mention is how we work in the audit mandates either with our own Deloitte auditors, the firm clients or with Auditor Generals. Being specialists of pension, actuarial calculations and accounting standards, we do provide significant value to auditors and clients. We even get great comments from actuarial firms that we work with, even if we can be seen at some point as counterparties to them. The success we think can be measured in different ways. The main things we can mention are: we understand the benefits offered, we know how they are calculated from an accounting actuarial valuation perspective and we know how accounting results are determined. We work efficiently in identifying the main issues, getting the appropriate questions out and preparing a documentation that will answer the objectives that are set out. When an event occurs that need special accounting treatments (past service costs, curtailments, settlement, annuity purchase, asset ceiling calculation,…) we know what information is important and what is needed to support a file. As such, we find that success comes with a complete documentation, an effective approach, avoid unnecessary questions to clients / actuaries. We sometimes have challenge in dealing with actuaries as they may see us as competing with them to find an actuarial / accounting answer. Also, by reviewing calculations that they perform we may be seen as the ones that are looking for their errors. In order to mitigate this kind of feeling and ensure orderly communications with the actuaries, we do adopt an approach of collaboration. We always make the communications with actuaries very professional and in good faith on both sides. We keep our mind opened to evolving approaches but maintaining adequate actuarial practice and the accounting results being compliant with the standards. We also discuss openly on adhoc basis with accounting specialists in all major actuarial firms to exchange views and keep transparent on new issues and evolving practices. So far, the communication has been great for most cases even when significant issues have come up.

From a specific valuation perspective, we have helped 2 clients in recent years to perform actuarial accounting valuation of sick leave benefits and document adequately the valuation and results. The success was measured on different basis. Ultimately, the client received its required information on a timely basis. The client was also able to ask a large number of questions and get the appropriate answers in an understandable language. Finally, the client had a solid basis and high confidence to face the questions coming from their auditors on the various areas such as data review, assumption selection, valuation process, actuarial results, accounting calculations and finally the reporting in the financial statements. One of the main challenge we faced was getting the necessary support for assumption selection. The client wanted to be comfortable with its selection of assumptions but also be able to explain for both internal / external stakeholders how these were derived. Understanding that assumption selection is one key area that auditors look for and to mitigate this risk, we recommended providing a better structure for their assumption support documents, especially for sick leave utilization and turnover rates that are supported by plan specific experience. It resulted in a more efficient approach that was time and cost saving. We have provided visual support in order to help all the parties understand the behavior from an historical point of view and the assumption setting process. We also performed back testing of the assumption to show that assumption was reasonable with the experience of the plan. You will find below 2 examples of the supporting graphs that were used in the documentation.





Working with Governments

We have been working with governments both on very specific pension issues but also on many other occasions for non pension elements. Deloitte being a provider of a vast array of professional services, we do have a number of initiatives that were specifically performed with Ontario.

From a pension specific perspective, we have been involved highly with the Québec municipal Ministry to apply the PS3250 and PS3255 accounting standards to municipalities since 1997 when it was first adopted. In Québec, contrary to other major provinces in Canada, the pension plans are direct responsibility of the municipalities (local Governments). There is no multiemployer plan like OMERS or BC Municipal. As such, there are a large number of plans following PS3250 and PS3255 and some cover a large number of members. In applying the standards, a number of issues came up and needed the Ministry to look at the effect on municipalities but also define some guidelines to apply the standards. Martin and Deloitte have been involved since 1997 with the Ministry to discuss numerous issues and help the Ministry to provide recommendations on complex actuarial and accounting elements. We can note the following:

- Identify key accounting provisions that apply to pension plans
- Review the impact on the municipalities financial statements of transition
- Identify some relief options to manage taxation level for number of accounting events
- Discuss the impact of the 2008 crisis on municipalities and identify the options / treatments to offer some tax management relief to the municipalities
- Look more recently at the major changes in pension legislation that affected municipalities and identify the appropriate accounting treatment
- Asset ceiling, market-related value of assets, discount rate selection, mortality changes, presentation in financial statements …

In this implication with the Quebec Ministry, we did get exposure to a very large number of issues in accounting actuarial valuations and we did have to provide support from the very specific accounting literature (key paragraphs). Since this was applied to very large public employers, it also had a significant impact on the practice in general and how actuaries were calculating results under PSAS. We believe that this involvement makes us very well positioned to support the OPCD on complex actuarial and accounting issues that will come up. The large number of plans for Québec municipalities do provide us with a large exposure to situations that have come up and prepares us to the needs that OPCD will have.

In another work with the Québec government, Deloitte has been providing support to compare the accounting practice in Canada of various governments on how they select the discount rate and what valuation methodology they used. A review of the valuation results presented in the notes or annual report of the main plans was also looked at. In performing this work, we did have to prepare reporting in specific format that could be used by interested parties at government level. As such, we needed to be sure the explanation was appropriate, to the point and accessible to a non-familiar reader. We believe that this experience, above the fact that it provided us a good view of the Canadian public sector plans in Canada, will also help us define the appropriate communication needs and format that OPCD will be able to use.

We also did work with the NB Government on the preparation of a white paper on Shared Risk Plan accounting. This new type of plan is highly complex and also is not totally contemplated by the PS3250 that is more based on traditional plan structures (either DB or DC). Plans with conditional benefits are more addressed under IFRS, although there is also some grey area in this standard. We did provide support to the Government to define an approach to value and account for these plans. In doing this we needed to educate some people on accounting, we needed to understand the steps of the actuarial valuation process and we needed again to report on a complex issue to non-familiar individuals. We think that this is something that will be helpful to support the OPCD in the upcoming challenges of complex accounting issues.

Deloitte has been involved with a number of large municipal Auditor Generals in particular in Québec where large municipalities do have audit firm working on the financial statements but also Auditor General looking at the work. We have been either supporting the Auditor General review (as a support expert to the AG) or in communication with the Auditor General (as the auditor of the municipalities) for most of the large municipalities:

- City of Montréal and Transport Commission
- City of Laval
- City of Longueuil
- City of Gatineau
- City of Terrebonne

Through these mandates, we have performed work in all areas included in accounting valuation and reporting; methodologies, assumptions, gains and losses, expense and balance sheet, asset ceiling, disclosures, detailed calculations, sensitivity testing. We also provided advice throughout these mandates to ensure the Auditor General would improve the understanding and also become aware of good practices for documentation as well as tests to perform. This provided some knowledge transfer opportunity for Deloitte to make our contacts better professionals in an area they are usually less familiar.

We also provided similar support to the OAG (Canada) in their review of a number of Crown corporations. In all our mandates, we did get good feedback from our OAG contacts, some of which are included in our references. We did also ensure that formal communication would be through an external report that has a structure to facilitate the review of conclusions and the reading of the document. We reached our objective since all our contacts did confirm that they were impressed with our documentation process and the working papers we provided.

In addition, Martin and Trevor have the experience working with the OPCD in regards to pension accounting advice. In a recent mandate, they have been involved in providing advice and guidance to OPCD on complex accounting and reporting matters related to accounting for pensions and the Province's consolidated financial statements. More specifically, they provided expertise in actuarial assessment in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250. In that work, both the accounting expertise, knowledge of the tests and the actuarial calculation requirements were involved to support OPCD understand the work performed by an actuary with that regards. They were also involved in looking at models used to project expense and balance sheet figures over future years using different scenarios. We understand that different views could be applied to asset ceiling test and this will be part of the initial steps to be defined and a crucial input to any projection of results. Still, this experience of having already worked with your team gives us the confidence that we will be able to coordinate our efforts, both Deloitte and OPCD, to deliver you the optimal results you will be expecting and support you in the calculations and assumption requirements.

Schedule D – Reports for Public Pension Related Initiative

Each Vendor should provide in its proposal:

- Describe the proponent's demonstrated knowledge, skills, experience and expertise with developing reports with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative of a public pension related initiative and any recommendation made as part of the report.

Audit report to our auditors and Auditor Generals

As indicated in a previous section, our pension actuarial group performs more than 150 pension and non-pension benefits audit supports annually, among which 15 to 20 relate to public pension. These are used for Deloitte audits but also for supporting Auditor Generals. In performing our work, we do prepare formal reports and working papers. These documents need to be orderly prepared and contain the necessary requirements to support the audit. The usual documentation includes:

- background section
- tailored executive summary portion
- section detailing our approach
- section with the findings for each of our tests (methodologies, assumptions, events, expense, asset ceiling, …)
- section with the list of professionals that were involved
- finally, a list of detailed working papers is also included

We prepare the structure of our reporting in order to maximize the understanding of the work performed and the findings. We have found by use with auditors and Auditor Generals that this answers the need for documentation. We specifically received great feedbacks from working with external stakeholders on how the information communicated was complete, to the point and easily accessible. We believe that we have shown expertise in preparing these documents over the last few years and we will use this to ensure optimal communication with OPCD and the stakeholders. Our reporting to auditors led to their file being complete but also in some cases has impacted the audited entity process / reporting for which adjustments were made.

Government analysis of accounting approach

We did perform a pension review of the major public pension plans in Canada for the Quebec government. This document was meant to cover main plan provisions, main assumptions used, accounting results and methodologies. We did perform the analysis, summarized the information received and prepare the necessary report. Reporting to a Government, we did structure our report again to have a succinct but complete executive summary. The document needed to cover all steps of the work and really tie to the objectives that were set out initially. We did work this in a collaborative approach with the Government representatives and therefore ended doing some back and forth iterations to incorporate both our views of what made it a successful document that would answer the stated objectives but also include the Government views about what wording might be more appropriate to some stakeholders. We still had the ultimate responsibility to define the structure based on the work we were performing and findings in the course of the mandate. We also think that this shows our experience in this type of communication and will help us ensure high-quality work to OPCD. Although we did not end up with specific recommendation, the content and our analysis of the information was aiming to support the position taken by the Government on some of its accounting decisions compared to other governments.

Shared risk plan white paper

Another example of reporting on public pension plan is the work we did with the Government of NB to define the accounting treatment for transition of a traditional DB plan to a Shared Risk Plan model. This work required us to really cover a highly complex accounting issue but also having legislative and actuarial complexities. We performed the analysis of the legislation and the accounting and prepared a report with our findings. An executive summary was needed to ensure the conclusion of our analysis was highlighted appropriately and the main elements leading to it were also summarized. As this is a complex issue, numerous subsections covering the plan details, the legislation considerations, the valuation reports, the funding and benefit policy, and the accounting standards were also included in the reporting. This work shows that we do have the expertise to translate complex issues into accessible documentation and provide with a summary that adequately covers the issue, the process and our conclusions. Our work led to a recommendation on the adequate treatment of this particular type of plan in order to support the financial statement preparation.

Schedule E – Ceiling Test and Sensitivity Analysis Scenarios

Each Vendor should provide in its proposal:

- Describe the proponent's demonstrated knowledge, skills, experience and expertise with running different asset ceiling tests and sensitivity analysis scenarios. Cite examples to demonstrate experience and describe results achieved.

Quebec municipalities Ministry for application of PS3250 and PS3255 standards

Through the implication with the Québec municipalities Ministry Deloitte has provided a number of recommendations on accounting treatment of some events / issues that are closely looked at by the Auditor Generals. We have been involved in the treatment of special events including the asset ceiling and its accounting treatment. PS3250 has extreme volatility consequence for asset ceiling while IAS19 has some self-correcting mechanisms that help alleviate this extreme fluctuation. At some point, this element did become a sensitive issue for some municipalities' pension plans and affected their financial statements and taxation needs. We were involved with the Ministry to define a possible recommendation of how this would be applied and eventually determine some recommendation to mitigate the taxation impact for municipalities. Our expertise in PS3250 combined with our knowledge of IFRS for asset ceiling proved to support the Ministry. We did projection of plan situations and tested asset ceiling under numerous scenarios to search for an adequate solution to the situation and taxation issues.

Comprehensive review of the ceiling test under PS3250

In preparation of the Province of Ontario's Financial Statements, Deloitte was engaged by the OPC to provide support in analyzing issues around pension accounting. A key element of the work prepared was the assessment of the application of the public sector accounting standards as related to asset ceiling and valuation allowance. Our work included review of two large Ontario plans for which we prepared a document containing the following details for each:

- Summary of the accounting situation
- Overview of the accounting paragraphs that apply to this and the explanation
- Review of the considerations that go into the ceiling test and the Future Economic Benefit (FEB) calculation
- Review of the employer access to future contribution reduction or surplus withdrawal
- Summary of findings relating to observations made in discussing the applicability of the asset ceiling test for Ontario's 2015-16 Financial statements

One section above the rest from the document we prepared for the OPCD highlights our expertise with running different ceiling tests and scenario testing. Within our review of the consideration that go into the ceiling test and the Future Economic Benefits (FEB) calculation, we highlighted the main components of a ceiling test including notion of an open group, future service accruals on an accounting and funding basis, required contributions and contribution holiday. Further, we defined different levels of testing in regards to the minimum contribution that we ran through testing and projection. This allowed us to work through different examples with OPCD, going from a basic testing to a very comprehensive level of testing under PS3250.

This experience has allowed Deloitte and the OPCD to better understand the asset ceiling notion and the concepts that go into it. We recognize that a significant number of assumptions and inputs go into this type of work and that different views may lead to different results. These may be part of the scenarios to look at in the accounting calculations. This is why we believe that any work on asset ceiling will need to start by defining a solid basis on these assumptions and scenarios.

Asset ceiling and annual audits

As indicated previously, our pension actuarial team supports Deloitte audit teams on a large number of annual audits. Although not always applicable, there are number of plans that show an asset position and for which testing of the amount presented needs to be performed. Even more complex, the test under IFRS, including IFRIC14 requires usually some projection of results to validate the asset position, even for plans that might currently be in liability position. So our team does have extensive experience in these issues, calculations and discussions with clients / actuaries. We are exposed to a significant number of these situations. As an illustration, you can refer to the section on similar projects where we noted that under IFRS, for 3 main clients of Deloitte, we did have asset ceiling consideration this year due mainly to the plans being closed to new entrants and for which we did go through a comprehensive process with the clients and actuaries. Plan closing and reduction in active membership are an illustration of important considerations in asset ceiling tests but we can think of many other elements that are of importance in the detailed calculations of asset ceiling. Deloitte being involved on a large volume of clients, we believe that we are well-positioned to be faced with all of these particular situations that may come up and as such be able to support OPCD in understanding the effect of "what if" situations.

Sensitivity and Scenario Analysis for Audit

As actuaries in a large Audit firm, we act as the pension specialists for many pension and benefit plans. Each of these engagements has a defined scope but typically it involves the review of actuarial assumptions and review of the accounting results to gain comfort with the movements of the obligation, plan assets, profit and loss, and other comprehensive income where applicable. To completely gain comfort, reviewing both assumptions and results, we must use both sensitivity and scenario testing.

When reviewing actuarial assumptions, particular assumptions may depend on stochastic projections. For example:

- For plans under all standards, if there is an element of increase of pensions in payment that is linked to the Consumer Price Index (CPI) or the return on assets, we will perform stochastic projection. For illustration, if a plan assumed an annual increase of pension in payment of 1.2%, and the plan formula for the increase was the maximum of a) 50% of CPI and b) 75% CPI minus 1%, we would perform a stochastic projection of inflation levels over future years to determine the likely distribution for what the underlying indexation would be. Finally we would compare our expectation with the assumption retained. Doing so will require some modelling for projection of future events like CPI.

- For plans under PSAS, there is use of the expected return on assets assumption. When there is an expected return on assets assumption, we would look at the plans target investment strategy (the distribution of total assets into asset classes), and then we would perform a stochastic projection of these asset classes over a defined period to determine the likely distribution for what we would expect the aggregate return to be. This would be compared with the assumption retained. So again, we do use modelling into our regular work.

Sensitivity analysis is a particularly useful tool for completing our review of accounting schedules. For example:

- For reconciliation of the benefit obligation to explain how it evolves every year, there are 3 main elements of gain/loss; change in financial assumptions, change in demographic assumptions, and plan experience. When there is a change in the assumptions, this will result in some element of gain/loss whether it's very minimal or large. In order for the Deloitte team to determine the impact of changes in assumptions, we often rely on sensitivity testing. A common example is determining the impact of a 100 bps decrease in the discount rate. We would use the plan duration, which is the sensitivity of the

cash-flows, and determine the percentage increase in pension benefit obligation from a 100 bps decrease in the discount rate.

Other assumption changes may also incorporate sensitivity analysis; change in retirement assumption may rely more on active member duration, change in the indexation for deferred members may rely more on deferred member cash-flow sensitivity, change in the mortality assumption may rely on the complete cash-flows sensitivity to all members living an extra year. We will make use of the actuarial knowledge we have about how an obligation for a member is valued. We also have available valuation tools that help us estimate the impact of very specific assumption changes. Our proposed team members have been involved in actuarial valuation preparation and actuarial results review hence they are very familiar with the elements that go into the calculations.

Finally, for sensitivity, we can also mention that our team often supports the disclosure for sensitivity results. When entities present such information in their notes, often seen under IFRS where disclosure of significant assumptions must come with a sensitivity analysis of these assumptions. The actuarial team will support the auditors in assessing whether a change in obligation value disclosed is acceptable based on the actuarial principles and calculations. Our actuarial group would prepare a similar analysis to validate the actuary results.

In a similar manner, we provide support to audit teams at the start of their audit process when they identify what are the major risks to be reviewed and covered. To do this, our team will prepare sensitivity analysis of the main plan assumptions to calculate the impact on the obligation and help the audit team determine if this change is material for the audit work and therefore represents a major risk. To do this, we need to understand the main plan provisions and define the impact of the assumption change in the actuarial valuation calculation.

Schedule F – Methodology and Implementation Plan

Each Vendor should provide in its proposal:

- The proponent shall describe the methodology and implementation plan they will use to deliver the Client's Requirements as described in Section 1.5 of this RFS.

From Section 1.5 of the RFS

- Working with management of the Office of the Provincial Controller's Accounting Policy and Financial Reporting Branch (APFRB), the provider will provide actuarial/accounting services related to the following possible areas:
  - Review the economic assumptions (i.e. management best estimates) used for the accounting valuations of the pension plans and non-pension benefits reported by the Province.
  - Review the actual and forecast numbers prepared by APFR staffs for the Province's various pension and non-pension benefits. Including assessing the reasonableness and completeness of assumptions used by APFRB staff in the models, including any sensitivity analysis as required.
  - Provide recommendations, if any, on improvements in the pension and non-pension benefits accounting models currently used to by APFRB.
  - Perform ceiling test requirements in accordance with PS3250.50 to PS3250.59 for all sole sponsor or joint sponsor pension plans that are in an accrued benefit asset position.
  - Provide advice on any accounting issues related to pension and non-pension benefits, as required.
  - Participate in discussions with internal and external stakeholders, as required.

- The Vendor will participate in meetings as necessary to support the engagement objectives.

Implementation Plan – start of mandate

In order to start the mandate on a solid basis, we believe that a first initial meeting between Deloitte and OPCD would be the best first step. Martin and Trevor will cover a number of elements to ensure that the mandate starts on the right track and uses most optimal approach.

With this initial meeting, many elements of process and basic information will be covered like:

- Identify the key personnel on both sides and define their expected role
- Review the list of pension and non-pension benefit plans that are to be covered
- Identify the documents that are to be made available (valuation reports, plan texts, internal procedures, financial statement notes, assumption selection documents, data)
- Determine the assumption selection process already in place
- Determine the valuation process used and discuss the main models in place for APFR staffs work and

the projection / sensitivity scenarios

- Identify the list of issues that are currently foreseen
- Agree to the communication procedures for information
- Discuss expected timing of the support needed by OPCD over the period covered by the mandate
- Billing procedures also will be defined

The objective of this meeting will be to cover the important elements and allow for both sides to define their needs / expectations.

Although the scope of work description under 1.5 of the RFS does not clearly identify tangible deliverables or definite milestones and delivery dates, we have identified below how we would proceed to get some of the main activities to a conclusion. These activities are identified as follows:

- Review economic assumptions (management best estimate) under PSAS
- Review actual and forecast numbers prepared by the APFR staffs, including sensitivity analysis
- Work with OPCD on discussions with internal / external stakeholders
- Perform ceiling test requirements

Review economic assumptions (management best estimate) under PSAS

This activity covers a very important step in performing accounting actuarial valuation. This is an area where our expertise comes into play and where we can provide a good support to management in its process. This will usually follow a review of the management actual position on the assumptions and provide documentation to support / comment the assumptions and provide possible adjustments where applicable.

Step	Description
Initial discussion with the OPCD	Identify the process for selection of assumption used Determine outside resources being used to make selection Identify the basis and rationale for each key assumption selected Determine the objective of our review and confirm the documentation expected
Obtain the necessary documents	Detail of assumptions selected Rationale behind the selection, process and supporting information Explanation for changes made in methodologies over year, if applicable
Review of assumptions	Review plan provisions that may have an impact on the key assumptions selected Compare with assumptions in funding valuation (especially demographic ones) Identify inputs used for any assumption, including expected return on plan assets (which is a key assumption and more subjective inputs being challenged usually) Review market information available and surveys Review assumption models (ex when stochastic methodology used)
Prepare the preliminary analysis document	Summary of the assumptions and the process Identification of documents received and used in review Comments on every assumption scoped in our work Identification of any assumption that may be of concern
Discuss the analysis with OPCD	Send the preliminary analysis document to OPCD Run through the main elements of the analysis performed and the conclusion Discuss further if any assumptions need deeper analysis or support
Prepare formal communication	Document to be used with internal / external stakeholders

Although the deliverable may differ somewhat in format based on the needs, it will contain these most likely elements:

- Summary of the assumptions
- Identification of the documents used and prepared
- Summary of the conclusion reached

Review actual and forecast numbers prepared by APFR staffs

This activity covers our accounting expertise for actuarial calculations in an accounting environment. It also makes use of our experience in dealing with design and use of valuation models and projection of results through deterministic or stochastic scenarios.

Step	Description
Initial discussion with the OPCD	Identify the valuation process in place and the models used Determine the projection assumptions used in forecasting results Define the access to the models / excel spreadsheets for our work Determine the data being used Determine the sensitivity applied to some of the assumptions Identify the scenarios (assumptions and others) that are expected to be prepared Determine the document / outcome expected from our work
Review the APFR staffs results prepared	Review the calculations and projections Reperform accounting results for expense and balance sheet Identify any difference and determine the rationale for difference Review any stochastic input / output being used Perform the work on the various scenarios
Identify questions	Define queries that may come up in our review Identify weaknesses of the process and possible improvements Raise questions to OPCD Review answers and adjust as needed the work (support APFR staffs as needed)
Prepare analysis document for OPCD	Identify information received Describe work performed and steps taken List the issues / questions raised and adjustments if any Comment on the appropriateness of the results
Discuss document prepared	Review with OPCD Go over the conclusion of our review of the results Identify elements that may need to be improved in the valuation process or future scenarios to include in future years

Although the deliverable may differ somewhat in format based on the needs, we will ensure that the content will be prepared considering the following

- The identification of the valuation process and forecast modelling
- The scenarios being looked at (sensitivity)
- The extent of our findings and how they are to be addressed
- The specific needs of OPCD if changes are required to be supported by comprehensive documentation or regular communications with OPCD and APFR staffs

Work with OPCD on discussion with internal / external stakeholders

This activity is about discussion. As such, it will make use of our expertise in delivering comprehensive, understandable information and explanation for actuarial and accounting elements or concepts. This is one area where the multiple files we work on with auditors, actuaries and entity management will provide the needed skills to deliver quality services. Below we provide some summary of steps that we would take to engage in these discussions.

Step	Description
Initial discussion with the OPCD	Identify the issue / concept that is to be discussed Identify the main message that is to be delivered and elements to cover Identify the key people (stakeholders) that we will be having discussion Define the level of understanding of the people and whether some basic information needs to be provided Defined the supporting documentation or agenda needed Identify where Deloitte and OPCD get involved respectively in the discussion
Obtain documents	If the discussion is to be focused on some specific documentation, it needs to be obtained
Have the discussion	Go over the elements that need to be covered Maintain the discussion at appropriate level of understanding Explain some concepts that may not be familiar to the stakeholders Ensure that discussion is held at professional level, never lose sight of the objective and the spirit of collaboration Identify if any next step is required after the discussion (document, analysis, meeting …)
Deloitte and OPCD review the outcome of the discussion	Identify how the discussion went Determine the next steps, as applicable (who, what, when)

Even if these discussions may be with different stakeholders and cover various issues, some common features of our approach to these discussions will be:

- Make sure we all agree on the elements to discuss and the needed documentation
- Ensure that discussions are at the appropriate understanding level for the stakeholders
- Always make those in collaborative and professional manner
- Understand what role Deloitte plays and OPCD plays to avoid misunderstanding of responsibilities
- Identify any next steps required

Perform ceiling test requirements

This activity covers a very specific area of the pension accounting standards. It is an element that needs some judgment and also that needs a comprehensive analysis to document appropriately the position taken. Under PSAS, the asset ceiling test is required when the plan presents a surplus and shows an asset on the balance sheet. This is done on a plan by plan basis. It does encompass a notion of future economic benefit (FEB) that requires the Government to define what it believes can represent a benefit in form of either surplus withdrawal or future reduction in the Government contribution through contribution holiday. The asset ceiling is important since as per the accounting standards, any change of the ceiling over year will have an immediate impact on the annual expense of the Government and thus may be a very volatile component when the asset ceiling applies. Here are the steps we think could be taken to provide expertise to the specific situation of the Government.

Step	Description
Initial discussion with the OPC	Identify the plans that are to be modelled Determine the various components of the test and how it is to be applicable Discuss for the affected plans the initial view on whether the Government could take some contribution holiday, if so on what circumstances Identify if one approach applies to all plans or if different situations exist (ex a closed plan)
Obtain the necessary documents	Accounting results for the affected plans Supporting plan text/funding policy for contribution holiday judgment Initial analysis that exists at OPCD
Prepare an analysis of the situation for the plans	Define and structure the valuation model Prepare the assumptions that will be included in the model Based on the elements defined above, determine the FEB components for the affected plans
Perform valuation models	Determine possible contribution holidays FEB calculation basis Impact of the asset ceiling
Discuss the valuation models with OPCD	Send the valuation models documents to OPCD Run through the main elements of the analysis performed and the conclusion
Prepare formal communication	Depending on the needs, could take the form of a revised analysis or more formal document to be used with Auditor General or other external stakeholders

Some key elements are really important to look at when preparing this analysis:

- Valuation basis used for plan assets (market-related value?)
- Possibility of Contribution holiday – what supports this and what are the constraints
- Well-defined process to calculate this since it is a very complex element of accounting that not all stakeholders fully understand and can appreciate the accounting requirements
- Actuarial assumptions to include in projection

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Public Sector Pension and Non-Pension Benefit - Management Consulting Services

Pricing proposal to serve the Ontario Government

Pricing proposal
Reference: RFS TBS-OTB-OPCD-22

Closing date: Friday, November 3, 2017

Proponent and contact information

Deloitte LLP
1190, avenue des Canadiens-de-Montréal
Montréal, Québec H3B 0M7
Canada

Contact: Martin Raymond
Email: maraymond@deloitte.ca
Tel: (514) 393-7367

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- **understand** your business and what is important to you
- **provide** value and build trust through technical competence and consistent results
- **demonstrate** professionalism through effective interaction and communications
- provide a **no surprises** experience

Deloitte LLP
1190, avenue des Canadiens-de-
Montréal, QC H3B 0M7
Canada
Tel: (514) 393-7367
www.deloitte.ca

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November 3, 2017

Private and confidential

Email delivery

Attention of Mark Donaldson
Director, Treasury Board Secretariat
Office of the Provincial Controller Division

Re: Actuarial Services – RFS TBS-OTB-OPCD-22 (Pricing proposal)

Deloitte is pleased to submit this pricing proposal to provide actuarial services to the Office of the Provincial Controller Division (the "OPCD") about pension and non-pension benefit management consulting services. As you will see from our proposal, professionals at Deloitte possess relevant experience and have conducted similar engagements for a variety of clients, including public sector. Should we be the successful bidder, we are also able to draw upon an experienced team who not only understands actuarial services, but also appreciates the challenges and complexities associated with the communication issues of actuarial results and accounting complexities. Deloitte being highly involved in pension and non-pension benefit plans audit, the OPCD will have access to individuals that have significant expertise in understanding the market practice on accounting for these benefits and have specialized views on interpretation of accounting standards.

If you have any questions with respect to the information contained within this proposal, please do not hesitate to contact us. We look forward to working with the OPCD on this important initiative.

Sincerely,

Martin Raymond
Partner

Deloitte LLP

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Pricing considerations

Extract from the RFS

- Pricing Schedule (Schedule A) completed and submitted as a separate file.
- If HST is applicable, Vendors must itemize HST as a separate line item in the Pricing Schedule
- Vendors must propose all dollar amounts in Canadian funds
- The Pricing Schedule must set out the full legal name of the Vendor; a list of each Role (including Experience Level) proposed; and the full legal name of each consultant proposed for each Role (by experience level) to achieve completion of the proposed services within the timeframe specified by the Client; and total Fixed Price that the Vendor will charge the Client for Services performed and Deliverables provided
- The amount for Total Fixed Price is fixed and not subject to change unless otherwise agreed to by both the Client and the Vendor in a Change Order
- If required by the Client, the Vendor must also include a list of each Role (including experience level) proposed; and the hourly rate for each Role, to be applicable only in the case of a Change Order

Notes

- The role / experience is provided in general terms. More details are found under the Schedule B of the Technical proposal

Schedule A - Pricing Schedule

Please provide the following information in accordance with Sections 2.2.1 and 2.2.2 of this Request for Services:

Legal Name of Vendor:
Deloitte LLP

Part A – Vendor Personnel

Complete the following table in respect of all proposed Vendor Personnel that will perform the Services and/or provide the Deliverables. Vendors should not include proposed Subcontractors in this Part A of Schedule A.

List the names of Consultants who will be assigned to the Project	**Role and Experience Level**
Martin Raymond	Project Lead (Partner at Deloitte): over 20 years of experience
Trevor Gary	Senior Analyst (Senior at Deloitte) : 4 years of experience
Matt Colley	Subject Matter Expert (Senior Manager at Deloitte) : 12 years of experience

Will Subcontractors be used for this Project? Yes [ ] No [x] If "Yes", complete Part B.

Part B – Vendor Subcontractors

Complete the following table in respect of the proposed Vendor Subcontractors at any tier of subcontracting, including any Vendor contractors that will perform the Services and/or provide the Deliverables.

Legal Name of Subcontractor	List the names of Consultants who will be assigned to the Project	Role and Experience Level
N/A	N/A	N/A
N/A	N/A	N/A

Part C – Fixed Price

In the following table, enter the Fixed Price in respect of each role to be performed and the particular Deliverables to be provided, which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

For the purposes of bidding, the Ministry has estimated that 75 hours of effort is required for each role totalling 150 hours over the term of the Agreement. The Ministry reserves the right, as required, to alter the number of working days for each role as the project unfolds. The Ministry reserves the right to alter the number of working days at the time of award.

Fixed Price for each Core Deliverable	Amount
• One (1) Senior Consultant / Project Lead shall provide 75 hours of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements. – Martin Raymond	$ 33,750
• One (1) Intermediate Consultant / Sr. Analyst shall provide 75 hours of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements. – Trevor Gary	$ 18,750
Total Fixed Price:	$ 52,500

Part D – Other Expenses

In the following table, Vendors should list all expenses applicable to the Project that have not been included in the Total Fixed Price amount as stated in Part C of this Schedule A. Vendors should review the Travel, Meal and Accommodation Expenses section of the RFS prior to completing this table.

Expenses by Type *(List each item below):*	Proposed Amount
N/A	$ -
N/A	$ -

Part D – Other Expenses

In the following table, Vendors should list all expenses applicable to the Project that have not been included in the Total Fixed Price amount as stated in Part C of this Schedule A. Vendors should review the Travel, Meal and Accommodation Expenses section of the RFS prior to completing this table.

Expenses by Type *(List each item below):*	**Proposed Amount**
Total Other Expenses:	$ Nil

Part E – Maximum Price

In the following table, Vendors shall calculate Subtotal Price by adding Total Fixed Price, as stated in Part C of this Schedule A, to Total Other Expenses, as stated in Part D of this Schedule A.

Vendors shall calculate Maximum Price by adding the Subtotal Price to the applicable HST.

Subtotal Price (Part C + Part D):	$ 52,500
HST (if applicable):	$ 6,825
Maximum Price (Subtotal Price + HST):	**$ 59,325**

Part F – Follow-on Work Hourly Rates

In the following table, enter the Hourly Rates in respect of each particular Role to be performed which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

In the event that Follow-on work is requested, the Ministry will prepare a contract amendment to engage the consultant(s) for a specified number of days of work. Details on deliverables will be disclosed in the amendment as well.

Fixed Price for each Core Deliverable	**Hourly Amount**
• One (1) Senior Consultant / Project Lead Partner (Martin Raymond)	$ 450
• One (1) Intermediate Consultant / Senior Analyst Senior (Trevor)	$ 250
• Other possible consultants Senior Manager (Matt Colley)	$ 375

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FW_ Public Accounts Technical Briefing 201617_Sept 5_Draft_v6_speaking notes_cv edits.pptx.rtf

From: Hosick, Sarah (TBS) []
To: Uros Karadzic [uros.karadzic@ca.ey.com]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: FW: Public Accounts Technical Briefing 201617_Sept 5_Draft_v6_speaking notes_cv edits.pptx
Date: Wednesday, September 06, 2017 15:30:43
Attachment 1: Public Accounts Technical Briefing 201617_Sept 5_Draft_v7_speaking notes....pptx
Attachment 2: Pension Panel Slides _2016-17 PA Tech Briefing_Sept 6 1030_v1.pptx

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Hi Uros,

I've attached the decks for the 3:30pm meeting. Please keep confidential and do not distribute as the Public Accounts results have not been released yet.

Password to follow.

Thanks

Sarah

Sarah Hosick

Executive Assistant & Special Policy Advisor (A)

Assistant Deputy Minister's Office | Office of the Provincial Controller

Office of the Treasury Board | Treasury Board Secretariat

7 Queen's Park Cres E, 2nd Floor, Toronto, ON, M7A 1Y7

416-212-8512

Public Accounts Technical Briefing 201617_Sept 5_Draft_v7_speaking notes....pdf

t Public Accounts Technical Briefing 201617_Sept 5_Draft_v7_speaking notes....pptx (375296 Bytes) cannot be converted to P

Pension Panel Slides _2016-17 PA Tech Briefing_Sept 6 1030_v1.pdf

Pension Asset Expert Advisory Panel

Technical Briefing

September 7, 2017

Pension Asset Expert Advisory Panel -- Process

- Panel was provided with briefings and documents (relevant legislation, plan texts, sponsor agreements) to assist members to fully understand the facts and circumstances of the Plans and the basis for the government's accounting conclusions.

- Panel met with the Auditor General and members of her team to fully understand the basis for the OAG's accounting conclusions.

- Panel performed its own independent analysis of those documents and the legal, actuarial and accounting issues and reached its own conclusions.

- Panel considered:
  - guidance in PSAS specifically on Retirement Benefits
  - other relevant guidance in PSAS, and that issued by other standard setters identified in PSAS as sources to consult, in areas where the retirement benefits standard is not clear

Panel's Position on Recognition of Asset

- Net pension asset meets the definition of an economic resource because:
  - accounting surplus exists, and
  - future economic benefit is available to government as contribution reductions, freeing cash for other purposes.

- Unilateral control not necessary for asset recognition:
  - in fact, cannot exist in JDBPs or any other jointly controlled arrangement
  - sponsors jointly control the total net pension asset and must agree on how it will be used
  - key notion with joint control is that each sponsor can deny the other sponsor(s) access to the asset, ensuring no one side can make unilateral decisions
  - each sponsor should then recognize an asset relating to its portion of that jointly controlled surplus.

Panel's Position on Measurement of Asset

- Retirement benefits standard states that a sponsor measures the benefit of a surplus by the extent to which it can either take assets out of plan or reduce future contributions

- Contribution reductions are not the same as surplus withdrawal:
  - legal requirements for surplus withdrawal and contribution reductions are very different
  - joint sponsors free to decide on level of contributions in compliance with terms of Plan and Pension Benefits Act
  - no third-party approvals needed for contribution reductions

- No requirement for any agreement to be in place specifying exactly when and by how much contributions will be reduced
  - agreements in place already sufficient
  - standard says benefits need only be reasonably expected

- No onerous funding requirements exist for OTPP or OPSEUPP

Overall Conclusions of Panel

Recognition and measurement of the asset

- Net pension asset, without any valuation allowance, should be recognized in the Province's financial statements.
- Recognizing the asset will provide a faithful representation of the Province's financial position.
- Recognizing the asset will properly reflect the intention of the "deal" between the sponsors.

Overall

- Reasonable expectation that Sponsors will be able to benefit from lower contribution levels in future
- Established mechanisms exists to put these expectations into practice (in Plan documents and legislation)
- Surplus assets have real economic value government can benefit from so should be recognized

Appendix: Panel members

- Patricia O'Malley (Chair) – former Chair of Canadian Accounting Standards Board, former member of International Accounting Standards Board, Chair of the Canadian Actuarial Standards Oversight Council, former technical partner KPMG

- Murray Gold – Leading practitioner and senior pension and benefits partner at Koskie Minsky LLP

- Uros Karadzic – Pension actuary, member of the PSAB's Employment Benefit Taskforce, partner at EY

- Paul Martin – Comptroller with the Government of New Brunswick, member of the PSAB's Employment Benefit Taskforce and previously a partner with the national accounting firm of Grant Thornton LLP

FW_ Summary of impact based on proposed year-end adjustments.rtf

From: Petsche, Nadine (TBS) []
To: Jack, Shannon (TBS) [Shannon.Jack@ontario.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: Summary of impact based on proposed year-end adjustments
Date: Saturday, May 27, 2017 09:32:47
Attachment 1: Summary of impact based on proposed adjustments - by year (EY 26 May 2017).pdf
Attachment 2: Summary of impact based on proposed adjustments (EY 26 May 2017).pdf
Attachment 3: image001.jpg

Shannon,

Please schedule a meeting to brief Cindy on these results. We are still awaiting feedback from the OAG on our proposed direction w.r.t. adjustments, but would like to brief Cindy on these results and receive her feedback/direction.

Thanks.

Nadine

From: Christina Chan [mailto:Christina.Chan@ca.ey.com]
Sent: May-26-17 11:02 AM
To: Fong, Pauline (TBS); Ma, Patricia (TBS); Li, Wendy (TBS); Patel, Bharat (TBS); Sun, Alicia (TBS)
Cc: Petsche, Nadine (TBS); Shayan Jafrani
Subject: Summary of impact based on proposed year-end adjustments

Hi everyone,

Thank you for forwarding us the most updated spreadsheets for all plans. We have reflected them accordingly for our analysis.

As promised, please find attached a summary of impact based on the proposed year-end adjustments. We have prepared an one-pager with both years on it (on legal size paper), as well as an individual summary page for each of the two comparative years.

Let us know if you have any questions.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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Summary of impact based on proposed adjustments - by year (EY 26 May 2017).pdf

Summary of impact based on proposed adjustments as at 31 March 2016 - DRAFT

For illustration purposes only

Current	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Pension Liability - Continuity	50.0%	100.0%	50.0%	47.7%	50.0%		
Opening pension liability	(8,667)	1,208	(487)	1,056	28.5	(906)	(7,768)
Pension expenditure	118	538	180	761	194.3	(47)	1,744
Less: contributions made during Fiscal year by ON	(1,598)	(361)	(214)	(945)	(206.1)	-	(3,324)
Ending fiscal pension liability, at 31 March 2016	(10,147)	1,385	(521)	872	16.7	(953)	(9,347)

Proposed	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Pension Liability - Continuity	49.0%	100.0%	47.7%	47.7%	50.0%		
Opening pension liability	(8,667)	1,208	(487)	1,056	28.5	(906)	(7,768)
Opening balance adjustment (in aggregate)	651	(666)	(277)	(83)	(0.2)	906	531
Pension expenditure	232	560	155	754	194.3	-	1,895
Less: portion of contributions allocated in excess of ON	(13)		-	(4)	-	-	(17)
Less: contributions made during Fiscal year by ON	(1,598)	(361)	(214)	(945)	(206.1)	-	(3,324)
Ending fiscal pension liability, at 31 March 2016	(9,395)	741	(823)	778	16.5	-	(8,683)

Differences	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Opening pension liability	-	-	-	-	-	-	-
Opening balance adjustment (in aggregate)	651	(666)	(277)	(83)	(0.2)	906	531
Pension expenditure	114	22	(25)	(7)	-	47	151
Less: portion of contributions allocated in excess of ON	(13)	-	-	(4)	-		(17)
Less: contributions made during Fiscal year by ON	-	-	-	-	-	-	-
Ending fiscal pension liability, at 31 March 2016	752	(645)	(302)	(94)	(0.2)	953	664

Summary of impact based on proposed adjustments as at 31 March 2017 - DRAFT

For illustration purposes only

Current	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Pension Liability - Continuity	50.0%	100.0%	50.0%	47.3%	50.0%		
Opening pension liability	(10,147)	1,385	(521)	872	16.7	(953)	(9,347)
Pension expenditure	(508)	518	132	621	198.7	*(47)*	915
Less: contributions made during Fiscal year by ON	(1,635)	(368)	(219)	(991)	(215.5)	-	(3,428)
Ending fiscal pension liability, at 31 March 2017	(12,290)	1,535	(608)	502	(0)	(1,000)	(11,861)

Proposed	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Pension Liability - Continuity	49.0%	100.0%	47.7%	47.3%	50.0%		
Opening pension liability	(9,395)	741	(823)	778	16.5	-	(8,683)
Pension expenditure	(381)	464	113	615	198.7	-	1,010
Less: portion of contributions allocated in excess of ON	40	-	-	(5)	0.5	-	36
Less: contributions made during Fiscal year by ON	(1,635)	(368)	(219)	(991)	(215.5)	-	(3,428)
Ending fiscal pension liability, at 31 March 2017	(11,371)	837	(929)	397	0	-	(11,066)

Differences	OTPP	PSPP	OPSEUPP	HOOPP	CATTPP	Other agencies	Total
Opening pension liability	752	(645)	(302)	(94)	(0.2)	953	664
Pension expenditure	127	(54)	(19)	(6)	-	47	95
Less: portion of contributions allocated in excess of ON	40.0	-	-	(5.0)	0.5	-	36
Less: contributions made during Fiscal year by ON	-	-	-	-	-	-	-
Ending fiscal pension liability, at 31 March 2017	919	(698)	(321)	(105)	0.3	1,000	795

Summary of impact based on proposed adjustments (EY 26 May 2017).pdf

Summary of impact based on proposed adjustments - DRAFT

For illustration purposes only

Current	OTPP		PSPP		OPSEUPP		HOOPP		CATTPP		Other agencies		Total	
	F2015	F2016	F2015	F2016	F2015	F2016	F2015	F2016	F2015	F2016	F2015	F2016	F2015	F2016
Pension Liability - Continuity	50.0%	50.0%	100.0%	100.0%	50.0%	50.0%	47.7%	47.3%	50.0%	50.0%				
Opening pension liability	(8,667)	(10,147)	1,208	1,385	(487)	(521)	1,056	872	28.5	16.7	(906)	(953)	(7,768)	(9,347)
Pension expenditure	118	(508)	538	518	180	132	761	621	194.3	198.7	(47)	(47)	1,744	915
Less: contributions made by ON	(1,598)	(1,635)	(361)	(368)	(214)	(219)	(945)	(991)	(206.1)	(215.5)	-	-	(3,324)	(3,428)
Ending fiscal pension liability	(10,147)	(12,290)	1,385	1,535	(521)	(608)	872	502	16.7	(0.1)	(953)	(1,000)	(9,347)	(11,861)

Proposed	OTPP		PSPP		OPSEUPP		HOOPP		CATTPP		Other agencies		Total	
Pension Liability - Continuity	49.0%	49.0%	100.0%	100.0%	47.7%	47.7%	47.7%	47.3%	50.0%	50.0%				
Opening pension liability	(8,667)	(9,395)	1,208	741	(487)	(823)	1,056	778	28.5	16.5	(906)	-	(7,768)	(8,683)
Opening balance adjustment (in aggregate)	651	-	(666)	-	(277)	-	(83)	-	(0.2)	-	906	-	531	-
Pension expenditure	232	(381)	560	464	155	113	754	615	194.3	198.7	-	-	1,895	1,010
Less: portion of contributions allocated in excess of ON	(13)	40		-	-	-	(4)	(5)	-	0.5	-	-	(17)	36
Less: contributions made by ON	(1,598)	(1,635)	(361)	(368)	(214)	(219)	(945)	(991)	(206.1)	(215.5)	-	-	(3,324)	(3,428)
Ending fiscal pension liability	(9,395)	(11,371)	740	837	(823)	(929)	778	397	16.5	0.2	-	-	(8,683)	(11,066)

Differences	OTPP		PSPP		OPSEUPP		HOOPP		CATTPP		Other agencies		Total	
Opening pension liability	-	752	-	(645)	-	(302)	-	(94)	-	(0.2)	-	953	-	664
Opening balance adjustments at 1 April 2015	651	-	(666)	-	(277)	-	(83)	-	(0.2)	-	906	-	531	-
Pension expenditure	114	127	22	(54)	(25)	(19)	(7)	(6)	-	-	47	47	151	95
Less: portion of contributions allocated in excess of ON	(13)	40	-	-	-	-	(4)	(5)	-	0.5			(17)	36
Less: contributions made by ON	-	-	(0)	-	-	-	-	-	-	-	-	-	(0)	-
Ending fiscal pension liability, at 31 March 2017	752	919	(645)	(698)	(302)	(321)	(94)	(105)	(0.2)	0.3	953	1,000	664	795
F2016 differences, excluding opening balance adjustment		167		(54)		(19)		(11)		0.5		47		131

Commentary

1. Reflect all proposed adjustments (contribution receivable, unamortized contribution differences, cumulativetransfer, reflect other participating employers)
2. Need to consider the treatment of recognizing difference between the portion of contributions included in assets and actual ON contributions
   For HOOPP, expense is subsequently determined based on the calculated opening and ending pension liability and actual contributions by other source. As such, it's implicitly included in pension expense (outside of calculation tool)
3. Pension expenditure for HOOPP reflects immediate gain/loss recognition arising from change in % allocation
   This is consistent with OPCD's current practice performed outside of the calculation spreadsheet
4. Increase of approximately $100M on OTPP's annual pension expense relates to removal of expected return on contribution receivable
5. F2016 Pension expense (income) for other agencies is estimated based on F2015 for illustration purposes
6. Above figures do not reflect asset ceiling test and the adjustment for the differential use of the Rate Stabilization Fund ("RSF") for OPSEUPP

image001.pdf

EY

FW_ TBS-OTB-OPCD-15.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: TBS-OTB-OPCD-15
Date: Tuesday, September 20, 2016 10:09:02
Attachment 1: image001.png
Attachment 2: SOW_DT_July21_2016.pdf

From: Raymond, Martin (CA - Montreal) [mailto:maraymond@deloitte.ca]
Sent: July 20, 2016 10:11 PM
To: Virani, Shyrose (TBS); Petsche, Nadine (TBS); Colley, Matthew (CA - Toronto)
Cc: CA Ontario Online Bidding (CA)
Subject: RE: TBS-OTB-OPCD-15

Shyrose and Nadine,

Find enclosed the signed version of the SOW.

I have added the start date of July 21, 2016 as we are having an initial call on this Thursday.

I have also added my electronic signature.

No other change to the document you provided.

We really look forward to working with you.

Let us know if anything else is needed for paperwork.

Regards

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Virani, Shyrose (TBS) [mailto:Shyrose.Virani@ontario.ca]
Envoyé : 20 juillet 2016 10:41
À : Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : CA Ontario Online Bidding (CA) <onlinebidding@deloitte.ca>
Objet : TBS-OTB-OPCD-15

Treasury Board Secretariat is pleased to advise that you are selected proponent pursuant to the above-noted procurement process.

We will send you official letter shortly, in the meantime, we are sending you our draft SOW, please review and call Nadine at 416-325-1448 between 11:30 – 1:00 if you get a chance, so that we can finalize the dates.

Thank you,

Shyrose Virani

Administrative Coordinator

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SOW_DT_July21_2016.pdf

FORM OF STATEMENT OF WORK – OPS ENTITY

Statement of Work for Management Consulting Services

This Statement of Work no. **– RFS TBS-OTB-OPCD-15 made in duplicate and effective July 21, 2016 ending on March 31, 2017.**

Deloitte LLP (the "Vendor" or “Deloitte”) and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of **July 21, 2016** between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$ $100,000.00 does not include HST

4. *Project Start Date:* July 21, 2016

5. *Project End Date:* March 31, 2017

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following

- Taking into account public sector accounting principles, advice and guidance on complex accounting and reporting matters related to accounting for pensions on the Province’s consolidated financial statements.

- The Vendor will participate in meetings as necessary to support the engagement objectives:

- Working with management of OPCD’s Accounting Policy and Financial Reporting Branch (APFR), the provider of complex accounting services related to the following possible areas:
    - Develop discussion and analysis material
    - Develop draft input/briefing materials/option papers
    - Provide accounting advice and guidance related to the accounting for pensions on the Province’s financial statements
    - Participate in discussions with internal and external stakeholders, as required

  As part of this engagement, the consultant(s) would be expected to provide professional accounting expertise in assessing actuarial assessments for specified plans in relation to

applying the ceiling test to the accrued pension benefit assets in accordance with PS3250 (3250.050 to PS3250.059).

7. *Ownership and Licences* - **Attachment D** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Deloitte's working relationship with OPCD is vital to the success of their engagement. The Project Lead that will handle OPCD work is Martin Raymond (partner), the leading consulting actuary for pension at Deloitte. In his work, Martin will be supported by Trevor Gary. Martin and Trevor will have access to some specific personnel of Deloitte that may be involved to limited extent depending on the needs. Clair Grindley and Matt Colley will be the 2 main subject matter experts that may have some implication.. Max Bazile, another actuarial resource is identified just as a support should a very large workload come in a short period of time and OPCD needing some urgent support. _Deloitte's communication strategy will be centred on periodic project update meetings, the frequency of which will be determined by the OPCD and Deloitte.

9. *Work Location* - All meetings will be within Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive.

    If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Fixed Price or Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Billing and Payment Process* – The Vendor shall provide the Client with quarterly billing statements that outline the per diem charges [as provided Deloitte's response to RFS TBS-OTB-OPCD-15, no later than 10 Business Days after the end of each quarter.

    Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Name of Individual	**Level**
Martin Raymond (Project Lead)	Partner, Actuarial Services
Trevor Gary (Senior Analyst)	Senior, Actuarial Services
Matt Colley (subject matter expert on Ontario process and protocols)	Senior Manager, Audit

Clair Grindley (subject matter expert on pension accounting)	Partner, Audit
Max Bazile (backup resource for actuarial team)	Senior Manager, Actuarial Services

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client:	Treasury Board Secretariat, Office of the Provincial Controller Division
Branch:	Accounting Policy and Financial Reporting
Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Client's designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Indemnity* – the indemnity set out in the Master Agreement applies to this assignment.

18. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

19. *Vendor Representative and Receipt of Notices*

The name and title of the Vendor's Representative: Martin Raymond
1190 Avenue des Canadiens-de-Montréal,
Montréal, Quebec
Canada
H3B 0M7

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

Her Majesty the Queen in right of Ontario as represented by The President of the Treasury Board

Per:

Signature: _____

Name: _____

Title: _____

Pursuant to delegated authority.

DELOITTE LLP.

Per:

Signature:

Name: **Martin Raymond**

Title: **Partner**

I have the authority to bind the Vendor.

FW_ Treasury Board Secretariat of Ontario Invoice - November 29, 2016.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Treasury Board Secretariat of Ontario Invoice - November 29, 2016
Date: Wednesday, November 30, 2016 11:43:11
Attachment 1: TBSO Nov T20161129_Tax Invoice_Number_TR136191973.pdf
Attachment 2: image001.png

Pls. approve

From: nicole.smellie@ca.pwc.com [mailto:nicole.smellie@ca.pwc.com]
Sent: November 29, 2016 12:58 PM
To: Virani, Shyrose (TBS)
Cc: lucy.durocher@ca.pwc.com
Subject: Treasury Board Secretariat of Ontario Invoice - November 29, 2016

Good Afternoon Shyrose,

Please find attached a PDF copy of our **November** invoice. Unless specified by you, we will not be forwarding a hard copy by mail.

For your convenience we accept the following payment methods:

Wire Transfer

Cheque

Credit Card

Please Remit Payment Referencing Invoice Number To:

Please remit Payment and Invoice Copy To:

Please contact Nicole Smellie:

CIBC, 199 Bay St., CCW, Concourse Level, Toronto, Ontario Canada M5L 1G9
Account Name: PricewaterhouseCoopers LLP **Transit No:** 010:00002 Swift Code: CIBCCATT

PwC Central Accounting Centre, PwC Centre, 354 Davis Rd.,

Suite 600
Oakville, ON
L6J 0C5

nicole.smellie@ca.pwc.com to receive secure link or by phone 416-941-8383 ext. 14070

CAD Account: 63-55412
USD Account: 04-77419

Amex, MasterCard, and Visa Accepted

*Email payment details, including invoice number and amount paid to:
accounts.receivable@ca.pwc.com

Please note that an invoice number **must be included** for all payments. **For credit card transactions Foreign Currency exchange rate charges, and foreign transaction fees may apply for invoices issued in currency other than Canadian dollars.**

If you have any questions regarding this invoice please do not hesitate to contact myself or **Lucy Durocher**.

Kind Regards,

Nicole Smellie
PwC | Billing Administrator, Assurance
T: +1 416 941 8383 ext. 14070
Email: nicole.smellie@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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responsibility of such person. We accept no responsibility for any loss or damages suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

Ce courriel est strictement réservé à l'usage de la personne à qui il est adressé (le destinataire). Il peut contenir de l'information privilégiée et confidentielle. L'examen, la réexpédition et la diffusion de ce message par une personne autre que son destinataire sont interdits. Nous déclinons toute responsabilité à l'égard des pertes ou des dommages subis par une personne autre que le destinataire par suite de décisions ou de mesures fondées sur le contenu de cette communication ou autrement. Si vous avez reçu ce courriel par erreur, veuillez communiquer avec son expéditeur et en détruire toutes les copies.

TBSO Nov T20161129_Tax Invoice_Number_TR136191973.pdf

Invoice

Ms. Nadine Patsche
Director, Accounting Policy and Financial Reportin
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Lucy Durocher
Telephone: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com

Invoice number:	TR136191973	Account number:	60144520
Invoice date:	November 29, 2016	Payment requested by:	December 14, 2016

CAD

Fees for Professional Services: Interim billing for Pension Accounting advice of 36.8 hours to November 25, 2016.

Fees	**14,097.00**
HST	**1,832.61**
Total due	**15,929.61**

Remittance information

Electronic wire or EFT (not e-Transfer): CIBC, 199 Bay Street, CCW Concourse Level, Toronto, Ontario, M5L 1G9
Account name: PricewaterhouseCoopers LLP
Transit no.: 010:00002 Swift code: CIBCCATT CAD account: 63-55412 USD account: 04-77419
Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Invoice *Remittance copy*

Ms. Nadine Patsche
Director, Accounting Policy and Financial Reportin
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Lucy Durocher
Telephone: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com

Invoice number:	TR136191973	Account number:	60144520
Invoice date:	November 29, 2016	Payment requested by:	December 14, 2016

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Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

image001.pdf

FW_ Treasury Board Secretariat of Ontario Invoice, April 7, 2017.rtf

From: Virani, Shyrose (TBS) []
To: Bernard, Dena (MOF) [Dena.Bernard@ontario.ca]
Subject: FW: Treasury Board Secretariat of Ontario Invoice, April 7, 2017
Date: Friday, April 07, 2017 12:35:22
Attachment 1: ATT00001.gif
Attachment 2: TBSO April 20170407_Tax Invoice_Number_TR137128383.pdf

---

From: nicole.smellie@ca.pwc.com [nicole.smellie@ca.pwc.com]
Sent: April 7, 2017 11:09 AM
To: Virani, Shyrose (TBS)
Cc: lucy.durocher@ca.pwc.com
Subject: Treasury Board Secretariat of Ontario Invoice, April 7, 2017

Good Morning Shyrose,

Please find attached a PDF copy of our **April** invoice. Unless specified by you, we will not be forwarding a hard copy by mail.

For your convenience we accept the following payment methods:

Wire Transfer **Cheque**

Please Remit Payment Referencing Invoice Number To: **Please remit Payment and Invoice Copy To:**
CIBC, 199 Bay St., CCW, Concourse Level, Toronto, Ontario Canada M5L 1G9
Account Name: PricewaterhouseCoopers LLP **Transit No:** 010:00002 Swift Code: CIBCCATT PwC Central Accounting Centre, PwC Centre, 354 Davis Rd.,
Suite 600
Oakville, ON
L6J 0C5
CAD Account: 63-55412
USD Account: 04-77419
*Email payment details, including invoice number and amount paid to:
accounts.receivable@ca.pwc.com

Please note that an invoice number **must be included** for all payments. **For credit card transactions Foreign Currency exchange rate charges, and foreign transaction fees may apply for invoices issued in currency other than Canadian dollars.**

If you have any questions regarding this invoice please do not hesitate to contact myself or **Lucy Duroccher**.

Kind Regards,

Nicole Smellie
PwC | Billing Administrator, Assurance
T: +1 416 941 8383 ext. 14070
Email: nicole.smellie@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2

http://www.pwc.com/ca

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ATT00001.pdf

TBSO April 20170407_Tax Invoice_Number_TR137128383.pdf

Invoice

Ms. Nadine Patsche
Director, Accounting Policy & Financial Reporting
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Michael Hawtin
Telephone: +1 416 815 5003
Email: michael.hawtin@ca.pwc.com

Invoice number:	TR137128383	Account number:	60144520
Purchase order:	228100		
Invoice date:	April 7, 2017	Payment requested by:	April 22, 2017

Fees for Professional Services: Assistance to Pension Asset Expert Advisory Panel for 4.5 days @ $1,600 per diem, for the period ending March 31, 2017.

	CAD
Fees	**7,200.00**
Disbursements	**26.79**
Total fees and disbursements	**7,226.79**
HST	**939.48**
Total due	**8,166.27**

Remittance information

Electronic wire or EFT (not e-Transfer): CIBC, 199 Bay Street, CCW Concourse Level, Toronto, Ontario, M5L 1G9
Account name: PricewaterhouseCoopers LLP
Transit no.: 010:00002 Swift code: CIBCCATT CAD account: 63-55412 USD account: 04-77419
Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Invoice *Remittance copy*

Ms. Nadine Patsche
Director, Accounting Policy & Financial Reporting
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Michael Hawtin
Telephone: +1 416 815 5003
Email: michael.hawtin@ca.pwc.com

Invoice number:	TR137128383	Account number:	60144520
Purchase order:	228100		
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HST registration # 87057 6089 RT0001

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FW_ Treasury Board Secretariat of Ontario Invoice, January 31, 2017.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: FW: Treasury Board Secretariat of Ontario Invoice, January 31, 2017
Date: Wednesday, February 01, 2017 12:43:07
Attachment 1: Treasury Board Jan 20170201_Tax Invoice_Number_TR137106714.pdf
Attachment 2: image001.png

For your approval

From: nicole.smellie@ca.pwc.com [mailto:nicole.smellie@ca.pwc.com]
Sent: February 1, 2017 11:42 AM
To: Virani, Shyrose (TBS)
Cc: lucy.durocher@ca.pwc.com
Subject: Treasury Board Secretariat of Ontario Invoice, January 31, 2017

Good Morning Shyrose,

Please find attached a PDF copy of our **January** invoice. Unless specified by you, we will not be forwarding a hard copy by mail.

For your convenience we accept the following payment methods:

Wire Transfer

Cheque

Credit Card

Please Remit Payment Referencing Invoice Number To:

Please remit Payment and Invoice Copy To:

Please contact Nicole Smellie:

CIBC, 199 Bay St., CCW, Concourse Level, Toronto, Ontario Canada M5L 1G9
Account Name: PricewaterhouseCoopers LLP **Transit No:** 010:00002 Swift Code: CIBCCATT

PwC Central Accounting Centre, Centre, Suite 600
PwC
354 Davis Rd.,

Oakville, ON
L6J 0C5

nicole.smellie@ca.pwc.com to receive secure link or by phone 416-941-8383 ext. 14070

CAD Account: 63-55412
USD Account: 04-77419

Amex, MasterCard, and Visa Accepted

*Email payment details, including invoice number and amount paid to:
accounts.receivable@ca.pwc.com

Please note that an invoice number **must be included** for all payments. **For credit card transactions Foreign Currency exchange rate charges, and foreign transaction fees may apply for invoices issued in currency other than Canadian dollars.**

If you have any questions regarding this invoice please do not hesitate to contact myself or Lucy Duroccher .

Kind Regards,

Nicole Smellie
PwC | Billing Administrator, Assurance
T: +1 416 941 8383 ext. 14070
Email: nicole.smellie@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

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Treasury Board Jan 20170201_Tax Invoice_Number_TR137106714.pdf

Invoice

Ms. Nadine Patsche
Director, Accounting Policy & Financial Reporting
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Michael Hawtin
Telephone: +1 416 815 5003
Email: michael.hawtin@ca.pwc.com

Invoice number:	TR137106714	Account number:	60144520
Invoice date:	January 31, 2017	Payment requested by:	February 15, 2017

CAD

Fees for Professional Service:

Assistance to Pension Asset Expert Advisory panel - OTPP and OPSEUPP for 12 days @ $1,600 per diem.

Fees	**19,200.00**
HST	**2,496.00**
Total due	**21,696.00**

Remittance information

Electronic wire or EFT (not e-Transfer): CIBC, 199 Bay Street, CCW Concourse Level, Toronto, Ontario, M5L 1G9
Account name: PricewaterhouseCoopers LLP
Transit no.: 010:00002 Swift code: CIBCCATT CAD account: 63-55412 USD account: 04-77419
Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

Invoice *Remittance copy*

Ms. Nadine Patsche
Director, Accounting Policy & Financial Reporting
Treasury Board Secretariat of Ontario
Frost Bulding North - 1st Floor
95 Grosvenor Street
Toronto On Canada M7A 1Y7

PricewaterhouseCoopers LLP
PwC Tower
18 York Street, Suite 2600
Toronto, ON, Canada M5J 0B2
Telephone: +1 416 863 1133
Facsimile: +1 416 365 8215

Contact: Michael Hawtin
Telephone: +1 416 815 5003
Email: michael.hawtin@ca.pwc.com

Invoice number:	TR137106714	Account number:	60144520
Invoice date:	January 31, 2017	Payment requested by:	February 15, 2017

CAD

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Account name: PricewaterhouseCoopers LLP
Transit no.: 010:00002 Swift code: CIBCCATT CAD account: 63-55412 USD account: 04-77419
Email payment details, including invoice number and amount paid, to: accounts.receivable@ca.pwc.com.

Cheques payable to: PricewaterhouseCoopers LLP *Enclose remittance copy of invoice with payment.*
Send to: PwC CAC, PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5

HST registration # 87057 6089 RT0001

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

image001.pdf

FW_ debriefing - Deloitte.rtf

From: Patel, Bharat (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: debriefing - Deloitte
Date: Friday, December 08, 2017 16:55:56

Mark,

As discussed can you please keep Cindy aware that DT asked for briefing on our decision about pension contract to E&Y and guide what feedback you want to provide?

Thanks,
Bharat

-----Original Appointment-----
From: Virani, Shyrose (TBS)
Sent: December-08-17 3:45 PM
To: Virani, Shyrose (TBS); Patel, Bharat (TBS); Sun, Alicia (TBS); Fong, Pauline (TBS); cawarburton@deloitte.ca
Subject: FW: debriefing - Deloitte
When: December-18-17 10:00 AM-10:30 AM (UTC-05:00) Eastern Time (US & Canada).
Where: TBS-R-7 Queen's Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom

-----Original Appointment-----
From: Virani, Shyrose (TBS)
Sent: December-06-17 11:41 AM
To: Virani, Shyrose (TBS); Sun, Alicia (TBS); Fong, Pauline (TBS); cawarburton@deloitte.ca
Subject: debriefing - Deloitte
When: December-18-17 10:00 AM-10:30 AM (UTC-05:00) Eastern Time (US & Canada).
Where: TBS-R-7 Queen's Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom

---

From: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Sent: December 6, 2017 10:40 AM
To: Virani, Shyrose (TBS)
Cc: Raymond, Martin (CA - Montreal); Colley, Matthew (CA - Toronto)
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Attachments: letter attached

Thank you very much for notifying us of this contract decision. Please can we book a debrief meeting to receive feedback on our response.

Thanks

Cara

--

Cara Warburton

Senior Manager | Public Sector

22 Adelaide Street West, Suite 200, Toronto, ON, M5H 0A9, Canada

D: (416) 601 5763 | M: (647) 300 9400

--

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FW_ security clearance.rtf

From: Virani, Shyrose (TBS) []
To: sean.cable@ca.pwc.com [sean.cable@ca.pwc.com]; michael.walke@ca.pwc.com [michael.walke@ca.pwc.com]
Subject: FW: security clearance
Date: Sunday, October 23, 2016 15:25:57

From: Virani, Shyrose (TBS)
Sent: October 23, 2016 2:38 PM
To: 'mario.chasse@ca.pwc.com'; 'sean.cable@pwc.com'; lucy.durocher@ca.pwc.com; 'michael.walke@pwc.com'; 'martin.boucher@ca.pwc.com'
Cc: 'robert.urbanoski@ca.pwc.com'
Subject: security clearance

Hi

Hi

I just need to find out if you have been screened for the security check, if so, can I please have your Security C number, if not, Triton will be in touch with you.

Thanks

Shyrose Virani

FW_ security screenings.rtf

From: Warburton, Cara (CA - Toronto) [cawarburton@deloitte.ca]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: security screenings
Date: Monday, November 14, 2016 17:29:31
Attachment 1: image002.png
Attachment 2: image003.png

Hi Shyrose

Please could you check if Martin's clearance has been approved and if so please could you provide me with the # and expiry date.

Thanks

Cara

From: Raymond, Martin (CA - Montreal)
Sent: Monday, November 14, 2016 4:26 PM
To: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>; Gary, Trevor (CA - Toronto) <tgary@deloitte.ca>; Bazile, Max (CA - Toronto) <mbazile@deloitte.ca>; Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>
Cc: Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Subject: RE: security screenings

Cara

I did do the Triton access and completed some info.

Is this a 2nd requirement to complete additional info ? or just the Max access ?

I had used my passport info to complete it.

Thanks

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services

Deloitte

1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada

Tel / Direct : 514-393-7367

Fax : 514-390-4104

maraymond@deloitte.ca | www.deloitte.ca

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De : Warburton, Cara (CA - Toronto)
Envoyé : 14 novembre 2016 16:24
À : Gary, Trevor (CA - Toronto) <tgary@deloitte.ca>; Bazile, Max (CA - Toronto) <mbazile@deloitte.ca>; Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>; Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc : Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>
Objet : FW: security screenings

I spoke to Shyrose this morning and she initiated these security clearance requests in connection with the Pension Accounting and Premier's Advisory accounting work.

She is going to resubmit the requests with Triton shortly, please can you all action the email when received.

Items to note:

· The link can only be accessed once – so do not action if you do not have time to

complete in one sitting

· It takes approx. 20 minutes to complete the clearance process

· Each individual page times-out after 5 minutes

· You will need the following information in order to complete the process – 5 years address history, Proof of legal status to work in Canada eg. Passport #, Birth Certificate, PR card, credit card for payment

Thanks very much

Cara

From: Warburton, Cara (CA - Toronto) [mailto:cawarburton@deloitte.ca]
Sent: November 11, 2016 10:51 AM
To: Virani, Shyrose (TBS)
Cc: Bazile, Max (CA - Toronto)
Subject: RE: security screenings

Hi Shyrose

Max timed out on his Trion application, please can you reissue it.

Thanks

Cara

--

Cara Warburton

Senior Manager | Company Security Officer

22 Adelaide Street West, Suite 200, Toronto, ON, M5H 0A9, Canada

D: (416) 601 5763 | M: (647) 300 9400

--

Please consider the environment before printing.

From: Virani, Shyrose (TBS) [mailto:Shyrose.Virani@ontario.ca]
Sent: Sunday, October 23, 2016 2:24 PM
To: Gary, Trevor (CA - Toronto) <tgary@deloitte.ca>; Bazile, Max (CA - Toronto) <mbazile@deloitte.ca>; Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>; cgrindley@deloitte.ca; Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Cc: Warburton, Cara (CA - Toronto) <cawarburton@deloitte.ca>
Subject: security screenings

Hi

I just need to find out if you have screened for the security check, if so, can I please have your Security C number, if not, Triton will be in touch with you.

Thanks

Shyrose Virani

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image002.pdf

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image003.pdf

Deloitte.

FW_ security screenings.rtf

From: Virani, Shyrose (TBS) []
To: Grindley, Clair (CA - Toronto) (clgrindley@deloitte.ca) [clgrindley@deloitte.ca]
Subject: FW: security screenings
Date: Sunday, October 23, 2016 14:25:37

From: Virani, Shyrose (TBS)
Sent: October 23, 2016 2:24 PM
To: tgary@deloitte.ca; Bazile, Max (CA - Toronto); kdanyluk@deloitte.ca; 'cgrindley@deloitte.ca'; maraymond@deloitte.ca
Cc: cawarburton@deloitte.ca
Subject: security screenings

Hi

I just need to find out if you have screened for the security check, if so, can I please have your Security C number, if not, Triton will be in touch with you.

Thanks

Shyrose Virani

FW_ some advice.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: FW: some advice
Date: Monday, March 20, 2017 10:55:42

Lucy seems to think that the accounting advice RFS is still open?

From: lucy.durocher@ca.pwc.com [mailto:lucy.durocher@ca.pwc.com]
Sent: March-17-17 9:45 AM
To: Petsche, Nadine (TBS)
Cc: Keates, James (TBS)
Subject: Re: some advice

Hi Nadine,

Of course. I assume this would be under the pension accounting advice engagement - which is still open, as opposed to the Panel writer engagement.

In terms of timing, the Panel is close to finalizing the internal memo to be shared with your group (in addition to the public supplemental report). While it asks more questions than gives answers, it may be a useful starting point for a conversation. I expect this to be finalized early next week.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Keates, James (TBS)" <James.Keates@ontario.ca>
Date: 03/16/2017 03:45 PM
Subject: some advice

Hi Lucy.
Just wanted to let you know that James Keates from our accounting policy group might reach out to you for some additional background w.r.t. pension governance/influence on multi-employer plans.
Thanks in advance.
Nadine

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Format for plan analysis.rtf

From: Petsche, Nadine (TBS) []
To: Colavecchia, Pina (CA - Toronto) [pcolavecchia@deloitte.ca]
CC: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
Subject: Format for plan analysis
Date: Saturday, November 05, 2016 06:48:05

Pina,
In the interest of expediting the analysis and documentation related to the other plans, I think it might make more sense to just build on the information note format that was provided for OPSEUPP. We (OPCD) will just leverage the key elements of the analysis in developing the supplement to the OTPP position paper. Your thoughts? N

Fw_ Advisory (revised wording related to accounting opinion).rtf

From: Petsche, Nadine (TBS) []
To: Li, Wendy (TBS) [Wendy.Li@ontario.ca]
Subject: Fw: Advisory (revised wording related to accounting opinion)
Date: Monday, November 07, 2016 11:37:09

Wendy,
Please send me extract from the table for the AG's 1st recommendation only. Just the recommendation. Thx. N
From: Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>
Sent: Monday, November 7, 2016 9:03 AM
To: Petsche, Nadine (TBS); Colley, Matthew (CA - Toronto); Jesty, Paula (CA - Toronto)
Cc: Veinot, Cindy (TBS)
Subject: RE: Advisory (revised wording related to accounting opinion)

Hi, Nadine. We will have some alternate wording for this to propose to you. But before we do, I'm wondering if it would be possible to see the comment that it is responding to? Or to get an understanding of the key points raised in that comment? Please let me know. If it's easier to just talk about it, we can have a call.

The summary itself is in for final review as is the wording for the limitations around the opinion to be given to the panel.

Regards,

Kerry

--

Kerry Danyluk

Partner | National Accounting and Assurance

D: +1 (416) 775 7183

kdanyluk@deloitte.ca | deloitte.ca

--

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From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Saturday, November 5, 2016 9:57 AM
To: Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>; Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>; Jesty, Paula (CA - Toronto) <pjesty@deloitte.ca>
Cc: Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>
Subject: RE: Advisory (revised wording related to accounting opinion)

Good morning!

Just forwarding the most current wording for your review and feedback. Please advise of any concerns. Thanks.

Nadine

During the course of the Public Accounts audit, the Auditor General was provided with analysis and support on the province's interpretation of public sector accounting standards to the Province's jointly sponsored pension plans. This information included an external accounting opinion that addressed issues related to the requirement for a legally enforceable right to reduce contributions (which supported the Province's interpretation) and considerations on incorporating the impact of legal uncertainty in estimating the valuation of the net pension assets.

From: Petsche, Nadine (TBS)
Sent: November-04-16 4:33 PM
To: Danyluk, Kerry (CA - Toronto); Colley, Matthew (CA - Toronto); Jesty, Paula (CA - Toronto)
Cc: Veinot, Cindy (TBS)
Subject: RE: Advisory

Thanks Kerry. Your feedback is helpful.

For additional context, the extract is part of a response that would be reflected in the AG's Annual Report which is expected to be released in December. Based on your feedback, I have amended the wording below. Your feedback on the revised wording would be appreciated.

Nadine

From: Danyluk, Kerry (CA - Toronto) [mailto:kdanyluk@deloitte.ca]
Sent: November 4, 2016 3:48 PM
To: Petsche, Nadine (TBS); Colley, Matthew (CA - Toronto); Jesty, Paula (CA - Toronto)
Subject: RE: Advisory

Hi, Nadine. I'd like to understand the context a bit better. Will this commentary go in a public document? We will need to have the context before responding.

With respect to the actual wording, I don't think it's true to say that our report supported your accounting treatment. You recorded an asset of around $10 billion and we declined to provide a view on the amount of the asset. So this description goes beyond the scope of our report and we would not agree to it as worded below.

Regards,

Kerry

--

Kerry Danyluk

Partner | National Accounting and Assurance

D: +1 (416) 775 7183

kdanyluk@deloitte.ca | deloitte.ca

--

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Please consider the environment before printing.

From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Friday, November 4, 2016 3:32 PM
To: Colley, Matthew (CA - Toronto) <mcolley@deloitte.ca>; Jesty, Paula (CA - Toronto) <pjesty@deloitte.ca>; Danyluk, Kerry (CA - Toronto) <kdanyluk@deloitte.ca>
Subject: Advisory

Matt/Paula/Kerry,

We are currently drafting our responses to the AG's Chapter 2 of her Annual Report. Below is an extract that refers to your opinion. It is a generic reference which I understand from discussions is OK. Please confirm.

Nadine

During the course of the audit of the Public Accounts of Ontario 2015-16, the Province shared background and analysis on interpretation of public sector accounting standards to the Province's jointly sponsored pension plans, including an accounting opinion from an external public accounting firm which addressed questions regarding legally enforceability of the Province's right to recognize a pension asset under PS 3250 and the impact of uncertainty with regards to assessing the government's expectations of future benefit from a pension asset.

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Fw_ Benefit Trust Accounting - employees on LTD.rtf

From: Sun, Alicia (TBS) []
To: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]; Christina Chan [Christina.Chan@ca.ey.com]
CC: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Fw: Benefit Trust Accounting - employees on LTD
Date: Tuesday, May 02, 2017 16:54:48

Christina/Shayan,

My understanding that your colleague will continue to provide support on the ELHT accounting issue.

Please see below a question from EDU. Can you please pass it on to your colleague responsible for this item?

Thanks,
Alicia

Sent from my BlackBerry 10 smartphone on the Rogers network.
From: Sinasac, Elizabeth (EDU) <Elizabeth.Sinasac@ontario.ca>
Sent: Tuesday, May 2, 2017 4:38 PM
To: Sun, Alicia (TBS)
Cc: Yeung, Anthony (EDU); Yang, Andrew Dehai (EDU); Di Pasquale, Romina (EDU)
Subject: Benefit Trust Accounting - employees on LTD

Hi Alicia,

We recently had a question from one of the school boards on the proposed accounting treatment of employees on long term disability (LTD).

Q – The funding that flows from school boards to the trust is a fixed amount based on 2014-15 financial statement information plus prescribed percentage increases. If an active employee goes on LTD, the amount of funding to the trust does not change. If more or less employees join the plan, the amount of funding does not change. Due to this, the actuaries are not clear how to value the liability related to the LTD since it is not based on a “per person” amount; it is a fixed amount for the board. How would the LTD liability be valued now that the funding is now fixed? Even though an person will go on LTD and receive benefits, this doesn’t mean that the boards’ funding to the Trust will increase. How would the liability get adjusted?

Is this a question you could pass on to your consultants for review?

Thanks,

Elizabeth

Fw_ Flowchart for Minister Sousa.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Fw: Flowchart for Minister Sousa
Date: Sunday, October 23, 2016 16:09:42
Attachment 1: Pension accounting_October 21 2016.pptx

Hi Lucy. Rec'd this from Cindy earlier today. Please note that she would like to use the same numbers, if possible, for the diagram. Thx. N
From: Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>
Sent: Sunday, October 23, 2016 2:50 PM
To: Petsche, Nadine (TBS)
Cc: Hosick, Sarah (TBS)
Subject: Flowchart for Minister Sousa

Hi Nadine -- I put together some slides explaining the numbers re: the pension issue. How are things going with the flowchart? Depending where things are, you may want to use the same numbers if you are using numbers.

Please send an update as we need to get this to the MO for tomorrow morning -- thanks,

Pension accounting_October 21 2016.pdf

TBS

OPCD

Detailed analysis of pension accounting for FES

October 23, 2016

Explanation of Pension Asset

Balance of net assets before impact of regulation		
	31-Mar-15	9,154
Write down of assets based on regulation (AG's interpretation)		-9,154
Revised net asset value based on regulation		0
Pension expense in fiscal 2015-16		-298
Contributions to plans in fiscal 2015-16		1,812
Pension asset prior to valuation allowance		
	31-Mar-16	1,514
Valuation allowance, based on regulation (AG's interpretation)		-1,514
Revised net asset value based on regulation		0
Pension **recovery** estimated for fiscal 2016-17		317
Contributions to plans in fiscal 2016-17		1,901
Impact of HOOPP plan (not included elsewhere as immaterial)		22
Pension asset prior to valuation allowance		
	31-Mar-17	2,240
Valuation allowance based on AG's interpretation (no regulation)		-2,240
Revised net asset value based on regulation		0

2015-16 actual fiscal impact

2016-17 estimated fiscal impact

2015-16 Public Accounts

In 2015-16, the increase in the pension asset for OTPP and OPSEU resulted from the **net** of:

1) Pension **expense** (reduces net asset)

2) Contributions from the Province to the plan (increases net asset)

2016-17 FES

In 2016-17, the estimated increase in the pension asset for OTPP and OPSEU results from the **sum** of:

1) Pension **recovery** (increases net asset) – see next slide

2) Contributions form the Province to the plan (increases net asset)

Why does pension expense become a recovery in 2016-17?

The pension recovery estimated for fiscal 2016-17 for OTPP and OPSEUPP is:

OTPP -- Pension recovery	-452
OPSEUPP -- Pension expense	135
Analysis of pension recovery for OTPP	-317

Why is OTPP in a recovery position?

The pension recovery is made up of:

Current period benefit cost		1,512
Expected interest on accumulated obligation (6.25%)		3,617
Expected return on assets (6.25%)	-	4,871
Amortization of net actuarial gains	-	682
Other adjustments	-	27
Pension recovery	-	452

Two key issues:

- The assets exceed the obligation in the plan (measured using a discount rate based on the long-term rate of return on assets -- 6.25%), therefore, the expected return on the assets exceeds the interest on the obligation
- The **actual** performance of the assets has exceeded the **expected** performance, therefore leading to net actuarial gains that are being amortized over time, also offsetting the benefit cost

Fw_ OTPP .rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Fw: OTPP
Date: Wednesday, September 21, 2016 12:10:29

Fyi. We had requested additional info on one of the items in the legal letter. Nadine

Original Message
From: Pomykacz, Rob (MOF) <Robert.Pomykacz@ontario.ca>
Sent: Wednesday, September 21, 2016 11:57 AM
To: Petsche, Nadine (TBS)
Cc: Killoch, Alex (MOF)
Subject: FW: OTPP

Hi Nadine,

As requested, please find information below from Allan Shapira on the "Call Right" provision under the term sheet.

Thanks,
Rob

-----Original Message-----
From: Allan Shapira [mailto:allan.shapira@aonhewitt.com]
Sent: September 21, 2016 10:27 AM
To: Killoch, Alex (MOF); Pomykacz, Rob (MOF)
Subject: OTPP

I am responding to the questions on the surplus credits under the term sheet.

It is important to understand the purpose of the term sheet. The OTF and the government entered into this agreement to freeze any increase in contribution rates for a specified period. That meant that if the plan funding deteriorated during this perIod such that an actuarial report identified a funding shortfall that had to be addressed by the sponsors, this shortfall would have to be addressed by benefit reductions for future service.

If there were benefit reductions, the term sheet created a corresponding surplus credit that could be used by the OTF if and when the plan was in surplus. There have been no material benefit reductions to date nor are any anticipated now that the next required filing is after the expiration of the term sheet. Any credit that exists would be a negligible amount.

Allan

Sent from my iPhone

****
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Fw_ Pension Asset Expert Panel.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Fw: Pension Asset Expert Panel
Date: Friday, October 07, 2016 10:06:05

Hi Cindy,

Please see some names below from our actuary.

Nadine - I believe we have a touch base call scheduled for this afternoon at 1pm. Please confirm if this call will go ahead.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca
----- Forwarded by Lucy Durocher/CA/ABAS/PwC on 10/07/2016 10:02 AM -----

From: Mario Chasse/CA/ABAS/PwC
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 10/06/2016 05:17 PM
Subject: Re: Fw: Pension Asset Expert Panel

Hi Lucy.... here are a list of good actuaries that are outside of accounting firms:

Andrew Fung - Morneau Shepell - 416-380-2168 - AFung@morneaushepell.com - Andrew used to work at OMERS, so very familiar with JSPP. Before OMERS he was a consultant at another large actuarial firm.

Anne G.S. Soh - OMERS - (416) 369-3133 - asoh@omers.com - Anne is Vice President, Actuarial Services & Plan Actuary at OMERS (an internal actuary of a large JSPP in Ontario)

Phillip Morse - Willis Towers Watson - (416) 960-7113 - philip.morse@willistowerswatson.com - Phillip is the valuation actuary and senior consultant of a large JSPP

Regards

Mario Chassé
PwC | Director, Actuarial Services
T: +1 416 365 8822
Email: mario.chasse@ca.pwc.com
Assistant: Tasha Adhihetty | T: +1 416 941 8383 ext. 16232
PricewaterhouseCoopers LLP

PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: Lucy Durocher/CA/ABAS/PwC
To: Mario Chasse/CA/ABAS/PwC@Americas-CA
Date: 10/06/2016 03:14 PM
Subject: Fw: Pension Asset Expert Panel

Hi Mario,

Please see request from the Province for names of good actuaries that are outside of the accounting firms. Do you know anyone that might fit the bill?

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca
----- Forwarded by Lucy Durocher/CA/ABAS/PwC on 10/06/2016 03:13 PM -----

From: "Veinot, Cindy (TBS)" <Cindy.Veinot@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Cc: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
Date: 10/06/2016 03:12 PM
Subject: Pension Asset Expert Panel

Hi Lucy,

As you may have seen, the Province is setting up an expert panel to review the pension asset issue. We would like to include an actuary on the panel, from outside the accounting firms (so as not to conflict another firm as the panel may well engage someone). Would you be able to ask your internal actuarial contacts if they have any recommendations for someone from one of the actuarial firms who has a high level of expertise in JSPPs. It could be someone who has recently retired.

Thanks,

Cindy

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Fw_ Pension Comparison - question and timelines confirmation.rtf

From: Hatzis, Len (TBS) []
To: Murray Gold [mgold@kmlaw.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]
Subject: Fw: Pension Comparison - question and timelines confirmation
Date: Friday, September 16, 2016 22:12:46

Murray
Please see the additional comment from our client re the issues involved. Thank you
Sent from my BlackBerry 10 smartphone on the Rogers network.
From: Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca>
Sent: Friday, September 16, 2016 8:46 PM
To: Kaufman, Paul (TBS); Hatzis, Len (TBS)
Subject: RE: Pension Comparison - question and timelines confirmation

Paul/Len,

Not sure if it's feasible, but given the AG's focus on level of 'uncertainty' associated with the ability of the Province to benefit from the assets, if the analysis can also address how the plans differ in that regard as well, it would be very beneficial to our position.

N

From: Kaufman, Paul (TBS)
Sent: September 16, 2016 8:38 PM
To: Hatzis, Len (TBS); Murray Gold
Cc: Veinot, Cindy (TBS); Petsche, Nadine (TBS)
Subject: Pension Comparison - question and timelines confirmation

Hi Murray -

To confirm our discussion, you are going to provide a comparative legal/governance analysis of how the frameworks for the two Ontario pension plans we identified (OTPP and OPSEU) and the four BC plans we identified (municipal, teachers, college, public service) compare on the issue of the authority of the pension boards and the plan partners to determine the utilization of plan surpluses. Your preliminary thinking is that in Ontario this determination is left to the partners, while in BC either the boards or the partners can make this determination.

You expect that you can provide this analysis by Monday or Tuesday.

We've provided the relevant joint trust agreements for the plans noted above and you don't expect that you need further documentation from us to respond to this request, but you will let us know if any need arises.

Cindy, if the above is inconsistent with what you are looking for please advise.

Paul

Fw_ September 15 letter.rtf

From: Hatzis, Len (TBS) []
To: Steele, Jana [JSteele@osler.com]; Marin, Jon [jomarin@osler.com]; Rienzo, Douglas [DRienzo@osler.com]
CC: Kaufman, Paul (TBS) [Paul.Kaufman@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Fw: September 15 letter
Date: Saturday, September 17, 2016 08:11:55
Attachment 1: MOF letter.pdf

Hi Jana
Here is a letter (with attachments) that has relevance re the fmp. Thanks
Sent from my BlackBerry 10 smartphone on the Rogers network.

MOF letter.pdf

ONTARIO TEACHERS' PENSION PLAN

5650 Yonge Street
Toronto, Ontario, Canada
M2M 4H5

tel: 416-228-5900 or 1 877-812-7989
fax: 416-730-5349
www.otpp.com

September 15, 2016

Alex Killoch, Director
BPS Pensions Branch
Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto, Ontario
M7A 1Y7

Dear Alex:

As requested, we are outlining the annual process for providing actuarial and financial information about the Ontario Teachers' Pension Plan (Plan) to the Ministry of Finance. We are also providing information related to the funding valuation of the Plan and in particular, the discount rate setting process. Copies of various documents, correspondence and memos have been attached for reference purposes with applicable dates noted below.

Annual Process Related to the Province of Ontario Budget

Each December, the Ministry of Finance provides a request for information to the President and CEO of the Plan to assist in the preparation of the Ontario Budget. Specific assumptions to be used in the analysis are provided including return on investment, inflation, real rate of return and anticipated salary growth. The Province selects the best estimate assumptions in accordance with the Chartered Professional Accountants of Canada Public Sector Accounting Board Handbook. (December 11, 2015 request from the Province attached).

The external Plan actuary – Mercer – prepares the liability and current service cost calculations using the "projected benefit method, pro-rated on services" and economic assumptions are requested by the Province. Supporting information including contribution and benefit information is provided by the Plan. (January 26, 2016 correspondence from Mercer and the Plan attached).

Supplemental information was prepared by Mercer at the request of the Province in June of 2016 to assist in addressing inquiries from the Office of the Auditor General of Ontario. (June 17, 2016 Memo attached).

Annual Funding Valuation Process

On an annual basis, Mercer prepares a preliminary valuation for review by the Ontario Teachers' Pension Plan Board (Board). It is the Board's responsibility to decide key actuarial assumptions in close collaboration with the Plan actuary. The independent actuary must confirm that the

assumptions are independently reasonable and are appropriate in aggregate in accordance with the Canadian Institute of Actuaries Standards of Practice.

The annual assumption setting exercise is robust. The determination of the discount rate is informed by the Funding Management Policy (described below) and the Discount Rate Review process which reflects what the Plan's assets can reasonably be expected to earn over the long run less expenses and less provisions for adverse deviation (PFAD). The Plan takes into consideration two key PFADs: plan maturity and insufficient return. PFADs are set with reference to the demographic profile of the Plan, the risk tolerance and intergenerational fairness between members. A key challenge is the maturity of the Plan with the ratio of active members to pensioners being 1.4 to 1 with the ratio projected to decrease in the future. Longevity compounds this challenge as Teachers in Ontario live longer than the general Canadian population and their life expectancy continues to increase.

For the January 1, 2016 funding valuation (which will be filed with the regulatory authorities by September 30th), the nominal discount rate is 4.8% with an underlying real return of 2.75%. This real return takes into account PFADs of approximately 150 basis points.

Funding versus Accounting Valuations

The funding valuation assesses the Plan's long-term financial health to facilitate determination of future contribution rates and benefit levels. For the Plan, the cost method used is the aggregate method which allows the Plan to address funding surpluses and deficits through future benefits changes (eg. Conditional Inflation Protection (CIP)) and enables the Plan to factor in cash flows from future service. This differs from accounting standards which requires use of the projected benefit method prorated on services.

There are also differences in the assumption setting process. The Plan's assumption setting process for the annual funding valuation is noted above. Please refer to the attached Memo prepared by Mercer dated September 15, 2016, which outlines key methods and assumptions to be used to value pension plans per Canadian Public Sector Accounting Standards (PS3250).

Funding Management Policy

The Plan Sponsors (the Province of Ontario and Ontario Teachers' Federation) are jointly-responsible for two key decisions: a) what pension benefits the Plan will provide, and b) the contribution rate needed to ensure the Plan's benefits are fully funded over the long term. In doing so, the Sponsors negotiate the use of surplus funds and, when there is a funding shortfall, both share responsibility for eliminating it.

In March 2003, the Sponsors adopted a Funding Management Policy (FMP) as a supplement to the Partners' Agreement, with the objective to provide a guidance framework for decision making when there is a funding surplus or shortfall. A key component in the creation of the FMP was the concept of 'funding zones', each defined by a range. The funding zones provide a point of reference for whether action is required by the Sponsors, and if so, guidance is provided on how to use any surplus funds or resolve any shortfall – specifically, answering the question of when is it prudent to increase or decrease benefits, raise or lower contribution rates, or simply conserve assets for an uncertain time. While the FMP outlines preferred mechanisms

associated with its various funding zones, it is ultimately the Sponsors' responsibility to decide what actions to take.

In March 2015, a zone for Temporary Plan Improvements was added to the FMP, to allow for temporary contribution decreases, surplus distribution and/or benefit improvements (so long as they do not increase the long-term cost of the Plan) when assets exceed the projected cost of future benefits when valued using the Temporary Basis. Uses of surplus in this zone are paced, amortized over a period between three and 10 years, with an annual spending limit applied to amortization terms shorter than 10 years. The zone includes a provision that temporary improvements cease if a significant market event occurs. (FMP Framework and Summary attached).

As noted in Mercer's June 17th Memo, "should the plan earn future returns that are equal to the valuation discount rate adopted by the Province for financial statement reporting purposes, it is possible that some of the future contribution requirements could be reduced by agreement of the Sponsors as experience gains would be recognized in the funding valuation based on the assumptions currently used for funding purposes".

*****

We trust that the above information and various attachments provide a helpful overview of the annual process for providing financial information to the Ministry of Finance as well as the process in place for the annual funding valuation. Please do not hesitate to call if you have any questions or require further information.

Sincerely,

Barbara Zvan, FSA, FCIA, CERA
SVP, Strategy & Risk and Chief Investment Risk Officer
(416) 730-6364
Barbara_zvan@otpp.com

Cc: Ross Peebles
Joshua Paul
Rob Pomykacz
Allan Shapira
Mary Cover

Ministry of Finance

Income Security and Pension Policy Division

Office of the Assistant Deputy Minister
Frost Building South, 5th floor
7 Queen's Park Crescent East
Toronto ON M7A 1Y7
Tel.: 416 212-8073
Fax: 416 327-0760

Ministère des Finances

Division des politiques en matière de sécurité du revenu et de régimes de retraite

Bureau du sous-ministre adjoint
Édifice Frost Sud, 5e étage
7 Queen's Park Crescent East
Toronto ON M7A 1Y7
Tél.: 416 212-8073
Téléc.: 416 327-0160

Ontario

December 11, 2015

Mr. Ron Mock
President and Chief Executive Officer
Ontario Teachers' Pension Plan Board
5650 Yonge Street, Suite 400
Toronto, Ontario
M2M 4H5

Dear Mr. Mock:

In preparation for the 2016 Ontario Budget, I am writing to request actuarial and financial information, as at December 31, 2015, on the Teachers' Pension Plan (TPP) and the Teachers' Retirement Compensation Arrangement (TRCA). This information is required for calculating the Province's 2015-16 pension expense and pension liability.

To ensure that the information requested in this letter is consistent with the Province's best estimates (as required by the Public Sector Accounting Board [PSAB]), please use the following economic assumptions in your actuarial calculations for the requested TPP information.

Economic Assumption (annual rates)	Basis 1	Basis 2	Basis 3	Basis 4
Return on Investment	6.50%	6.25%	6.25%	6.00%
Inflation	2.25%	2.25%	2.00%	2.00%
Real Rate of Return	4.25%	4.00%	4.25%	4.00%
Salary Growth	2.25% for 2016 to 2019 and 3.25% thereafter	2.25% for 2016 to 2019 and 3.25% thereafter	2.00% for 2016 to 2019 and 3.00% thereafter	2.00% for 2016 to 2019, 3.00% thereafter

Despite the salary growth assumption above, please reflect in the valuation a 1% lump sum increase for the school year 2015-16, a 1% increase for the school year 2016-17 and additional 0.5% increase half-way through the school year 2016-17.

...2

We understand the Board may be preparing its financial statements based on International Financial Reporting Standards and Canadian Institute of Chartered Accountant Standard Section 4600. There has not been any change in reporting requirements under the Public Sector Accounting Board. Therefore, the actuarial and financial information we are requesting in this letter should be prepared in the same manner as has been provided to us in prior years.

Please provide the following actuarial and financial information with one set of calculations for each set of assumptions outlined in the table above. In these calculations for the TPP, please use the projected benefit method, prorated on services:

1. Actuarial present value (APV) of accrued benefit obligations, as at December 31, 2015. ***Basis 4 in last year's letter was used by the Province for 2015. Please include an APV reconciliation on that basis from December 31, 2014 to December 31, 2015 for all four bases.***

2. Actuarial value and market value of pension fund assets, as at December 31, 2015. The actuarial value of assets should be determined on the same basis as in prior years.

3. Interest on accrued benefits, cost of benefits accrued (separating out current period benefit cost, cost related to any plan amendments, transfers and other costs), actuarial adjustments, and the benefits paid (separate retirement pensions from other benefit payments) for the year ended December 31, 2015.

4. Contributions broken down by employee contribution, Province of Ontario contribution and other transfers for the year ended December 31, 2015 and the additional payments from the Province of Ontario with respect to "payments re foregone inflation adjustment" under subsection 5(2.1) of the *Teachers' Pension Act* for the year ended December 31, 2015. Please provide the same level of detail as would be disclosed in the "Contributions" note to the TPP's 2015 financial statements.

5. Return on investment, inflation and salary escalation assumptions that will be used in the TPP's 2015 financial statements.

6. Expected average remaining service life of active employees, as at December 31, 2015.

7. Net gain and loss for the year ended December 31, 2015 that would be subject to smoothing on the same basis as in prior years. Please also provide the same level of detail as in prior years.

...3

8. The "Schedule of Contributions and Interest Receivable from the Province of Ontario" (due in early January, 2016).

9. Number of pensioners and active members, as at December 31, 2015.

10. Please provide a brief, high level explanation of the source(s) of the actuarial gains and losses for 2015.

11. Please provide the 2016 service cost for all requested bases.

12. 2015 financial statements of the TPP and the TRCA as soon as they are available.

Please provide items 1 to 5 above for the TRCA based on what will be reported in the TRCA's 2015 financial statements. Note that we do not require that the information on the TRCA be based on the Province's economic assumptions.

Although the TPP has been amended to provide conditional inflation protection for service after December 31, 2009, the intention of the Partners is to provide 100% inflation protection to the extent possible. As such, please provide us with the actuarial calculation for #1 and #3 above assuming that inflation protection for post 2009 service will be provided at 100% and at 50% of the annual increase in the Consumer Price Index.

We require these estimates by **January 29, 2016.** Should you have any questions, please contact Mr. Rob Pomykacz at robert.pomykacz@ontario.ca, or by telephone at (416) 327-0156.

To expedite the preparation of Ontario's 2015-16 *Public Accounts*, I would also ask that you communicate by letter by April 30, 2016 whether, to the best of your knowledge, there were any events between December 31, 2015 and March 31, 2016, which would in your opinion, affect these valuation results in a material way.

Please forward all the information requested in this letter to:

Mark Rozic, Manager (Acting)
External Reporting Branch
Office of the Provincial Controller Division
Treasury Board Secretariat
2nd Floor, Office 260, Frost Building South
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel: (416) 325-8293
Fax: (416) 325-2029
E-mail: mark.rozic@ontario.ca

And to:

Alex Killoch, Director
BPS Pensions Branch
Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel: (416) 325-5724
Fax: (416) 212-8293
E-mail: alex.killoch@ontario.ca

Thank you for your cooperation in this matter.

Yours sincerely,

Leah Myers

c: Alex Killoch
Sanjeev Batra
Mark Rozic
Pauline Fong
Joshua Paul
Mary Cover
Rob Pomykacz
Bill Pelow

ONTARIO TEACHERS'
PENSION PLAN / RÉGIME DE RETRAITE DES ENSEIGNANTES ET DES ENSEIGNANTS

5650 Yonge Street
Toronto, Ontario, Canada
M2M 4H5

tel. 416-226-2700 or 1-800-668-0105
fax. 416-730-7807 or 1-800-949-8208
www.otpp.com

January 26, 2016

Mark Rozic, Manager (Acting)
External Reporting Branch
Office of the Provincial Controller Division
Treasury Board Secretariat
2nd Floor, Office 260, Frost Building South
7 Queen's Park Crescent
Toronto, Ontario M7A 1Y7

Dear Mr. Rozic:

I am responding to a letter dated December 11, 2015 from Ms. Leah Myers that requested actuarial and financial information about the Ontario Teachers' Pension Plan (registered pension plan - RPP) and the Retirement Compensation Arrangement (RCA) at December 31, 2015.

Items 1, 3 (except the benefit payment breakdown), 6, 10 and 11 are included in the enclosed letter from Mercer (Canada) Limited.

Item 2 - Market Value of Pension Fund Assets ($ millions)

Please note that we no longer use an asset smoothing method for our financial statements. As such, there is no separate "actuarial" value of assets.

Market value of assets at December 31, 2015	Not yet available

Item – 3(a) RPP Benefits Paid ($ millions)

Retirement Pensions	$ 5,056
Survivor Pensions	273
Disability Pensions	27
Lump Sum Death Benefits	71
Refunds	1
Commuted Value Transfers	74
Transfers to Other Plans	8
Family Law Value Transfers	27
Total	$ 5,537

Item – 3(b) RCA Benefits Paid

The RCA pension payments made in 2015 were $7.40 million and the RCA lump sum payments in 2015 were $4.87 million.

Item - 4(a) RPP Contributions ($ millions)

Members		
Current Service	$	1,580
Optional Credit		35
Total	$	1,615
Province of Ontario		
Current Service	$	1,568
Interest		37
Optional Credit		32
Total	$	1,637
Other Employers	$	33
Transfers from Other Plans		14
Total	$	47
Grand Total	$	3,299

Item 4(b) - RCA Contributions ($ millions)

Members	$	5.6
Province of Ontario		3.3
Other Employers		2.4
Total	$	11.3

Item 4(c) - Payments re: Foregone Inflation Adjustments

The foregone inflation amounts for 2014 payments which are part of the government billing for payment in January 2016 are as follows:

		Total		**Province of Ontario**
RPP	$	1,130,253	$	1,106,279
RCA		12,205		11,946
Total	$	1,142,458	$	1,118,225

Item 5 - Economic Assumptions	**RPP**	**RCA**
Discount Rate	3.25%	1.625%
Salary Escalation Rate	2.50%	2.50%
Inflation Rate	1.50%	1.50%
Real Rate	1.70%	0.125%

Item 7 - Net Gain and Loss on Actuarial Value of Assets

Not applicable. Please note that we no longer use an asset smoothing method for our financial statements. As such, there is no separate "actuarial" value of assets.

Item 8 - Schedule of Contributions and Interest Receivable ($ millions)

Contributions	$	3,157
Interest		51
Total	$	3,208

Item 9 - Number of Pensioners and Active Members as at December 31, 2015

Pensioners	133,000
Active Members	183,000

Item 12 – Financial Statements

Not yet available.

We will provide any outstanding information as soon as it is available. In addition, we will send an updated version of this letter if any of the information contained herein is subsequently changed.

Please do not hesitate to call if you have any questions.

Sincerely,

Mary Cover, FSA, FCIA
Director, Pension Strategy and Enterprise Risk
(416) 730-2976
mary_cover@otpp.com

cc: Alex Killoch – Ministry of Finance

Lise Houle
Principal

120 Bremner Boulevard, Suite 800
Toronto ON M5J 0A8
416 868 2039 Fax 416 868 7695
lise.houle@mercer.com
www.mercer.ca

MERCER

26 January 2016

Ms. Mary Cover
Director, Pension Strategy & Enterprise Risk
Ontario Teachers' Pension Plan Board
5650 Yonge Street
Toronto, ON M2M 4H5

Private & Confidential

Subject: December 31, 2015 Valuation Results Using the Province's Assumptions

Dear Mary,

As requested, we have provided you with information for the Ontario Teachers' Pension Plan (OTPP) on points 1, 3, 6, 10 and 11 in the December 11, 2015 letter from the Ministry of Finance to Mr. Ron Mock. As instructed in the Ministry letter, the following sets of assumptions have been used in calculating the liabilities as at December 31, 2015:

	Basis 1	**Basis 2**	**Basis 3**	**Basis 4**
Valuation discount rate	6.50%	6.25%	6.25%	6.00%
Inflation rate	2.25%	2.25%	2.00%	2.00%
Real valuation discount rate	4.25%	4.00%	4.25%	4.00%
Salary escalation rate	2.25% for the years 2016 to 2019, 3.25% thereafter	2.25% for the years 2016 to 2019, 3.25% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter

For each basis, all the other assumptions and the valuation methods are those used by the Ontario Teachers' Pension Plan Board in the December 31, 2015 valuation for financial statement purposes. This includes proposed demographic assumption changes as well as negotiated salary increases providing a 1% lump sum increase at September 1, 2015, a 1% increase at September 1, 2016 and a 0.5% increase half-way through the school year commencing September 1, 2016. The demographic assumptions were updated to reflect recent experience of Plan members related to retirement, termination of plan membership, re-

instatement of inactive members and increases in salaries related to experience. The changes to the demographic assumptions are described in the presentation material from our meeting with the Technical Committee on January 13, 2016. The remaining demographic assumptions are provided in our Report on the Actuarial Valuation for Financial Statement Purposes as at December 31, 2014. We expect that our report on the December 31, 2015 actuarial valuation will be finalized in March, 2016.

For the sake of clarity, we note that the assumed increases in the YMPE and maximum pension limits under the Income Tax Act are the same rates as the long-term salary growth rates noted for each of the four bases.

The Province has requested that we prepare the results assuming that inflation protection for post 2009 service will be provided at 100% and at 50% of the assumed inflation rate. In this letter we have included results using both of these alternative inflation protection levels. We note that at the time of preparing this letter, the Plan provides for 70% of conditional inflation protection for post 2009 service.

At the Province's request, the liabilities have been calculated using the "projected benefit method, pro-rated on services". In the calculations presented in this letter, we have used the projected benefit method, pro-rated on service with three attribution periods to reflect the different indexing provisions for service accrued to December 31, 2009, service accrued from January 1, 2010 to December 31, 2013 and service accrued from January 1, 2014. However, we note that the same level of indexing was applied to all service from January 1, 2010 to December 31, 2015 for purposes of calculating the liabilities provided in this letter (whether the results are based on 100% or 50% conditional indexing).

We have included information regarding the experience gain/loss incurred relative to salary growth during the year as well as the impact on the December 31, 2015 liabilities due to changing the rate of inflation and salary growth assumption in Bases 3 and 4 in our tables relative to the assumptions from Bases 1 and 2. We note that since the assumed increases in salaries determined by the Province are set equal to the assumed inflation rate plus 1%, we have not separately identified the changes in salary only without the corresponding changes in inflation.

The results as at December 31, 2015 are summarized in the following tables.

Results using 100% conditional indexing for post 2009 service (results in $ millions)

	Basis 1	Basis 2	Basis 3	Basis 4
Valuation discount rate:	**6.50%**	**6.25%**	**6.25%**	**6.00%**
Inflation rate:	**2.25%**	**2.25%**	**2.00%**	**2.00%**
Salary escalation rate:	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**
1. Actuarial present value (APV) of accrued pension benefits at December 31, 2014 using **Last Year's Basis 4**	$113,801	$113,801	$113,801	$113,801
2. Increase in the APV of accrued pension benefits				
Interest on the APV of accrued pension benefits	$7,310	$7,310	$7,310	$7,310
Current Service Cost (mid-year)	2,868	2,868	2,868	2,868
Contributions for optional credit	34	34	34	34
Repayment of refunds	0	0	0	0
Transfers from other plans	14	14	14	14
Change in valuation assumptions and methods:				
Change in demographic assumptions	350	350	350	350
Change in interest rate from Basis 1	0	4,142	4,142	8,309
	$10,576	$14,718	$14,718	$18,885
3. Decrease in the APV of accrued pension benefits				
Pensions paid	$5,356	$5,356	$5,356	$5,356
Refund of contributions	0	0	0	0
Lump sum payments and transfers	180	180	180	180
Salary experience gains	1,028	1,028	1,028	1,028
All other experience gains	552	552	552	552
Negotiated Salary Increases	1,161	1,161	1,161	1,161
Change in inflation rate and salary growth rates from Basis 1	0	0	3,829	3,829
Change in other actuarial assumptions and methods	46[1]	46	46	46
	$8,323	$8,323	$12,152	$12,152
4. Net increase in the APV of accrued pension benefits	$2,253	$6,395	$2,566	$6,733
5. APV of accrued pension benefits at December 31, 2015	$116,054	$120,196	$116,367	$120,534
6. Annual current service cost at January 1, 2016 (BOY)	$2,880	$3,058	$2,899	$3,079

[1] Change to commuted value assumption to value benefits payable upon termination

Results using 50% conditional indexing for post 2009 service (results in $ millions)

	Basis 1	Basis 2	Basis 3	Basis 4
Valuation discount rate:	**6.50%**	**6.25%**	**6.25%**	**6.00%**
Inflation rate:	**2.25%**	**2.25%**	**2.00%**	**2.00%**
Salary escalation rate:	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**
1. Actuarial present value (APV) of accrued pension benefits at December 31, 2014 using **Last Year's Basis 4**	$112,004	$112,004	$112,004	$112,004
2. Increase in the APV of accrued pension benefits				
Interest on the APV of accrued pension benefits	$7,182	$7,182	$7,182	$7,182
Current Service Cost (mid-year)	2,508	2,508	2,508	2,508
Contributions for optional credit	34	34	34	34
Repayment of refunds	0	0	0	0
Transfers from other plans	14	14	14	14
Change in valuation assumptions and methods:				
Change in demographic assumptions	322	322	322	322
Change in interest rate from Basis 1	0	3,975	3,975	7,990
	$10,060	$14,035	$14,035	$18,050
3. Decrease in the APV of accrued pension benefits				
Pensions paid	$5,356	$5,356	$5,356	$5,356
Refund of contributions	0	0	0	0
Lump sum payments and transfers	180	180	180	180
Salary experience gains	979	979	979	979
All other experience gains	545	545	545	545
Negotiated Salary Increases	1,104	1,104	1,104	1,104
Change in inflation rate and salary growth rates from Basis 1	0	0	3,461	3,461
Change in other actuarial assumptions and methods	36[2]	36	36	36
	$8,200	$8,200	$11,661	$11,661
4. Net increase in the APV of accrued pension benefits	$1,860	$5,835	$2,374	$6,389
5. APV of accrued pension benefits at December 31, 2015	$113,864	$117,839	$114,378	$118,393
6. Annual current service cost at January 1, 2016 (BOY)	$2,523	$2,671	$2,574	$2,727

[2] Change to commuted value assumption to value benefits payable upon termination

We have the following comments on the results:

- Our valuation of the actuarial present value of the accrued pension benefits as at December 31, 2015 and the 2016 current service costs are based on membership data as at August 31, 2015. The actuarial present value of accrued pension benefits as at August 31, 2015 is then extrapolated forward to December 31, 2015, reflecting expected cashflows and the actual inflation adjustment as at January 1, 2016 of 1.30% for pre-2010 service and 0.91% for post-2009 service. The 2015 mid-year current service is based on membership data as at August 31, 2014. A summary of the membership data as at August 31, 2015 was included with our email of October 23rd, 2015 to Glen Tunney.

- We understand that the Province adopted Last Year's Basis 4 in establishing the actuarial present value of accrued pension benefits as at December 31, 2014. This is the same as Basis 1 for the current year.

- We have assumed that any change in the Province's assumptions (i.e. nominal and real discount rates, inflation rate, and salary escalation rate would occur at December 31, 2015).

The Expected Average Remaining Service Lifetime (EARSL) of active employees at August 31, 2015 and estimated for December 31, 2015, is 15.3 years. The increase in the EARSL from the prior year is primarily attributable to the change in assumed termination and retirement rates.

The net experience gain incurred on the plan liability since the prior year was primarily attributable to the lower than expected level of inflation for the January 1, 2016 indexing. Other experience gains and losses were relatively small.

The figures presented in this letter exclude the Ontario Teachers' Retirement Compensation Arrangement ("OTRCA"), which provides benefits to members that are in excess of those permitted to be provided from the registered pension plan. The Province has requested information on the OTRCA based on what will be reported in the OTRCA's 2015 financial statements, and does not require calculations on any other basis.

While the actuarial demographic assumptions used to estimate liabilities for the Plan represent the Ontario Teachers' Pension Plan Board's best estimate of future events and the economic assumptions are as provided by the Province, and while in our opinion the assumptions used for the valuation are appropriate provided the Province selected the economic assumptions in accordance with the Chartered Professional Accountants of Canada Public Sector Accounting Board Handbook ("PSAB Handbook"), the Plan's future experience will inevitably differ, perhaps significantly, from the actuarial assumptions. Any differences between the actuarial

assumptions and future experience will emerge as gains or losses in future valuations, and will affect the financial position of the Plan at that time.

We have tested the data for reasonableness and consistency, and in my opinion, the membership data on which the valuation is based are sufficient and reliable for the purpose of the valuation. In my opinion, the calculations have been made in accordance with my understanding of the reporting requirements under the PSAB Handbook and this report has been prepared, and, my opinions given, in accordance with accepted actuarial practice in Canada.

If you have any questions, please do not hesitate to call.

Sincerely,

Lise Houle

Copy:
Scott Clausen, Mercer
Jason Lipping, Mercer
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120 Bremner Boulevard, Suite 800
Toronto, Ontario M5J 0A8
Fax +1 416 868 7555
Lise.houle@mercer.com
www.mercer.ca

MEMO

TO: Mary Cover, Ontario Teachers' Pension Plan
DATE: 17 June 2016
FROM: Lise Houle
SUBJECT: Ministry of Finance Request for Supplemental Accounting Results
COPY: Scott Clausen, Jason Lipping, Mercer

As a follow-up to the accounting results we provided to you with our letter of January 26th, 2016, determined using the actuarial assumptions provided by the Ministry of Finance, we understand that the Ministry has requested supplemental information from the Ontario Teachers' Pension Plan as the Ministry addresses inquiries from the Office of the Auditor General of Ontario.

In particular, the Ministry has requested the following information relating to the Ontario Teachers' Pension Plan, using Bases 3 and 4 described in our January 26th letter:

- Present value of future current service accruals,
- Present value of future basic contributions, and
- Present value of future supplemental contributions

The requested information, calculated as at August 31, 2015 and rolled forward to December 31, 2015 is as follows:

	Basis 3	**Basis 4**
Valuation Discount Rate	6.25%	6.00%
Inflation Rate	2.00%	2.00%
Real Valuation Discount Rate	4.25%	4.00%
Salary Escalation Rate	2.00% for the years 2016 to 2019, 3.00% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter
PV of future service accruals	$36,767 million	$39,563 million
PV of future basic contributions	$36,073 million	$36,826 million
PV of future supplemental contributions	$2,888 million	$2,924 million

The present value of future service accruals is calculated as the difference between the actuarial present value of total projected pension benefits (ie aggregate liabilities) less the actuarial present value of accrued pension benefits as at December 31, 2015. The benefits used in our calculations reflect 100% conditional indexing for both pre-2010 and post-2009 service. The actuarial present

value of accrued pension benefits as at December 31, 2015 are those provided in our January 26th letter while the actuarial present value of total projected pension benefits are calculated using the same approach, but captures all projected service to date of expected decrement.

The actuarial present value of basic contribution reflects both expected basic employee and employer contributions to be paid to date of assumed decrement.

The actuarial present value of future service accruals and of basic contributions only considers current active and inactive members of the Ontario Teachers' Pension Plan. In keeping with the approach used for the funding valuation, the present value of future supplemental contributions is determined on an open-group basis and reflects scheduled contributions to December 31, 2026.

It is our understanding that the province intends to use these figures to perform a high level test to consider if there should be a limit applied to the asset/surplus held as at December 31, 2015. We note that, should the plan earn future returns that are equal to the valuation discount rate adopted by the Province for financial statement reporting purposes, it is possible that some of the future contribution requirements could be reduced by agreement of the Sponsors as experience gains would be recognized in the funding valuation based on the assumptions currently used for funding purposes.

For more details on the actuarial assumptions, methods and data used in our calculations, please refer to our January 26th letter. The demographic assumptions are summarized in our Report on the Actuarial Valuation for Financial Statement Purposes as at December 31, 2015.

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120 Bremner Boulevard, Suite 800
Toronto, Ontario M5J 0A8
Fax +1 416 868 7555
scott.clausen@mercer.com
www.mercer.ca

MEMO

TO: Mary Cover, Ontario Teachers' Pension Plan
DATE: 15 September 2016
FROM: Scott Clausen, Mercer
SUBJECT: Canadian Public Sector Accounting Standards (PS3250)

As discussed, the purpose of this memo is to provide section references from Canadian Public Sector Accounting Standards (PS 3250) that refer to the selection of methods and assumptions to be used to value pension plans for the purpose of the province's financial reporting. All Section references shown in this memo refer to Sections from PS3250.

Actuarial Cost Method:

.029
The projected benefit method prorated on services should be used to attribute the cost of retirement benefits to the periods of employee service.

.030
When a retirement plan provides benefits that accrue in a non-uniform manner, the projected benefit method prorated on services may need to be adjusted to reflect the manner in which retirement benefits are earned by employees. For example, a pension plan formula may state that the pension benefit accrues at one percent of salary for the first 15 years and at two percent of salary for the final 20 years. In this circumstance, the prorating of the total estimated benefit to each accounting period would be adjusted to reflect the rates at which pension benefits are earned in that 35-year period.

.032
In other retirement plans, regular benefit increases for inflation protection may be provided even when such protection is not promised in a contractual agreement or in legislation. For those plans, careful analysis and professional judgment are needed to determine the substance of a government's obligation. If a regular pattern of benefit increases can be established over a reasonable period, it may be appropriate to incorporate the cost of such inflation protection in the cost of retirement benefits earned to the accounting date and reported as an accrued benefit obligation.

Asset Valuation:

.035

When determining a government's retirement benefit liability and expenditure / expense, plan assets would be valued at market-related values. Under this method, plan assets are recorded at market value or they are adjusted to market value over a period not to exceed five years. Values adjusted to market closely approximate current economic value in a manner that can minimize short-term fluctuations. Market-related values would be used because they are objective and verifiable. Once a basis of valuation is chosen it would be applied consistently.

Actuarial Assumptions:

.042

Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts.

.044

The actuarial assumptions underlying the valuation of the retirement benefit liability and expenditure / expense would be internally consistent. For example, when a government determines its discount rates by reference to its plan asset earnings, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the short-term forecast of rates of return on assets currently held in the fund. When a government determines its discount rates by reference to its cost of borrowing, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the specific rates of interest and the periods committed to by the government on the amounts borrowed.

Limit on Accrued Benefit Asset:

.050

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

.053

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

.054

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

.055

The objective of the Recommendation in paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

.056

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

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

Actuarial Gains and Losses:

.061

Actuarial gains and losses would be amortized over a reasonable future period because of their tentative nature and because further adjustments will likely be required in the future. A reasonable future period is the **expected average remaining service life of the related employee group**. Amortization may commence in the period following the determination of the adjustment. Actuarial gains and losses would be determined on a market value basis or a basis adjusted to market value, consistent with paragraph .035.

Past Service Costs:

.066

The cost of plan amendments related to prior period employee services should be accounted for in the period of the plan amendment.

Joint Defined Benefit Plans:

.079

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

.081

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

FUNDING MANAGEMENT POLICY (FMP) FRAMEWORK DESCRIPTION

Valuation Basis

Assets = 110% of Liabilities valued at interest rates + 0.5%

Zone:	**Permanent Plan Improvements**
Mechanism:	**Improve benefits as negotiated**
Funding Risk:	Plan is essentially fully funded at Government of Canada long bond rates. Funding security is desired to ensure the Plan can support these benefits continually in the future. The impact of new teachers is important as they will create losses.

That is, Assets ~ 133% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.25%

Zone:	**Temporary Plan Improvements**
Mechanism:	**Improve benefits or lower contributions as negotiated[1]**
Funding Risk:	Plan is well funded and can afford changes that temporarily provide a benefit enhancement (as long as it does not create a long term cost) and/or lower the contributions being paid into the Plan.

[1] Amortization period used to determine temporary benefit

That is, Assets ~ 107% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.55%

Zone:	**Fully Funded (Do Nothing)**
Mechanism:	**Maintain Base Benefits and Contributions**
Funding Risk:	Plan is adequately funded to provide base benefits supported by the base contributions. Given the volatility of market factors and the numerous assumptions in the funding valuation, "fully funded" is considered a range.

Zone:	**Additional Support Required From Current FMP Levers**
Mechanism:	**Raise Contribution Rates and/or Invoke Conditional Inflation Protection as negotiated**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions. An increase to the contribution rate (within FMP maximum) and/or a decrease to the level of indexing being provided are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Zone:	**Additional Support Required From New/Additional Changes**
Mechanism:	**Negotiate other plan changes**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions and CIP is fully invoked and contribution rates are increased to maximum outlined in FMP. Plan changes are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
Application (Article I):	**Section 1.01 and 1.02** ▪ Requires the Board to use Board's "best estimates assumptions," including a margin for adverse deviation in the case of the discount rate. ▪ Sets out what best estimates economic assumptions may be based on. ▪ Requires the Board to maintain indices to record inflation adjustments for post-2009 service. **Sections 1.03 and 1.04** ▪ If the Board uses a discount rate different from that outlined in the FMP and this discount rate is more penalizing (that is, produces a larger deficit or a smaller surplus), the FMP becomes void in 12 months unless both Partners notify the Board otherwise. These sections serve as an "exit" provision for the Partners. **Section 1.05** sets out under what circumstances each section of the FMP applies. **Section 1.06** limits surplus distributions or contribution decreases to those permitted by law. **Section 1.07** makes temporary improvements conditional on not having a restoration basis deficit.
Definitions (Article II):	**Section 2.01** Defines key terms, including: ▪ Basic contributions (contributions as per Sch.1 on January 1, 2012), which is used throughout the FMP as the target contribution rate (10.4% on earnings up to the YMPE/12% above the YMPE). ▪ Run-rate benefits (benefits as per Sch.1 on January 1, 2009), which include 100% inflation protection and assume basic contributions. ▪ Reference Rate (rate chosen by the Board representing Government of Canada nominal and real return bonds, which may be based on market or smoothed data; has recently been 3 year smoothed nominal and real return bonds). ▪ Remaining amortization value (difference between the temporary improvement value and the commitment value). ▪ Temporary improvement value (present value of a temporary improvement amortized over 3-10 years; if amortized over fewer than 10 years, improvement for a year is limited to the amount of basic contributions paid during a year).
Restore basic contributions and benefits (Article III):	**Section 3.01** ▪ Restoration basis is used (*reference rate* + 1.55%). ▪ Defines assets (refers to PBA Regulations) and current and revised liabilities. **Section 3.02** ▪ Sets out that current and revised liabilities are calculated using the restoration basis, plus an adjustment. The phrase "plus an adjustment" is used throughout the FMP and reflects the fact that the Board often files using a basis that is higher than required under the FMP. **Section 3.03** ▪ Outlines how indexing is accounted for in the valuation (that is, level of indexing provided in current filing zone continues).
Restoration Basis: *Surplus* (Article III continued)	*Sections 3.04 to 3.08 apply when surplus exists using the restoration basis and current contributions are higher than target, partial indexing (for previous years or go forward) exists or other benefits have been reduced.* **Section 3.04** Sets conditions under which sections 3.05-3.08 apply: ▪ If Assets > Liabilities (surplus reported); and ▪ Current contributions > Basic contributions (i.e., contributions are above long-term target level); or ▪ Current Benefits < Run-Rate Benefits (i.e. contributions are above long-term target level or benefits are below the long-term target level). **Section 3.06** Sets out the order of how to restore past benefit reductions or contribution increases: ▪ Actions can consist of increasing benefits to run-rate (long-term target) including prospective restoration or lowering contributions to basic (target) or a combination. ▪ First, increase go-forward indexing to 50% for post-2013 service period, then to 100% on all post-2009 service periods. Second, restore current pension amounts to run rate level, as much as possible, starting with the years where indexing was less than 50% until all years of partial indexation are restored to the same level and then restore to 100% for all service periods. ▪ Partners reserve the right to reconsider order in the future. **Section 3.07** A number of conditions apply after a decision: ▪ Assets equal to or greater than revised liabilities (i.e. no deficit created); ▪ Inflation indexing restored to no more than if 100% of inflation was provided;

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	▪ Inflation indexing restored to no less than current level (i.e. can't lower prior inflation indexing given); ▪ The value of revised benefits needs to be between current and run-rate benefits (similarly, contributions must be between current and target). **Section 3.08** (Expires December 30, 2017) Sets out the limits from the 2013 Term Sheet (commonly known as the JSPP Agreement) with respect to escalated adjustments and benefit improvements: ▪ Escalated adjustments if assets are greater than 100% of the current liabilities (and not below 100% after). ▪ Benefit improvement or restoration if net assets available for benefits are greater than 105% of the current (unsmoothed) liabilities (and not below 105% after).
Restoration Basis: *Deficit* (Article III continued)	*Sections 3.09 to 3.14 apply when the liabilities are greater than the assets using the restoration basis; thus the Partners must raise contribution rates, lower the amount of indexing and/or decrease other benefits.* **Section 3.09** Sets conditions under which Sections 3.10 to 3.14 apply: ▪ If Current liabilities > Assets (i.e., deficit reported). **Section 3.11** Sets out that deficit can be eliminated by changing contributions or benefits provided that: ▪ Assets are equal to or greater than revised liabilities; and ▪ Revised member contributions are no more than 15% (above YMPE). **Section 3.12** The Partners can agree to change benefits or contribution level as long as: ▪ Partners have entered into a written agreement governing the manner in which contributions by the Minister and the Employers will be adjusted to offset any reduction in benefits; and ▪ No indexing granted gets taken away. **Section 3.13** Outlines the current intention that member contributions will be increased up to 15% (above YMPE) before benefits are reduced or less than full indexing is provided. **Section 3.14** Sets out the limits with respect to the 2013 Term Sheet regarding employer contribution increases.
Funding Zone: Temporary (Article IV):	**Section 4.01** ▪ Temporary basis is used (*reference rate* + 1.25%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent). - Current liabilities (liabilities including the greater of current and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Revised liabilities (liabilities including the greater of revised and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus). **Section 4.02** Sets out that the liabilities are calculated using the temporary basis, plus an adjustment. *Sections 4.03 to 4.06 apply when the plan has a surplus using the temporary basis; that is, there is surplus available for improving benefits, decreasing contributions or distributing surplus, all on a temporary basis. The surplus spend is amortized over a period of three to ten years, at the partners' choice. If amortization period is less than ten years, the annual spend limit is the amount of basic contributions for a year.* **Section 4.03** Sets out conditions under which Sections 4.04 and 4.05 apply: - If assets > liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided. **Section 4.04**

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	The Board reports the commitment value (the amount of surplus that can be used to provide a temporary improvement). **Section 4.05** The Partners can agree to temporary improvements so long as after the change, assets over revised liabilities are equal to or greater than zero. **Section 4.06** provides a requirement for a side agreement setting out how Minister contributions are adjusted if there is a surplus distribution or temporary improvement of benefits.
"Do Nothing" Zone (Article IV continued):	*Sections 4.07 to 4.09 apply if assets are equal to or less than current liabilities using the temporary basis; that is, if there is a deficit using the temporary basis.* **Section 4.09** States that the Partners will not provide new improvements if there is a temporary basis deficit. That is, the Partners will do nothing, and Article III (restoration basis) will apply. However, no actions result from move to restoration because contributions and indexing are already at run-rate in order to be in temporary zone. The Partners could, however, have to file a valuation (using the restoration basis) if the filing schedule required a filing.
Funding Zone: Distributions (Article V):	**Section 5.01** ▪ Distribution basis is used (*reference rate* + 0.5%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent) - Liabilities (includes remaining amortization value) - Current targeted funding amount - Revised targeted funding amount - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus) **Section 5.02** Sets out that the liabilities are calculated using the distribution basis, plus an adjustment. *Sections 5.03 to 5.05 apply when the plan has a surplus using the distribution basis; that is, there is usable surplus for improving benefits above run-rate permanently or decreasing contributions below target level permanently.* **Section 5.03** Sets out conditions under which Sections 5.04 and 5.05 apply: - If Assets > 110% of Liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.05** The Partners can agree to change benefits or contributions so long as after the change assets remain greater than 110% of the liabilities and a side agreement has been entered into to set out how Minister contributions are adjusted if there is a surplus distribution or temporary improvement of benefits. *Sections 5.06 to 5.08 apply when the plan has a funding ratio that is at least 100% but less than 110% and valued using contribution rates at the basic or target level, full indexing provided prospectively and benefits fully restored.* **Section 5.06** Sets out the conditions under which Sections 5.07 and 5.08 apply: ▪ If Assets ≤ 110% of Liabilities; and ▪ Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and ▪ Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and ▪ Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.08** If the conditions in Section 5.06 are satisfied, there is not sufficient surplus to provide a permanent improvement; therefore, Article IV will apply to determine whether there is surplus using the temporary basis.

Subject	Summary of Provisions
Post-December 30, 2017 Valuations (Article VI):	*This section articulates at a high level the use of the surplus credits (earned pre-January 1, 2018) after December 30, 2017. OTF earns surplus credit for any unmatched forgone inflation (i.e., inflation indexing less than 50%) prior to January 1, 2018 or via other benefit reductions made before January 1, 2018. See the JSPP Agreement for more detail.* **Section 6.01** ▪ Restoration basis is used (reference rate + 1.55%). ▪ Defines: - Assets (PBA regulations) - Current Liabilities - Revised Liabilities **Section 6.02** Provides overriding provision for post-December 30, 2017: for valuations where assets are greater than current liabilities, Section 6.03 applies (with reference to the 2013 Term Sheet). **Section 6.03** Sets out the use of surplus credits: ▪ OTF has first call on surplus up to a limit;
Valuation frequency and filing (Article	*This section reinforces an earlier section of the Partners' Agreement that specifies that it is the Partners' joint decision whether to file (other than in a required filing year).* ▪ Partners' decision when to file. ▪ Partners will notify the Board within 7 months of valuation date.
Arbitration (Article VIII):	Refers to Arbitration already in prior section of the Partners' Agreement.
Limitations (Article IX):	FMP does not apply for changes required by law or for changes that increase the liabilities by less than 0.5% or for changes that use the $76m in section 60 *(Note $76m was utilized with January 1, 2008 filing).*

Fw_ Share the Pain.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Fw: Share the Pain
Date: Wednesday, September 21, 2016 16:31:46
Attachment 1: image001.png
Attachment 2: image003.png

From: Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>
Sent: Wednesday, September 21, 2016 4:18 PM
To: Petsche, Nadine (TBS); Veinot, Cindy (TBS)
Cc: Paul, Joshua (EDU); Roberto, Nicole (EDU); Pomykacz, Rob (MOF)
Subject: Share the Pain

Hello Nadine

The Ontario Teachers' Pension Plan has provided the following explanation regarding the calculation of the $4.3 billion reduction in "share the pain" contributions that arose as a result of the Partner's decision to use $8.6 billion of the January 1, 2016 surplus.

Please let me know if you have any questions.

Alex

Alex Killoch

Director, Broader Public Sector Pensions Branch

Ministry of Finance

416 325-5724

Alex.Killoch@Ontario.ca

From: Mary Cover [mailto:Mary_Cover@otpp.com]
Sent: Wednesday, September 21, 2016 3:55 PM
To: Killoch, Alex (MOF)
Cc: Barbara Zvan; Paul, Joshua (EDU); Roberto, Nicole (EDU); Pomykacz, Rob (MOF)
Subject: RE: Share the Pain

Dear Alex,

As requested and further to our conversation this afternoon, the purpose of this email is to outline the change in the present value of the future "share the pain" contributions from the January 1, 2016 preliminary valuation results of $6.6B to the January 1, 2016 filed results of $2.3B – i.e., a reduction of $4.3B.

Conditional Inflation Protection (CIP) is a key funding lever for the Ontario Teachers' Pension Plan (OTPP). When CIP is invoked, benefits earned subsequent to December 31, 2009 are subject to inflation protection levels below 100%. CIP levels are established when a funding valuation report is filed with the regulators. The level remains unchanged until a subsequent valuation is filed at which time the plan sponsors may decide to increase or decrease the percentage. This decision is informed by the funded status of the plan as at the valuation date.

In the January 1, 2016 preliminary valuation, CIP levels were 70% (in accordance with the most recently filed valuation report). The reduction in liabilities due to providing less than 100% inflation protection was $6.6B. The vast majority of this amount was in respect of active plan members. As a reminder, the OTPP utilizes an aggregate valuation funding method where the liabilities include future pension benefits in respect of both service accrued to date and service that is projected to be earned in the future. This valuation method recognizes the potential impact of reducing CIP levels below 100% on not just service from December 31, 2009 to the valuation date but also

on service projected to be earned in the future for current plan members. As an example, the valuation results assume that a member who joined the plan in 2015 will receive 70% inflation protection on the full pension entitlement they will eventually earn over their future career and that this reduction will apply each and every year for the remainder of their lifetime.

For every dollar that a member forgoes in inflation protection, the province and other employers contribute an extra dollar to the pension plan – i.e., their share the pain payment. Thus, for the 1.1.2016 preliminary valuation, given the present value of benefits to reflect less than 100% indexing for service earned after 2009 was $6.6B, the present value of future share the pain contributions was also $6.6B.

The plan sponsors chose to file the January 1, 2016 valuation using some of the preliminary surplus to increase the level of inflation protection from 70% to 90%. As a result, the reduction in liabilities due to providing less than 100% inflation protection decreased to $2.3B as did the present value of future share the pain contributions. Overall, the effect was an increase in liabilities of $4.3B and a corresponding decrease in the present value of future projected share the pain contributions of $4.3B.

It's worth noting that for benefits earned after 2013, share the pain payments are limited to the first 50% of forgone inflation protection. It's also worth noting that approximately 98% of the share the pain payments come from the Province – the remainder coming from other employers. Current annual share the pain contributions are significantly smaller as these contributions only apply to retirees that are in receipt of pensions and only in respect of the portion of their pension that was earned after December 31, 2009.

Please let me know if you have any questions or would like further elaboration.

Regards, Mary

Mary Cover, FSA, FCIA
Director, Pension Strategy & Enterprise Risk
mary_cover@otpp.com

Direct 416-730-2976
www.otpp.com

Ontario Teachers' Pension Plan
5650 Yonge Street, Toronto, Ontario M2M 4H5, Canada

http://www.otpp.com/

image001.pdf

image003.pdf

ONTARIO TEACHERS'
PENSION PLAN

Fw_ Your Scan job has arrived..rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: Your Scan job has arrived.
Date: Tuesday, September 20, 2016 09:36:00
Attachment 1: NuanceScanDoc_09_20_16_09_34.pdf

Hi Nadine,

Please see the scanned signed SOW for your records

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca
----- Forwarded by Lucy Durocher/CA/ABAS/PwC on 09/20/2016 09:35 AM -----

From: DoNotReply@pwc.com
To: ldurocher002@casmtp.pwcinternal.com
Date: 09/20/2016 09:34 AM
Subject: Your Scan job has arrived.

Your Scan to My Email task has completed successfully.

Your completed document is attached here.

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NuanceScanDoc_09_20_16_09_34.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective September 16, 2016.

PricewaterhouseCoopers LLP (the "Vendor" or "PwC") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client" or the "Province") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of March 22, 2016 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$100,000.00, excluding HST.

4. *Project Start Date:* September 16, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide accounting advice (the "accounting advisory services") regarding the acceptability of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards. The accounting advice may include:

   - Review of background information, position papers developed by the Client or third parties that have been engaged by the Client to draft accounting positions on accounting for the recognition and measurement of pension assets for jointly-sponsored pension plans, and other supporting information.
   - Provide written or oral comments on draft position papers as provided by the Client with respect to the application of Canadian Public Sector Accounting Standards.
   - Participation in discussions with internal and external stakeholders and other parties as directed by the Client.

   During the course of this project, the Client will provide to PwC a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements with the Client's auditor. If an accounting opinion is to be provided, the Client's auditor will confirm to us in writing that the information the Client

has provided to PwC is complete and consistent with their knowledge of the facts and circumstances of the specific transaction.

If requested to by the Client during the course of the project, the Vendor shall provide an accounting opinion (the "accounting opinion"), prepared in accordance with Section 7600, *Reports on the application of accounting principles* of the CPA Canada Handbook – Assurance ("Section 7600"), regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards.

Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting advice or accounting opinion (if applicable), including discussions with the Office of the Auditor General.

The Client agrees that any accounting advisory services are solely for the information and use of the Client. Subject to the obligations in Article 27 (Privacy) of the Master Agreement and as required by law by the Client's independent auditors, the Client agrees that any written work product of PwC will not be made available to any other persons or entities. An accounting opinion prepared in accordance with Section 7600 will, in compliance with Canadian GAAS, include restriction of use language identifying the parties to whom use is restricted and a statement that the report is not intended to be and should not be used by anyone other than the specified parties or for any other purposes. However the Client may provide access to PwC's observations and an accounting opinion prepared under Section 7600 (if applicable) to the Client's independent auditors solely for their informational purposes. Except as provided for in the preceding sentence, the Client agrees to seek and obtain the Vendor's written consent before including our accounting opinion (if applicable) or referring to the Vendor in any document disclosed to third parties, including disclosure of a summary of the accounting opinion or publication of the opinion in documentation that may be accessible to or intended for the public. The Vendor may, in their own discretion, waive the requirement to obtain written consent. The Client agrees that prior to or as part of providing their independent auditors with any written work product of PwC, including an accounting opinion prepared under Section 7600, the Client will notify its independent auditors that it is PwC's desire to be notified of, and to consent to, the disclosure of any PwC written work product or reference to any PWC work product in any materials to be disclosed to third parties. PwC agrees that the Client's obligation is only to notify its independent auditors of PwC's desire to be notified about, and to consent to, disclosure, and that the Client is not making any representation or warranty that its independent auditors will notify PwC or seek PwC's consent.

Acknowledgements and agreements

The Client acknowledges and agrees to the following:

a. The performance of the accounting advisory services does not constitute an engagement to provide audit, compilation, review or attest services in accordance with professional standards issued by the Chartered Professional Accountants of Canada ("CPA Canada") and, therefore, PwC will not express an opinion or any other form of assurance with respect to the accounting advisory services.
b. The accounting advisory services and accounting opinion (if applicable) to be provided do not include the delivery of any verbal or written advice on the application of accounting principles to a hypothetical transaction.
c. This engagement cannot be relied on to disclose internal control deficiencies, errors or fraud, should they exist.

d. PwC has no responsibility for updating the accounting advisory services or accounting opinion or for performing any additional services, except as agreed to in writing with the Client.
e. The Client's purpose for engaging PwC to perform the accounting advisory services is to supplement management's own technical accounting resources in performing accounting analysis and to assist management in making its determination as to the application of accounting principles and not to obtain an opinion from PwC as to such application, unless an accounting opinion is requested by the Client.
f. The Client shall be solely responsible for, among other things: (a) making all management decisions and performing all management functions; (b) designating one or more individuals who possess suitable skill, knowledge and/or experience, preferably within senior management to oversee the accounting advisory services (c) evaluating the adequacy and results of the accounting advisory services; (d) accepting responsibility for the results of the accounting advisory services; and (e) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities.
g. All management decisions and final conclusions reached in connection with the accounting advisory services will be the responsibility of the Client. PwC will not perform any management functions, make management decisions, or perform in a capacity equivalent to that of an employee of the Client.
h. PwC has no responsibility related to the Client's accounting or disclosure conclusions, whether or not such conclusions of the Client are related to the accounting advisory services and PwC has no responsibility for any disagreements between the Client and its independent auditor related to the Client's accounting.
i. The Client will be solely responsible for all decisions regarding the accounting treatment of any item or transaction and acknowledges that the accounting advisory services do not include the recording of any amounts in the Client's books or records. All amounts derived from the performance of the accounting advisory services will be reviewed and approved by, and will be the responsibility of, the Client's management.
j. The nature, scope and design of the accounting advisory services and the accounting opinion are solely the responsibility of the Client. PwC will rely, without independent verification, on the facts, information and assumptions provided by the Client. PwC will make no representation nor provide any assurance with respect to the adequacy of the services for the Client's purposes. Furthermore, PwC has no responsibility to advise the Client of other procedures that might be performed.
k. The Client will be solely responsible for providing accurate and complete information requested by PwC. PwC has no responsibility for the accuracy or completeness of the information provided by or on behalf of the client.
l. PwC's accounting and technical assistance will be based on the existing public sector generally accepted accounting principles. Should those generally accepted accounting principles be amended, superseded or revised in any manner, PwC's advice might change. PwC has no responsibility to inform the Client of any changes in generally accepted accounting principles that may occur after the completion of the engagement or any other oral or written work product prepared hereunder that would impact PwC's advice on the appropriate application of generally accepted accounting principles or to update its recommendations or any other oral or written work produce to take any such changes into account.
m. This engagement does not create a relationship between PwC and any person or party other than the Client. This engagement is not intended for the express of implied benefit of any third party.

n. The Client will identify an appropriate individual to serve as the project manager, including overseeing the accounting advisory services.

7. *Ownership and Licences* - **Attachment D** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be Lucy Durocher who is the engagement leader.

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Charges On Per Diem Rate Basis*– The Vendor and the Client agree that Work performed under this Statement of Work will be charged on a Per Diem Rate basis. The Per Diem Rate will vary, based on the nature of the final deliverable, as follows:

Nature of final deliverable	Per Diem Rate	Service Category	Estimated hours	Per Diem Rate
Accounting Advisory	General Consultant, Level 2	Service Category 2	20-25	$390/hour
Accounting Opinion	General Consultant, Level 2	Service Category 2	30-35	$990/hour

13. *Billing and Payment Process* – The Vendor shall invoice the Client in accordance with the requirements of the Master Agreement. Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	Individual's Role and Experience Level	Service Category	Per Diem Rate
Lucy Durocher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Martin Boucher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Sean Cable (or alternative as agreed to by the Client)	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"
Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client: Treasury Board Secretariat,
Office of the Provincial Controller Division
Branch: Accounting Policy and Financial Reporting

Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Clients designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all Confidential information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

18. *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**PricewaterhouseCoopers LLP, PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2**
Vendor Representative:	**Lucy Durocher**
Telephone number:	**416-869-2311**
E-mail:	**Lucy.durocher@ca.pwc.com**
Backup Vendor Representative:	**Martin Boucher**
Telephone number:	**514-205-5415**
E-mail:	**Martin.boucher@ca.pwc.com**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: N. Petsche

Name: Nadine Petsche

Title: Director, Accounting Policy & Financial Reporting

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature: PricewaterhouseCoopers LLP

Name: LUCY DURCHER

Title: PARTNER

I have the authority to bind the Vendor.

Fw_ CHAN, Christina.rtf

From: Virani, Shyrose (TBS) []
To: Stretovitch, Ana (TBS) [Ana.Stretovitch@ontario.ca]; Christina Chan [Christina.Chan@ca.ey.com]
Subject: Fw: CHAN, Christina
Date: Thursday, February 16, 2017 17:22:28

Original Message
From: Toronto Security Request (MOF) <TorontoSecurityRequest@ontario.ca>
Sent: Thursday, February 16, 2017 4:10 PM
To: Virani, Shyrose (TBS)
Subject: CHAN, Christina

Hi Shyrose,

Christina is set-up and we just need a picture. Please send her by tomorrow when it is convenient for you. I will be in the office as of 8am.

Regards,

Lee

-----Original Message-----
From: Virani, Shyrose (TBS)
Sent: February-16-17 2:56 PM
To: Toronto Security Request (MOF)
Cc: Stretovitch, Ana (TBS)
Subject: Form Returned: 2017-SSEM-REQUEST-FORM.pdf

Form Returned: 2017-SSEM-REQUEST-FORM.pdf

The attached file is the filled-out form. Please open it to review the data.

Fw_ Deloitte proposal _ TBS- OTB - OPCD - 20.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: Deloitte proposal / TBS- OTB - OPCD - 20
Date: Tuesday, January 17, 2017 12:31:22
Attachment 1: Picture (Device Independent Bitmap) 1.jpg
Attachment 2: Deloitte_Ontario_TBS_OTB_OPCD_20 - Pricing Proposal.pdf
Attachment 3: Deloitte_Ontario_TBS_OTB_OPCD_20 - Technical Proposal.pdf

---

From: Raymond, Martin (CA - Montreal) <maraymond@deloitte.ca>
Sent: Tuesday, January 17, 2017 11:27 AM
To: Petsche, Nadine (TBS)
Subject: Deloitte proposal / TBS- OTB - OPCD - 20

Dear Nadine,

Please find enclosed the documents prepared for the RFS related to Actuarial support services.
As requested under the RFS, the pricing schedule is provided as a separate file and not within the technical proposal.
Should you have any question in regards to those documents, you can reach out directly to my attention.

We look forward in working with the OPC on this mandate.

Have a nice day.

Technical Proposal

Pricing Proposal

Martin Raymond, FSA, FCIA
Partner – Audit – Actuarial services
Deloitte
1190 Avenue des Canadiens-de-Montréal, Montréal, H3B 0M7, Canada
Tel / Direct : 514-393-7367
Fax : 514-390-4104
maraymond@deloitte.ca | www.deloitte.ca

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Picture (Device Independent Bitmap) 1.pdf

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OFFICIAL SUPPLIER
FOURNISSEUR OFFICIEL

Deloitte_Ontario_TBS_OTB_OPCD_20 - Pricing Proposal.pdf

Deloitte.

Actuarial support services

Pricing proposal to serve the Ontario Government

Pricing proposal
Reference: RFS TBS-OTB-OPCD-20

Closing date: Tuesday, January 17, 2017

Proponent and contact information

Deloitte LLP
1190, avenue des Canadiens-de-Montréal
Montréal, Québec H3B 0M7
Canada

Contact: Martin Raymond
Email: maraymond@deloitte.ca
Tel: (514) 393-7367

Our **client service principles** are the framework we use to deliver **client service excellence**.

We will:

- **make** and meet our commitments to you
- **understand** your business and what is important to you
- **provide** value and build trust through technical competence and consistent results
- **demonstrate** professionalism through effective interaction and communications
- provide a **no surprises** experience

Deloitte LLP
1190, avenue des Canadiens-de-
Montréal, QC H3B 0M7
Canada
Tel: (514) 393-7367
www.deloitte.ca

Deloitte.

January 17, 2017

Private and confidential

Email delivery

Attention of Nadine Petsche
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller

Re: Actuarial Services – RFS TBS-OTB-OPCD-20 (Pricing proposal)

Deloitte is pleased to submit this pricing proposal to provide actuarial support services to the Office of the Provincial Controller (the "OPC"). As you will see from our proposal, professionals at Deloitte possess relevant experience and have conducted similar engagements for a variety of clients, including public sector. Should we be the successful bidder, we are also able to draw upon an experienced team who not only understands actuarial services, but also appreciates the challenges and complexities associated with the communication issues of actuarial results and accounting complexities. Deloitte being highly involved in pension audit, the OPC will have access to individuals that have significant expertise in understanding the market practice on accounting for pension benefits and have specialized views on interpretation of accounting standards.

If you have any questions with respect to the information contained within this proposal, please do not hesitate to contact us. We look forward to working with the OPC on this important initiative.

Sincerely,

Martin Raymond
Partner

Deloitte LLP

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Pricing considerations

Extract from the RFS

- Pricing Schedule (Schedule A) completed and submitted as a separate file.
- If HST is applicable, Vendors must itemize HST as a separate line item in the Pricing Schedule
- Vendors must propose all dollar amounts in Canadian funds
- The Pricing Schedule must set out the full legal name of the Vendor; a list of each Role (including Experience Level) proposed; and the full legal name of each consultant proposed for each Role (by experience level) to achieve completion of the proposed services within the timeframe specified by the Client; Fixed Price for each Deliverable; and total Fixed Price that the Vendor will charge the Client for Services performed and Deliverables provided
- The amount for Total Fixed Price is fixed and not subject to change unless otherwise agreed to by both the Client and the Vendor in a Change Order
- If required by the Client, the Vendor must also include a list of each Role (including experience level) proposed; and the per diem rate for each Role, to be applicable only in the case of a Change Order

Notes

- For fixed price and Core deliverables, we have assumed 90% of the estimated time found in the RFS (90% of 60 days) 54 days split 10 / 44 between Martin and Trevor
- For per diem, we have also included Matt and Clair, should they get involved in specific required activities but we did not include any specific fixed price for them as we expect Martin and Trevor to deliver the necessary services described
- The role / experience is provided in general terms. More details are found under the Schedule B of the Technical proposal
- We have used 7.25 hours for a working day, similar to OPC

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Schedule A - Pricing Schedule

Please provide the following information in accordance with Sections 2.2.1 and 2.2.2 of this Request for Services:

Legal Name of Vendor:
Deloitte LLP

Part A – Vendor Personnel

Complete the following table in respect of all proposed Vendor Personnel that will perform the Services and/or provide the Deliverables. Vendors should not include proposed Subcontractors in this Part A of Schedule A.

List the names of Consultants who will be assigned to the Project	**Role and Experience Level**
Martin Raymond	Project Lead (Partner at Deloitte): over 20 years of experience
Trevor Gary	Senior Analyst (Senior at Deloitte) : 3 years of experience
Matt Colley	Subject Matter Expert (Senior Manager at Deloitte) : 11 years of experience
Clair Grindley	Subject Matter Expert (Partner at Deloitte) : over 20 years of experience

Will Subcontractors be used for this Project? Yes [ ] No [x] If "Yes", complete Part B.

Part B – Vendor Subcontractors

Complete the following table in respect of the proposed Vendor Subcontractors at any tier of subcontracting, including any Vendor contractors that will perform the Services and/or provide the Deliverables.

Legal Name of Subcontractor	**List the names of Consultants who will be assigned to the Project**	**Role and Experience Level**
N/A	N/A	N/A
N/A	N/A	N/A

Part C – Fixed Price

In the following table, enter the Fixed Price in respect of each role to be performed and the particular Deliverables to be provided, which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

For the purposes of bidding, please include the estimated number of working days for each role not to exceed 45 in total. The Ministry reserves the right, as required, to alter the number of working days for each role as the project unfolds. The Ministry reserves the right to alter the number of working days at the time of award.

Fixed Price for each Core Deliverable	**Amount**
• One (1) Senior Consultant / Project Lead shall provide 10 working days of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements. – Martin Raymond	$ 30,100
• One (1) Intermediate Consultant / Sr. Analyst shall provide up to 44 working days of effort over the term of the agreement. The consultant shall provide all deliverable as described in Section 1.5 Client Requirements. – Trevor Gary	$ 68,640
Total Fixed Price:	$ 98,740

Part D – Other Expenses

In the following table, Vendors should list all expenses applicable to the Project that have not been included in the Total Fixed Price amount as stated in Part C of this Schedule A. Vendors should review the Travel, Meal and Accommodation Expenses section of the RFS prior to completing this table.

Expenses by Type *(List each item below):*	**Proposed Amount**
N/A	$ -
N/A	$ -
Total Other Expenses:	$ Nil

Part E – Maximum Price

In the following table, Vendors shall calculate Subtotal Price by adding Total Fixed Price, as stated in Part C of this Schedule A, to Total Other Expenses, as stated in Part D of this Schedule A.

Vendors shall calculate Maximum Price by adding the Subtotal Price to the applicable HST.

Subtotal Price (Part C + Part D):	$ 98,740
HST (if applicable):	$ 12,836
Maximum Price (Subtotal Price + HST):	**$ 111,576**

Part F – Follow-on Work Per Diem Rates

In the following table, enter the Per Diem Rates in respect of each particular Role to be performed which amount is fixed and not subject to change unless otherwise agreed to by the Client and the Vendor in a Change Order.

Fixed Price for each Core Deliverable	Per Diem Amount
• One (1) Senior Consultant / Project Lead Partner (Martin Raymond, Clair Grindley)	$ 3,010
• One (1) Intermediate Consultant / Senior Analyst Senior (Trevor)	$ 1,560
• Other possible consultants Senior Manager (Matt Colley)	$ 2,425

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Deloitte_Ontario_TBS_OTB_OPCD_20 - Technical Proposal.pdf

Deloitte.

Actuarial Support Services

Technical Proposal to serve the Ontario Government

Technical proposal
Reference: RFS TBS-OTB-OPCD-20

Closing date: Tuesday, January 17, 2017

Proponent and contact information

Deloitte LLP
1190, avenue des Canadiens-de-Montréal
Montréal, Québec H3B 0M7
Canada

Contact: Martin Raymond
Email: maraymond@deloitte.ca
Tel: (514) 393-7367

Our **client service principles** are the framework we use to deliver **client service excellence**.

We will:

- **make** and meet our commitments to you
- **understand** your business and what is important to you
- **provide** value and build trust through technical competence and consistent results
- **demonstrate** professionalism through effective interaction and communications
- provide a **no surprises** experience

Deloitte LLP
1190, avenue des Canadiens-de-
Montréal, QC H3B 0M7
Canada
Tel: (514) 393-7367
www.deloitte.ca

January 17, 2017

Private

Email delivery

Attention of Nadine Petsche
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller

Re: Actuarial Services – RFS TBS-OTB-OPCD-20 (technical proposal)

Deloitte is pleased to submit this technical proposal to provide actuarial support services to the Office of the Provincial Controller (the "OPC"). As you will see from our proposal, professionals at Deloitte possess relevant experience and have conducted similar engagements for a variety of clients, including public sector. Should we be the successful bidder, we are also able to draw upon an experienced team who not only understands actuarial services, but also appreciates the challenges and complexities associated with the communication issues of actuarial results and accounting complexities. Deloitte being highly involved in pension audit, the OPC will have access to individuals that have significant expertise in understanding the market practice on accounting for pension benefits and have specialized views on interpretation of accounting standards.

If you have any questions with respect to the information contained within this proposal, please do not hesitate to contact us. We look forward to working with the OPC on this important initiative.

For ease of presentation and to maintain the format of the submission in line with the RFS requirement, we note that after an executive summary, the next 2 sections include the completed Submission form and a summary of the Scope of services. The other sections will cover the required Schedules, pricing (A) being provided in a separate document and the resume / reference for our team members (B). We have added other Schedules to answer the Experience and Qualifications aspects of the Evaluation criteria.

Sincerely,

Martin Raymond
Partner

Deloitte LLP

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Executive summary

Deloitte is delighted to have this opportunity to propose actuarial services to the OPC with regards to pension accounting advice. We believe that our firm is an ideal choice to serve you.

> We surpass the mandatory requirements

Deloitte, one of Canada's leading professional services firms, provides audit, tax, consulting, and financial advisory services through more than 8,000 people in 56 offices, including a key office in the Toronto area.

Deloitte actuarial group has an extensive experience in performing and reviewing actuarial accounting valuation for pension plans. We serve a various range of clients, including many municipal clients and other public sector entities.

> We offer a competitive pricing

Pricing is provided under a separate document as required and reflects our desire to serve the OPC. This competitive pricing will not impact in any way the quality, time or effort put into the mandate. On the contrary, it will push our team to find innovative ways to serve the OPC and provide cost saving solutions for optimal delivery.

> We have the experience and skills to provide an outstanding service

Our team is built up of actuaries and accountants that will provide the OPC with work of high-quality. Their experience in pension and benefit accounting under PSAS and their profile will ensure that the work will be performed in timely manner in accordance with professional standards. Roles have been distributed between the team members according to their skills and experiences in order to maximize efficiency. All the team members are familiar with the recommendations contained in PSAS for pension accounting.

> We have a clear understanding of the process and requirements to perform accounting valuations and financial statements disclosures

As we provide similar services to a various range of clients on a continuous basis, we have a good understanding of the issues and a comprehensive view of the market practice.

> We offer a wide range of value added services to our clients

As consultants, our focus is to listen to clients and design specific solutions to achieve targeted results. We do not restrict ourselves to regular traditional approaches but try to define the most efficient one that applies to the client. In every task, we will tailor our level of involvement to your requirements and internal resources. We will advise you, and work in partnership with you, to achieve your objectives.

We value personalized approach and use open dialogue as much as possible. Our team will work with you in suggesting creative opportunities that add value to their consulting assignments.

Deloitte actuarial group has a unique balance in that it does work on providing consulting services, with also other work coming from audit support. This situation provides the group with both the consulting aspect and creativity along with the vision of rigorous application from auditing. This balance is important to develop better consultants that will provide services in line with today's highly regulated environment. Regular reviews we perform in audit and support we provide to some auditor generals in Canada give us a very clear knowledge of the communication challenges and the needed supporting documents for audit acceptance.

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> We regularly provide similar services to satisfied clients

Deloitte takes pride in developing relations based on communication and trust. Our knowledge and understanding of the pension and other post-retirement benefits allowed us to provide clients with the quality of service they deserve. Here is a list of public sector clients that Deloitte serves or has served recently:

- City of Montreal
- NB Government
- OTPP
- Quebec Municipal Ministry
- Ontario Government
- City of St-John (NB)
- Office of the Auditor General of Canada
- Revenu Québec

Submission form

Request for Services Number: **TBS-OTB-OPCD-20**

To: HER MAJESTY THE QUEEN in right of Ontario as represented by The Treasury Board Secretariat

1. Vendor Information

(a) The full legal name of the Vendor is: **Deloitte LLP**

(b) Please identify any other relevant name under which the Vendor conducts business:

Deloitte S.E.N.C.R.L./s.r.l
Deloitte Inc.

(c) The Vendor's address, telephone and facsimile numbers are:
Bay Adelaide Centre, East Tower
22 Adelaide Street West, Suite 200
Toronto, ON M5H 0A9

Tel: 416-601-6150
Fax: 416-601-6151

(d) The name and title of the Vendor's Representative:
Martin Raymond, Partner

(e) The mailing address, phone number and e-mail address of the Vendor's Representative:

1190 Avenue des Canadiens-de-Montréal,
Montréal, Quebec
Canada
H3B 0M7
Tel: 514-393-7367
Fax: 514-390-4104
Email: maraymond@deloitte.ca

(f) State the name, address, telephone and facsimile numbers and e-mail address of the Company Security Officer (CSO) for the Vendor:

Cara Warburton
Bay Adelaide Centre, East Tower
22 Adelaide Street West, Suite 200
Toronto, ON M5H 0A9
Tel: 416-601-5763
Fax: 416-601-6151
E-mail: cawarburton@deloitte.ca

(g) State the name and title of each of the individuals that the Vendor is proposing for this Project:

Names	**Titles**
Martin Raymond	Partner
Trevor Gary	Senior
Matt Colley	Senior Manager
Clair Grindley	Partner

2. Submission Requirements and Accuracy of Information

The Vendor accepts the terms and conditions set out in the RFS. While this submission is provided for evaluation purposes only and is not legally binding before the execution of a SOW, I confirm that the information provided is accurate.

3. Certificate(s) of Insurance

As required in Article 32.4 – Proof of Insurance in the Master Agreement, please identify the status of the Vendor's Certificate(s) of Insurance by placing a check mark (√) in one (1) of the following three (3) boxes:

☒ a) the Vendor has previously submitted a Certificate of Insurance to MGS, which has been approved

☐ b) the Vendor has included its Certificate of Insurance with this RFS submission (that will be subject to approval by MGS) prior to the Client issuing a SOW

☐ c) the Vendor agrees to submit a Certificate of Insurance (that will be subject to approval by MGS) prior to the Client issuing a SOW

4. Conflict of Interest

The Vendor must complete the following:

(a) If the box below is left blank, the Vendor will be deemed to declare that: (1) there was no Conflict of Interest in preparing its submission; and (2) there is no foreseeable Conflict of Interest in the Vendor or any of its Personnel performing the contractual obligations contemplated in the Request for Services.

(b) Otherwise, if the statement below applies, check the box.

☐ **The Vendor declares that there is an actual or potential Conflict of Interest relating to the preparation of its submission, and/or the Vendor foresees an actual or potential Conflict of Interest in it and/or its Personnel performing the contractual obligations contemplated in the Request for Services.**

(c) If the Vendor declares an actual or potential Conflict of Interest by marking the box above, the Vendor must set out below details of the actual or potential Conflict of Interest:
N/A

(d) The following individuals, as employees, advisors, or in any other capacity (i) participated in the preparation of our submission; **AND** (ii were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:
Job Classification (of last position with OPS):
Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):
Last Date of Employment with OPS:
Name of Last Supervisor with OPS:

Brief Description of Individual's Job Functions (at last position with OPS):
Brief Description of Nature of Individual's Participation in Preparation of Submission:

(e) The following are individuals that: (i) are proposed to be assigned by the Vendor to perform work under the SOW; **AND** (ii) were employees of the Ontario Public Service ("OPS") and have ceased that employment prior to the Requested Submission Date:

Name of Individual:
Job Classification (of last position with OPS):
Ministry/Agency/office of an officer of the Legislature of Ontario (where last employed with OPS):
Last Date of Employment with OPS:
Name of Last Supervisor with OPS:
Brief Description of Individual's Job Functions (at last position with OPS):

(f) We agree that, upon request, we shall provide the Client with a Conflict of Interest Declaration from each individual identified above in the form prescribed by the Client.

5. Schedules

This submission includes the following Schedules:

Schedule A (Pricing Schedule) – provided in a separate document as required
Schedule B (Resumes and references)
Schedule C (Similar projects and working with Governments)
Schedule D (Reports for public pension initiative)
Schedule E (Ceiling Test and Sensitivity Analysis)
Schedule F (Methodology and implementation plan)

Deloitte LLP
I acknowledge that providing my name on the line below in electronic form will constitute a signature for the purposes of the *Electronic Commerce Act, 2000*, S.O. 2000, c. 17.

I have authority to bind the Vendor.

Per:

Signature:

Name: Martin Raymond
Title: Partner
Date: January 17, 2017

Scope of services

Treasury Board Secretariat, Office of the Provincial Controller (OPC) requires actuarial services to support input to the 2017/18 Provincial Budget and the preparation of the 2016/17 consolidated financial statements of the Province, specifically related to pension balances and costs in accordance with public sector accounting standards.

Scope of the services

The Services and Deliverables to be provided by the Vendor will include the following:

- Working with management of the OPC's Accounting Policy and Financial Reporting Branch (APFR), to provide actuarial services related to the following possible areas:
    - Review APFR's calculation of estimated accounting valuations based on actuarial input for pension plans reflected on the Province's consolidated financial statements (Ontario Public Service Employees Union Pension Plan, Ontario Teachers' Pension Plan, College of Applied Arts and Technology, Health Care of Ontario Pension Plan and Public Service Pension Plan) as well as post-retirement benefits
    - Conduct related sensitivity and/or scenario analysis as requested by APFR
    - Participate in discussions and meetings with internal and external stakeholders, as required

- Working with management of the OPC, through the (APFR), provide actuarial services related to the following possible areas relating to the Ontario Public Sector Employees Union Pension Plan and Ontario Teachers' Pension Plan:
    - Design and execute various valuation models, as requested by APFR, relating to the ceiling test requirements in the CPA Canada public sector accounting handbook (PS3250.050 to PS3250.059)
    - Conduct sensitivity and/or scenario analysis as requested by APFR
    - Provide advice to APFR, for accounting purposes, on the ceiling tests and sensitivity analysis
    - Participate in discussions and meetings with internal and external stakeholders, as required

Based on the RFS, it is estimated that 60 working days of effort over the term of the Statement of Work (SOW), at the discretion of the provider, to be split between members, or for one individual as deemed appropriate.

- One (1) Senior Consultant / Project Lead
- One (1) Intermediate Consultant / Sr. Analyst

The successful candidate must demonstrate their understanding and experience/expertise with:

- Government financial reporting objectives of transparency and accountability, including an in-depth understanding of public sector accounting standards (PSAS)
- Specific public sector accounting standards as related to pension actuarial valuation and measurement
- Working with a variety of public sector stakeholders in matters related to actuarial assessments/accounting/measurement of pension assets under PSAS
- Ontario government's protocols regarding document confidentiality

Schedule A – Pricing

As per the RFS requirement, the pricing proposal has been provided in a separate file named:
Deloitte_Ontario_TBS_OTB_OPCD_20 – Pricing Proposal

Schedule B – Resumes and References

Based on the RFS requirement:

- Vendors are expected to submit a resume for each consultant proposed in the Submission Form - please include the resumes as Schedule B to your Submission Form

  NOTE : resumes are included in this Section

- For each proposed consultant, Vendors are expected to submit the consultant's most current project(s), and submit references (include name, title, organization and telephone number) whom the Client may contact for the purpose of conducting reference checks

  NOTE : some projects are presented and references are included in this Section

- Vendors are expected to demonstrate in their submission that each proposed consultant has the knowledge, experience and all other qualifications for the proposed Role, and will be able to provide the requested services

  NOTE : the description found in this Section will show the qualification of our proposed team

- Vendors must provide the Client with the opportunity to interview each proposed consultant, and must not charge the Client in connection with any interview

  NOTE : we confirm that interview with our proposed team is available as needed

- Vendors must identify all subcontractors that they propose to use, and must also identify which consultant(s) is provided by which subcontractor

  NOTE : we will not use any subcontractors, all services required will be provided by Deloitte professionals

Proposed Team

As you will see from this section, our proposed team does have the necessary qualification, skills and experience to deliver the needed activities related to this mandate. Considering that the focus of the work will be highly related to Public Service Accounting Standards and technical application of elements such as asset ceiling and sensitivities of actuarial results, we have included 2 actuaries in the Submission form that have both deep actuarial and accounting knowledge, experience and expertise. One member is fully qualified Fellow.

They have been exposed to working in large actuarial consulting firms and also have been within Deloitte gaining the deep key accounting knowledge that provide them with the overall skills to deliver the accounting work that the OPC is looking for.

The Project Lead that will handle OPC work is Martin Raymond (partner), the leading consulting actuary for pension at Deloitte. In his work, Martin will be supported by Trevor Gary (senior). Martin has joined Deloitte in October 2011 to lead the actuarial pension and benefit practice. Since then, his group has been supporting

Deloitte auditors with all regards related to pension and benefits. He is also responsible for any specific consulting pension and benefit services on non-audit Deloitte clients.

In their work, Martin and Trevor will also have access to some specific personnel of Deloitte that may be involved to limited extent depending on the needs. If required, their involvement is likely to be more for sound-boarding support or validation of approach. Clair Grindley and Matt Colley will be the 2 main subject matter experts that may have some implication. Matt is already involved in some other advice support to the Ontario government and as such will likely participate in some of the meetings in the course of the project. His understanding of the OPC environment, structure and strategy will ensure that we always provide the optimal approach in working with the OPC.

Since Martin and Trevor are identified as the 2 main members of the team to work on Core deliverables (Project Lead and Senior Analyst) we have provided more details for experience and references for these 2. For Matt and Clair, we provided their resumes but if needed, additional references will be available on demand.

The following table will provide a summary description of the team members.

Proposed resources		
Name of Individual	**Level**	**Description of role**
Martin Raymond (Project Lead)	Partner, Actuarial Services	As the account manager, Martin will be responsible for relation with the OPC. He will be the reference person for any strategic issue and will ensure that high-quality services be provided. He will work in collaboration with Trevor on the delivery of documents and advice. He will be responsible for the timeliness and quality of services performed, as well as ensuring that OPC expectations are met or exceeded. His vast experience in both accounting and actuarial fields will provide all the expertise that will be needed for the activities to be performed. Considering the deep knowledge that Martin has in public sector accounting for pension, he will drive the orientation of the analysis and advice.
Trevor Gary (Senior Analyst)	Senior, Actuarial Services	Trevor will be responsible to prepare along with Martin the documentation needed on the account. He will be involved in sensitivity and/or scenario analysis to support the file and will participate in data and calculations that will be required. He will be an every-day contact for data, questions and follow-ups. He will participate in most of the communications with the OPC. Trevor and Martin will meet on regular basis to provide status updates and agree to the required steps. During the implementation, his role will be to lead the information gathering and prepare initial documentation.
Matt Colley (subject matter expert on Ontario process and protocols)	Senior Manager, Audit	Matt is a Deloitte professional that is highly familiar with the Ontario processes and protocols. Based on his experience, he will support as needed the proposed team on adhoc basis. He will likely participate in some meetings with OPC and help ensure approach taken is optimal considering the Ontario government practices.
Clair Grindley (subject matter expert on pension accounting)	Partner, Audit	Clair is a specialist in complex accounting issues of different nature. She does specialize in pension specific area. She has a deep knowledge of the various accounting standards on pension and provide with a deep view of the accounting world. She works on regular mandates with Martin to provide a solid joint accounting and actuarial expertise that our clients are looking for. She will be an additional expert on pension accounting and a sound boarding support.

Shown expertise of the proposed team

Within the resumes of the proposed team, you will find more specific expertise for both Martin and Trevor. The following paragraphs are meant to show the extent of the work that both Martin and Trevor are involved on a regular basis. The proposed team works significantly with PS3250 and PS3255 annually as well as other pension accounting standards. The team has worked in all aspects of a valuation required for accounting purposes, namely:

- Review of membership data and sufficient information to support extrapolation purposes
- Selection and review of management best estimate assumptions
- Prepare models needed for selection of assumptions
- Determine the approach to define the accounting discount rate
- Prepare obligation reconciliation for gains and losses
- Prepare the year expense and reconcile year change
- Apply asset ceiling test when asset shown on the balance sheet
- Prepare actuarial report with the required content for accounting disclosures
- Answer auditor questions, including Auditor Generals

The pension actuarial group do perform annually more than 150 audits on different standard basis. Among these we are involved in 15 to 20 audit reviews specifically of public sectors and are very familiar with the requirements of PS3250 and PS3255. Sitting in an accounting firm, we are always searching through the applicable accounting standards to assess if work is performed in accordance with the requirements of those standards. This is definitively one key advantage that our professionals do have to support our clients. We also have access internally to very highly specialized experts (accountants) that are very familiar with how a standard has been developed. Sometimes it is important to understand the spirit of the standard to determine what is acceptable or not and not just the wording of a paragraph of the standard.

As you will see from some experiences we have detailed, our team has been involved in very complex key accounting issues, such as application of public sector to Shared risk plan model in New Brunswick. In performing this work, our team demonstrated a high level of knowledge of the accounting standards to define how it would apply to the specific plan model. This is one proof of the high familiarity that we do have with the standards and not only the public sector but also with other standards.

Our team is really connected to future public sector changes as Martin Raymond is involved in the CPA Task Force on PS3250 and PS3255 review. We also have connections with auditor generals around Canada. We therefore know how to communicate appropriately and prepare a file that will be complete.

The team performs a significant number of actuarial mandates for public sector in valuation services and also in audit services. As an illustration, here is a list of high-profile public sector clients for which we have been involved in recent years:

- City of Montreal
- NB Government
- OTPP
- Quebec Municipal Ministry
- Ontario Government
- City of St-John (NB)
- Office of the Auditor General of Canada
- Revenu Québec

Resumes and references

Following are the resumes of the proposed team along with references and specific relevant experience for Martin and Trevor the main resources identified to provide the core deliverables.

Martin Raymond, FSA, FCIA

Partner – Audit & Advisory
Actuarial, Rewards and Analytics

Profile

For 23 years, Martin has been with the Consulting practice as a specialist in pension plans. He is also an expert in retirement and benefits accounting, having served as the national specialist in this area for a large actuarial consulting firm. This experience has provided him with the skills to serve a diverse clientele and to handle complex accounting and financial disclosure issues.

As a partner in the actuarial department, Martin is responsible for managing and supervising the work related to Canadian pension plans and benefits for Audit teams but also for general consulting. Additionally, he is also actively involved in answering questions related to the application of pension accounting and pension legislation while assisting the firm's decision-making process in these areas.

His role includes follow-up on changes in accounting standards and best practices. Over the years, he developed different tools required to perform calculations and ensured integrity of work in accordance with the standards. He was also highly involved in training, both internally and to the firm's clients. His expertise was used many times in resolving clients' issues for accounting treatment of special events and also situations that demanded specific accounting interpretations.

Along with his responsibility as national specialist on accounting, Martin also served as general consultant for clients on actuarial issues. His work encompassed looking at funding and accounting projections along with optimizing strategies. He also helped employers in negotiation support to identify possible plan design changes and evaluating the costs. He supported employers in selecting actuarial assumptions and reviewed work of more junior staff to assess reasonableness of results. He was responsible for quality of services offered along with satisfaction of clients.

His skills as communicator has made him highly appreciated by clients, pension plan members and fellow colleagues. He takes pride in translating complex issues into accessible actuarial and accounting concepts for people less familiar with these matters. For pension and benefit arrangements to be appreciated by members, it needs to be well understood. This represents in many cases the challenge for today's plan sponsors and Martin would surely be an addition to this mandate.

Professional affiliations/Certifications

- Fellow of the Society of Actuaries (FSA since 1998)
- Fellow of the Canadian Institute of Actuaries (FICA since 1998)

Education

- B.Math. (actuarial science) – Université de Montréal

Other activities

- Speaker at the Canadian Institute in 2001-2002 on termination of plans
- Instructor at the AGFMQ (Quebec association of municipal financial managers) in benefits programs accounting in a municipal setting in 2006
- Member of the CIA (Canadian Institute of Actuaries) Task Force on Pension and Post-retirement Benefit Accounting Discount Rates (2009 to the present)
- Speaker at the Canadian Institute of Actuaries' pension seminar in 2012.
- Member of the CPA Task force on review of Public Sector accounting standards (2016 and forward)

Knowledge / experience and current / recent projects

His expertise in the pension accounting field has been recognized by clients, fellow actuaries and also by participation through accounting specific working groups. Of particular interest for this specific mandate, we note that Martin is a member of the CPA Task Force on employee benefits that will review the standards (PS3250 and PS3255) in upcoming years to determine if and to what extent changes are to be made to these standards to reflect the evolution in accounting practice since their initial implementation. Some issues that are to be looked at include deferral of actuarial gains and losses, discount rate selection, shared risk plan (SRP) treatment and multi-employer plans. Since a number of these elements are of interest to public sector entities, having someone that is involved in the discussions will provide great insight for the OPC to understand the issues, the discussion elements and the possible outcomes.

Martin has also worked with numerous public sector clients either as a consultant providing full valuation services but also through the auditing role of ensuring that accounting was performed in conformity with the accounting standards. His involvement in all types of employee benefit accounting standards (US, IFRS, ASPE, PSAS) has provided him with a broad view of the possible issues that come up and the likely ways of addressing them.

He is also recognized by the Québec municipalities Ministry as a key person involved in number of complex issues that have come up on pension and benefit accounting since the Québec municipalities have transitioned to public sector accounting in 2007. This implication is still ongoing on regular occasions when specific situations come up that need insights on the appropriate treatment. He has been involved in a number of areas that demanded accounting and actuarial expertise since that date, including:

- Impact of 2007 transition on municipalities financial statements
- Treatment of funded and non funded plans
- Selection of discount rate based on cost of borrowing
- Treatment of asset ceiling
- Use of reliefs for taxation purposes for various elements (past service costs, asset ceiling, non funded plans)
- Special approach used after the 2008 financial crisis to alleviate the taxation requirements
- Review of changes in pension plan legislation specific to municipalities and define the appropriate treatments.

He also has worked closely with the OAG on a number of pension and benefit audit supports for which his collaborative approach along with his understanding of issues and ease to communicate it has been greatly appreciated by the OAG personnel. The reporting format of the information, the illustrations provided on complex issues and the deep knowledge of both pension actuarial work and pension accounting understanding have been part of the successes of all the mandates performed.

Along with the Québec Ministry support and the OAG audit supports described as current projects, for which we do provide references, it should be noted that one other main area that shows expertise relates to his involvement with the Government of NB and City of St John (NB) on Shared Risk Plan (SRP) accounting treatment. This is a very complex accounting issue that is still being regularly discussed with accounting standard setters and accounting firms, but on which some judgment is needed to define a reasonable approach. The main elements that were part of the activities are:

- Review of the SRP legislation, plan provisions and funding policy
- Review of actuarial valuation reports on SRP

- Review of stochastic projection results to meet the risk management criteria
- Review of the accounting standards to define the defined benefit / defined contribution classification for accounting treatment
- Review the selection of assumption process as some benefits are conditional on plan situation
- Review of the joint defined benefit accounting provisions
- Meetings / discussions with clients and their actuaries
- Work in collaboration with the actuaries to define the appropriate calculations
- Review valuation numbers, accounting figures and confirm it is performed in accordance with accounting standards

All through these 2 SRP mandates, Martin was highly involved in helping understanding the standards, working in collaboration to find appropriate solutions and providing along the way the knowledge enhancements that the various parties were needing to appreciate the issues and understand the solutions.

In addition, Martin has experience working with the OPC in regards to pension accounting advice. In a recent mandate, his role was to provide advice and guidance to OPC on complex accounting and reporting matters related to accounting for pensions and the Province's consolidated financial statements. More specifically, Martin provided his expertise in actuarial assessment in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250. In that work, both the accounting expertise, knowledge of the tests and the actuarial calculation requirements were involved to support OPC understand the work performed by an actuary with that regards.

References

We authorize the OPC to verify information provided to confirm client satisfaction and demonstrated success.

Relevant project #1 – Office of the Auditor General	
Year of work	2016
Description of Contract	The Office of the Auditor General provides an allotment of sick leave days per month of service to its employee. The unused sick days given in a year may be carried forward to future years. This type of benefit requires an actuarial valuation to determine the obligation and the expense under PSAS. • Review plan provisions / data and prepare a summary • Recommend appropriate assumptions • Perform a detailed calculation of the liability of the OAG for sick leave benefits accumulated by its employees as of March 31, 2016; • Determine the related components to be disclosed in the financial statements, I.e. the benefit costs, the interest cost, and the actuarial loss or gain for 2015-16; • Estimate the benefit costs for the following year (2016-17); • Perform a sensitivity analysis on the following assumptions: discount rate, annual rate of increase in salary, retirement age and use of accumulated sick leave. • Prepare a report in accordance with standards of practice of the Canadian Institute of Actuaries (CIA) and with PSAS (PS 3255)
Contact Person	Shawn Audette
Telephone and Email	(613) 952-0213 ext: 5290 shawn.audette@oag-bvg.gc.ca

Relevant project #2 – City of Montréal	
Year of work	1997 to 2016
Description of Contract	Numerous cities on the island of Montreal merged in recent years into the City of Montreal. With these mergers came also the application of public sector accounting to municipalities in Quebec. As such, the City was faced with more than 40 pension and benefit plans to account for. Martin was involved over 5 years into preparing accounting results for the various plans and harmonizing communications for the City representatives. Communications to the management was also crucial and Martin was involved in many key employer meetings. His work also included treatment of many special events and also ensuring that work was in accordance with accounting requirements. He supported the setup of an accounting document that follow-up the quarterly evolution of the expense and the explanation of changes. The document also showed the expected expense over a 5-yr period in stochastic modelling. More recently, Martin is involved in the review of the accounting results of the pension plans. This includes the reconciliation of the results, the review of the assumptions, the impact of the changes in assumptions, the impact of changes in legislation and many more audit procedures related to employee benefits accounted under PS 3250 and PS 3255.
Contact Person	Jacques Marleau
Telephone and Email	(514) 872-3155 jmarleau@ville.montreal.qc.ca

Relevant project #3 – City of St John (NB)	
Year of work	2016
Description of Contract	Accounting of a pension plan under the Shared-Risk Plan model, a complex new pension framework in New-Brunswick. Define the accounting treatment under PS 3250: • Review plan provisions • Review legislation • Identify key accounting standards provisions • Discuss with Entity and actuary about the valuation of the obligation and accounting results • Work some illustrations and calculations to help the client through the process Define an acceptable approach within the accounting framework.
Contact Person	Hilary Nguyen
Telephone and Email	(506) 648-3713 hilary.nguyen@saintjohn.ca

Relevant project #4 – Québec Ministry of municipalities	
Year of work	1997 to 2016
Description of Contract	Public standards accounting is applicable to Québec municipalities since 1997. Martin involvement with the Ministry has been of different natures • Identify key accounting provisions that apply to pension plans • Review the impact on the municipalities financial statements • Identify some relief options to manage taxation level • Discuss the impact of the 2008 crisis on municipalities and identify the options / treatments to offer some tax management relief to the municipalities • Look more recently at the major changes in pension legislation that affected municipalities and identify the appropriate accounting treatment • On number of occasions be an expert / sound boarding resource for the Ministry on issues that come up
Contact Person	Yvon Bouchard
Telephone and Email	(418) 691-2015 (extension 3812) yvon.bouchard@mamot.gouv.qc.ca

Trevor Gary

Senior – Audit & Advisory
Actuarial, Rewards & Analytics

Profile

Trevor joined Deloitte's Actuarial, Rewards & Analytics Team from McMaster University where he completed his B.Sc. Mathematical Science and B.A. Economics. In the Audit practise, he actively leads on 30+ pension plan audits under various accounting standards. This included: review of accounting schedules, disclosures, and assumptions, audit planning for the pension plan, and liaising with clients and their consulting actuary to resolve pension related issues.

In the Advisory practice, Trevor acts as the main point of contact for Pension Due Diligence related to M&A/Transactions, he continues to actively pursue opportunities in the de-risking space, and has experience providing support for plans with a foreign domicile including the US, UK, and Switzerland.

Trevor's 'traditional' Actuarial experience at Deloitte has included work on actuarial valuations, annual client regulatory filings, benefit calculations including Family Law Value calculations, and providing client support in regards to following Canadian Pension Regulation. Trevor has worked on plans under each of the 11 pension regulators in Canada.

Education
BA, McMaster University, 2012
B.Sc., McMaster University, 2013

Training
Trevor is close to completion of his Associate of the Society of Actuaries (A.S.A.) designation.

Awards
- 1st place - 2014 Actuarial National Student Association (ASNA) Case Study Competition
- 2012 Vanier Cup Champion

Knowledge / experience and current / recent projects

Trevor has been involved over recent years in a large number of audit supports on the different accounting standards. Over all of these mandates, Trevor's work did cover the full array of the accounting support:

- Review of assumptions used and confirm they are reasonable
- Ensure the methodologies applied are in accordance with the accounting standards
- Question management on accounting choices made
- Explain the major changes occurring during a year
- Detail the main gains and losses
- Compute the expense and balance sheet entry
- Review content of financial statements notes and comment on it
- Provide sensitivity and extrapolation results
- Review asset ceiling calculations and determine the economic future benefit calculation

In one of its main audit assignment he was involved in recalculating specific member benefit obligation by analysing plan provisions, applying the accounting methodology, perform the projection and determine obligation and current service cost. He did prepare an actuarial report covering the methodology, data and calculations results to compare with the actuary calculation.

He has also been involved in a large audit support work with the OAG that covered 7 pension and employee benefit plans. The work specifically covered the array of the audit work described above but also covered a formal reporting going out to external user (the OAG). The documentation prepared by Trevor was received with high level of satisfaction and showed his level of professionalism and his commitment to quality work.

References

We authorize the OPC to verify information provided to confirm client satisfaction and demonstrated success. In addition to these references, Trevor has also been involved in the recent asset ceiling work with the OPC main contacts.

Relevant project #1 – Canada Post Corporation (OAG support)	
Year of work	2016
Description of Contract	Trevor, along with Martin supported the OAG in reviewing the actuary's work and ensure work performed in accordance with the accounting standards and actuarial practice. Activities covered: • Review of assumptions and changes during the year • Review main elements of gains and losses (explain the source and calculate independent assessment) • Comment on content of report and disclosures • Validate sensitivity disclosures • Prepare a formal report for external use to be sent to the OAG • Prepare knowledge transfer to the OAG on some complex accounting and actuarial elements Deloitte did receive a very good feedback from the OAG on work performed and communication between OAG and Deloitte
Contact Person	Patrick Charbonneau
Telephone and Email	(613) 952-0213 (extension 2226) Patrick.charbonneau@oag-bvg.gc.ca

Relevant project #2 – OTPP	
Year of work	2015 - 2016
Description of Contract	Working with the Deloitte audit team, Trevor has been involved in reviewing actuarial results. Applying the calculation requirements defined under accounting standards to perform independent assessment of member obligation result • Review plan provisions • Define appropriate benefit calculation and apply assumptions • Apply legislation limits • Discuss with the actuary some may results obtain to validate some aspects of the calculation • Compare results with the actuary calculation • Prepare a report defining our approach and key observations / results Objective was to ensure adequate obligation reported based on the accounting requirements.
Contact Person	Name and email will be provided on demand.

Matt Colley, CPA, CA

Senior Manager
Assurance and Advisory

Profile

Matt is a Senior Manager in the Audit Advisory Practice in Toronto, which focuses on Accounting Advisory, Transaction Consultation, Finance Transformation, and Audit Analytic services. Matt has over 11 years of public accounting experience and has been exposed to a variety of engagements and cross functional teams. Matt joined Deloitte in 2004 and spent the majority of his initial years with the firm performing attest services mainly in the public sector organizations. Matt currently advises Public Sector and Private Sector organizations on complex accounting matters, as well as systems and process improvements. From 2012 to 2014, Matt was seconded to Deloitte's National Office to assist audit practitioners with complex accounting issues and to audit practitioners prepare their clients for new accounting standards that were being developed under IFRS, ASPE, Accounting Standards for Not for Profit Organizations and Public Sector Accounting Standards, including helping many clients with the adoptions of PS 3450.

Through his experience in auditing and advising many different types of public sector organizations, Matt has been exposed to various public sector accounting and regulatory issues. In addition to providing complex accounting advice to public sector organizations, Matt is currently supports clients in finance transformation initiatives and helping organizations elevate the profile and efficiency of their finance function.

Relevant Experience

Provincial Ministry of Finance Complex Accounting Support: 2015 - Current: Matt is Deloitte's lead senior manager on engagement to advise management on a large complex transaction on a Government Business Enterprise. This engagement required Deloitte to work with the client to understand the transaction being proposed and to provide guidance to relevant stakeholders on the accounting implications of the transaction. Deloitte worked with management and various professional advisors to inform decision makers about the implications of the proposed transaction and to help the client document their analysis and conclusions. Deloitte also assisted the client in presenting the client's analysis and views to the Auditor General. This engagement required extensive research across all parts of the CPA Canada Handbook (Not-for-Profit, Public Sector, Private Company, and Public Reporting Issuers) to support the conclusions reached by management.

Provincial Review of the Implementation of a New Accounting Standard (PS 3260) - 2015: Deloitte was engaged to advise the internal audit function within a Provincial government on the complexities of implementing a new accounting standard on contaminated sites. Matt was the lead senior manager on the engagement which involved helping internal audit provide recommendations to identified ministries and a central agency on how to deal with complex issues associated with implementing the accounting standard and providing support to various ministries on how to improve their internal controls and documentation around the implementation of the accounting standard. The engagement also involved assisting management and internal audit in developing a position paper on how to treat certain complex issues resulting from the implementation of PS 3260 that was used in discussions with the auditor general.

Provincial Government Business Enterprise Complex Accounting Support - 2013- Current: Matt is the lead senior manager on a Deloitte engagement to advise Provincial Government Business Enterprise on complex accounting issues resulting from new transactions, and challenges with adopting new accounting standards under IFRS around employee benefits, revenue, and leases. Deloitte supports this client by providing updates on changes in accounting standards and by working with the client to develop analysis on the impact of new standards and proposed transactions.

Community involvement

- Board Member and Finance Committee Member – 2015: The Meighen Health Centre
- Finance Committee Member – 2009 – 2015: The Change Foundation
- Board Member and Treasurer– 2003 – 2009: Intrada Brass

Education / Professional designations / Industry Conferences

- Bachelor of Business Administration, University of Toronto (2004)
- Chartered Professional Accountant, Chartered Accountant (2007)

Clair Grindley, CPA, CA, ACA

Partner
National Office

Profile

Clair Grindley is a Partner in Deloitte's National Office and is focused on the application and interpretation of technical accounting guidance both in Canada and on a global level. She is the firm's technical accounting leader on employee benefit issues and works closely with our Firm actuarial experts on this area. Clair is involved in the development of technical accounting publications for the Canadian Firm and globally. She is also involved in the development and delivery of technical accounting learning to Deloitte practitioners and to Deloitte clients.

Clair has been with the Firm for 20 years including 5 years with Deloitte in the United Kingdom. Prior to joining National office she worked in the audit and assurance sector and subsequently in Deloitte's accounting advisory services group.

Professional and Community Affairs

- Member of Deloitte's Global Employee Benefits Subject Matter Group
- Member of CPA Canada's EFB ASPE (Section 3462) Briefing Taskforce (project now completed)
- Former Member of the Accounting Standards Boards IFRS Discussion Group (since inception)
- Former Member of the Accounting Standards Boards IFRS Advisory Committee (now replaced by IFRS Discussion Group)

Education and professional designations

- Bachelor of Accounting and French (Joint Honours) (Southampton, 1995)
- CPA, CA, ACA

Schedule C – Similar projects and working with Governments

Each Vendor should provide in its proposal:

- A description of the proponent's current or past experience with similar projects, with examples of successful outcomes, anticipated challenges, and corresponding mitigation strategies that the Vendor would employ.
- Provide a description of the proponent's previous pension actuarial experience with the Ontario Government or other senior Canadian Governments and provide specific examples of how that experience would assist the Vendor with the Deliverables.

Similar projects

Number of similar projects were performed by Deloitte over recent years that covered many complex accounting issues. Some of these have already been described in the Schedule B of team members to show their expertise. A summary of some examples for both PSAS and IFRS / ASPE is described below.

Under PSAS for one specific client, Martin and Deloitte provided various accounting advice over many years. Success was measured in that the client was satisfied and so was the Auditor General. Work was performed on accounting standards compliant basis and we did find practical approaches in an environment of multiple plans. Challenge was mostly around getting some harmonized approach to the multiple plans that were present (more than 40 at some point). Determining the main goals, identifying the material elements were crucial and helped mitigate the multiple plans situation. We were able to focus on the main ones that represented the biggest piece of the obligation. The other challenge was the level of knowledge of the various parties relating to accounting requirement. To overcome this, Martin was involved in number of training sessions to really provide a solid basis for the different key persons that would be involved. Throughout the years of engagement, Martin also used his communication skills and illustrative approach to help the client and the Auditor General to get familiar with the pension accounting and get a comprehensive understanding of the calculations performed. On every occasion, he found a way to increase the appreciation of the accounting standards and the required work. Complex elements that came up and needed to be explained and dealt with included; asset ceiling calculation and its relation to gains and losses, market-related value of asset methodology, discount rate for non funded plans, use of the available information to determine how to make some already available results into accounting compliant (time and cost savings).

Under IFRS, for 3 main clients of Deloitte, we did have asset ceiling consideration this year due mainly to the plans being closed to new entrants. Asset ceiling is a very complex application under IFRS that encompass minimum funding requirement calculations and determination of economic future benefits. Letters of credit could also be used to avoid minimum funding requirement effect. So a large number of pieces come into play in the calculations performed. Success of our work was measured by raising issues around the asset presented on the balance sheet, making the clients aware of the complexity of this and getting them understanding our approach and therefore limits on balance sheet asset. The main challenge we had was to get the actuaries to view the arguments we had on this issue and have them agree at least to some extent to our views. In order to overcome this challenge, we held some calls with the actuarial firm and we did have the client also listening to these calls, and provide their inputs. Having all interested parties included in the discussion proved to be a good way to mitigate that and avoid simple back and forth emails from actuary to actuary. We also did validate some of our position elements with other colleagues in various firms (actuarial and accounting) to understand the practice for some components of asset ceiling and get a broader view of the flexibility that exists and boundaries applied.

One other main success we can mention is how we work in the audit mandates either with our own Deloitte auditors, the firm clients or with Auditor Generals. Being specialists of pension, actuarial calculations and accounting standards, we do provide significant value to auditors and clients. We even get great comments from actuarial firms that we work with, even if we can be seen at some point as counterparties to them. The success we think can be measured in different ways. The main things we can mention are: we understand the benefits offered, we know how they are calculated, we know how accounting results are determined. We work efficiently in identifying the main issues, getting the appropriate questions out and preparing a documentation that will answer the objectives that are set out. When an event occurs that need special accounting treatments (past service costs, curtailments, settlement, annuity purchase, asset ceiling calculation…) we know what information is important and what is needed to support a file. As such, we find that success comes with a complete documentation, an effective approach, avoid unnecessary questions to clients / actuaries. We sometimes have challenge in dealing with actuaries as they may see us as competing with them to find an accounting answer and maybe reviewing calculations that they perform and thus being the ones that are looking for their errors. In order to mitigate this kind of feeling and ensure orderly communications with the actuaries, we do adopt an approach of collaboration. We always make the communications with actuaries very professional and in good faith on both sides. We keep our mind opened to evolving approaches but maintain the accounting compliance as a main goal. We also discuss openly on adhoc basis with accounting specialists in all major actuarial firms to exchange views and keep transparent on new issues and evolving practices. So far the communication has been great for most cases even when significant issues have come up.

Working with Governments

We have been working with governments both on very specific pension issues but also on many other occasions for non pension elements. Deloitte being a provider of a vast array of professional services, we do have a number of initiatives that were specifically performed with Ontario.

From a pension specific perspective, we have been involved highly with the Québec municipal Ministry to apply the PS3250 and PS3255 accounting standards to municipalities since 1997 when it was first adopted. In Québec, contrary to other major provinces in Canada, the pension plans are direct responsibility of the municipalities. There is no one single plan like OMERS or BC Municipal. So there are a large number of plans and some cover a large number of members. In applying the standards, a number of issues came up and needed the Ministry to look at the effect on municipalities but also define some guidelines to apply the standards. Martin and Deloitte have been involved since 1997 with the Ministry to discuss numerous issues and help the Ministry to provide recommendations on complex accounting elements. We can note the following:

- Identify key accounting provisions that apply to pension plans
- Review the impact on the municipalities financial statements of transition
- Identify some relief options to manage taxation level for number of accounting events
- Discuss the impact of the 2008 crisis on municipalities and identify the options / treatments to offer some tax management relief to the municipalities
- Look more recently at the major changes in pension legislation that affected municipalities and identify the appropriate accounting treatment
- Asset ceiling, market-related value of assets, discount rate selection, mortality changes, presentation in financial statements …

In this implication with the Quebec Ministry, we did get exposure to a very large number of accounting issues and we did have to provide support from the very specific accounting literature (key paragraphs). Since this was applied to very large public employers, it also had a significant impact on the practice in general and how actuaries were calculating results under PSAS. We believe that all these make us very well positioned to support the OPC on complex issues that will come up. The large number of plans for Québec municipalities do provide us with a large exposure to situations that have come up and prepares us to the needs that OPC will have.

In another work with the Québec government, Deloitte has been providing support to compare the accounting practice in Canada of various governments on how they select the discount rate and what valuation methodology they used. A review of the valuation results presented in the notes or annual report of the main plans was also looked at. In performing this work, we did have to prepare reporting in specific format that could be used by interested parties at government level. As such, we needed to be sure the explanation was appropriate, to the point and accessible to a non-familiar reader. We believe that this experience, above the fact that it provided us a good view of the Canadian public sector plans in Canada, will also help us define the appropriate communication needs and format that OPC will be able to use.

We also did work with the NB Government on the preparation of a white paper on Shared Risk Plan accounting. This new type of plan is highly complex and also is not totally contemplated by the PS3250 that is more based on traditional plan structures (either DB or DC). Plans with conditional benefits are more addressed under IFRS, although there is also some grey area in this standard. We did provide support to the Government to define an approach to account for these plans. In doing this we needed to educate some people on accounting, we needed to review standards and we needed again to report on a complex issue to non-familiar individuals. We think that this is something that will be helpful to support the OPC in the upcoming challenges of complex accounting issues.

In 2016 Martin and Trevor worked with the OPC to derive supporting analysis for complex accounting elements that may be scrutinized during the Public Accounts audit. Deloitte's role was to provide advice and guidance to OPC on complex accounting and reporting matters related to accounting for pensions and the Province's consolidated financial statements. More specifically, the Deloitte team provided their expertise in actuarial assessment in relation to applying the ceiling test to the accrued pension benefit assets in accordance with PS3250. In doing so, we were able to work with the OPC to define a process for calculating the valuation allowance, highlight key elements of the calculation such a future economic benefit and contribution reduction versus surplus withdrawal, and support discussion with the Province AG. The positive working relationship we had with the OPC team during this engagement will service as a foundation for the upcoming project. Further, our understanding of the OPC's process will serve as an efficiency to get the mandate started.

Schedule D – Reports for public pension initiative

Each Vendor should provide in its proposal:

- Describe the proponent's demonstrated knowledge, skills, experience and expertise with developing reports with an executive summary that presents findings and analysis of the information collected both from the qualitative and quantitative of a public pension related initiative and any recommendation made as part of the report..

Audit report to our auditors and Auditor Generals

As indicated in a previous section, our pension actuarial group performs more than 150 pension audit supports annually, among which 15 to 20 relate to public pension. These are used for Deloitte audits but also for supporting Auditor Generals. In performing our work, we do prepare formal reports and working papers. These documents need to be orderly prepared and contain the necessary requirements to support the audit. The usual documentation includes:

- background section
- tailored executive summary portion
- section detailing our approach
- section with the findings for each of our tests (methodologies, assumptions, events, expense, asset ceiling, …)
- section with the list of professionals that were involved
- finally, a list of detailed working papers is also included

We prepare the structure of our reporting in order to maximize the understanding of the work performed and the findings. We have found by use with auditors and Auditor Generals that this answers the need for documentation. We specifically received great feedbacks from working with external stakeholders on how the information communicated was complete, to the point and easily accessible. We believe that we have shown expertise in preparing these documents over the last few years and we will use this to ensure optimal communication with OPC and the stakeholders.

Government analysis of accounting approach

We did perform a pension review of the major public pension plans in Canada for the Quebec government. This document was meant to cover main plan provisions, main assumptions used, accounting results and methodologies. We did perform the analysis, summarized the information received and prepare the necessary report. Reporting to a Government, we did structure our report again to have a succinct but complete executive summary. The document needed to cover all steps of the work and really tie to the objectives that were set out initially. We did work this in a collaborative approach with the Government representatives and therefore ended doing some back and forth iterations to incorporate both our views of what made it a successful document that would answer the stated objectives but also include the Government views about what wording might be more appropriate to some stakeholders. We still had the ultimate responsibility to define the structure based on the work we were performing and findings in the course of the mandate. We also think that this shows our experience in this type of communication and will help us ensure high-quality work to OPC.

Shared risk plan white paper

Another example of reporting on public pension plan is the work we did with the Government of NB to define the accounting treatment for transition of a traditional DB plan to a Shared Risk Plan model. This work required us to really cover a highly complex accounting issue but also having legislative and actuarial complexities. We performed the analysis of the legislation and the accounting and prepared a report with our findings. An executive summary was needed to ensure the conclusion of our analysis was highlighted appropriately and the main elements leading to it were also summarized. As this is a complex issue, numerous subsections covering the plan details, the legislation considerations, the valuation reports, the funding and benefit policy, and the accounting standards were also included in the reporting. This work shows that we do have the expertise to translate complex issues into accessible documentation and provide with a summary that adequately covers the issue, the process and our conclusions.

Analysis of Pension Valuation Allowance Accounting Considerations

Our final example of reporting on public pension plan is the recent work we did with the OPC to define the methodology for determining the accounting treatment of plans in an asset position. We received information from the OPC for plans in an asset position including Funding Policies, Actuarial Funding Valuations, and current accounting results. We then prepared an analysis of the applicable Pension Acts and the accounting standards to ensure our methodology was sound in relation to both. Finally, we calculated any asset impairment at different levels of testing. We prepared an executive summary as the conclusions from our analysis leveraged several working papers and the calculation methodology relied on several inputs, the public sector accounting standards, and the applicable Act. This work shows that we do have the expertise to effectively communicate qualitative elements that govern a process such as the valuation test as well as proposing methods for successfully quantifying these elements.

Schedule E – Ceiling Test and Sensitivity Analysis

Each Vendor should provide in its proposal:

- Describe the proponent's demonstrated knowledge, skills, experience and expertise with running different ceiling tests and sensitivity analysis scenarios including providing ceiling tests and sensitivity analysis advice. Cite examples to demonstrate experience and describe results achieved. .

Quebec municipalities Ministry for application of PS3250 and PS3255 standards

Through the implication with the Québec municipalities Ministry Deloitte has provided a number of recommendations on accounting treatment of some events / issues that are closely looked at by the Auditor Generals. We have been involved in the treatment of special events including the asset ceiling and its accounting treatment. PS3250 has extreme volatility consequence for asset ceiling while IAS19 has some self-correcting mechanisms that help alleviate this extreme fluctuation. At some point, this element did become a sensitive issue for some municipalities' pension plans. We were involved with the Ministry to define a possible recommendation of how this would be applied and eventually determine some recommendation to mitigate the taxation impact for municipalities. Our expertise in PS3250 combined with our knowledge of IFRS for asset ceiling proved to be important to provide the needed support.

Comprehensive review of the ceiling test under PS3250

In preparation of the Province of Ontario's Financial Statements, Deloitte was engaged by the OPC to provide support in analyzing issues around pension accounting. A key element of the work prepared was the assessment of the application of the public sector accounting standards as related to asset ceiling and valuation allowance. Our work included review of two large Ontario plans for which we preparesd a document with the following details for each:

- Summary of the accounting situation
- Overview of the accounting paragraphs that apply to this and the explanation
- Review of the considerations that go into the ceiling test and the Future Economic Benefit (FEB) calculation
- Review of the employer access to future contribution reduction or surplus withdrawal
- Summary of findings relating to observations made in discussing the applicability of the asset ceiling test for Ontario's 2015-16 Financial statements

One section above the rest from the document we prepared for the OPC highlights our expertise with running different ceiling tests and scenario testing. Within our review of the consideration that go into the ceiling test and the Future Economic Benefits (FEB) calculation, we highlighted the main components of a ceiling test including notion of an open group, future service accruals on an accounting and funding basis, required contributions and contribution holiday. Further, we defined different levels of testing in regards to the minimum contribution that we ran through testing and projection. This allowed us to work through different examples with OPC, going from a basic testing to a very comprehensive level of testing under PS3250.

This experience has allowed Deloitte and the OPC to better understand the asset ceiling notion and the concepts that go into it.

Asset ceiling and annual audits

As indicated previously, our pension actuarial team supports Deloitte audit teams on a large number of annual audits. Although not always applicable, there are number of plans that show an asset position and for which testing of the amount presented needs to be performed. Even more complex, the test under IFRS, including IFRIC14 requires usually some projection of results to validate the asset position. So our team does have extensive experience in these issues, calculations and discussions with clients / actuaries. As an illustration, you can refer to the section on similar projects where we noted that under IFRS, for 3 main clients of Deloitte, we did have asset ceiling consideration this year due mainly to the plans being closed to new entrants and for which we did go through a comprehensive process with the clients and actuaries.

Sensitivity and Scenario Analysis for Audit

As actuaries in a large Audit firm, we act as the pension specialists for many pension and benefit plans. Each of these engagements has a defined scope but typically it involves the review of actuarial assumptions and review of the accounting results to gain comfort with the movements of the obligation, plan assets, profit and loss, and other comprehensive income where applicable. To completely gain comfort, reviewing both assumptions and results, we must use both sensitivity and scenario testing.

When reviewing actuarial assumptions, particular assumptions depend on stochastic projections. For example:

- For plans under all standards, if there is an element of increase of pensions in payment that is linked to the Consumer Price Index (CPI) or the return on assets, we will perform stochastic projection. For illustration, if a plan assumed an annual increase of pension in payment of 1.2%, and the plan formula for the increase was the maximum of a) 50% of CPI and b) 75% CPI minus 1%, we would perform a stochastic projection of inflation levels over future years to determine the likely distribution for what the underlying indexation would be. Finally we would compare our expectation with the assumption retained. Doing so will require some modelling for projection of future events like CPI.

- For plans under US GAAP and PSAS, there is use of the expected return on assets assumption. When there is an expected return on assets assumption, we would look at the plans target investment strategy (the distribution of total assets into asset classes), and then we would perform a stochastic projection of these asset classes over a defined period to determine the likely distribution for what we would expect the aggregate return to be. This would be compared with the assumption retained. So again, we do use modelling into our regular work.

Sensitivity analysis is a particularly useful tool for completing our review of accounting schedules. For example:

- For reconciliation of the benefit obligation to explain how it evolves every year, there are 3 main elements of gain/loss; change in financial assumptions, change in demographic assumptions, and plan experience. When there is a change in the assumptions, this will result in some element of gain/loss whether it's very minimal or large. In order for the Deloitte team to determine the impact of changes in assumptions, we often rely on sensitivity testing. A common example is determining the impact of a 100 bps decrease in the discount rate. We would use the plan duration, which is the sensitivity of the cash-flows, and determine the percentage increase in pension benefit obligation from a 100 bps decrease in the discount rate.

  Other assumption changes may also incorporate sensitivity analysis; change in retirement assumption may rely more on active member duration, change in the indexation for deferred members may rely more on deferred member cash-flow sensitivity, change in the mortality assumption may rely on the complete cash-flows sensitivity to all members living an extra year. We will make use of the actuarial knowledge we have about how an obligation for a member is valued. We also have available valuation tools that help us estimate the impact of very specific assumption changes. Our proposed team members have been involved in actuarial valuation preparation and actuarial results review hence they are very familiar with the elements that go into the calculations.

Finally, for sensitivity, we can also mention that our team often supports the disclosure for sensitivity results. When entities present such information in their notes, often seen under IFRS, the actuarial team will support the auditors in assessing whether a change in obligation value disclosed is acceptable based on the actuarial principles and calculations. Our actuarial group would prepare a similar analysis to validate the actuary results. In a similar manner, we provide support to audit teams at the start of their audit process when they identify what are the major risks to be reviewed and covered. To do this, our team will prepare sensitivity analysis of the main plan assumptions to calculate the impact on the obligation and help the audit team determine if this change is material for the audit work and therefore represents a major risk.

Schedule F – Methodology and implementation plan

Each Vendor should provide in its proposal:

- The proponent shall describe the methodology and implementation plan they will use to deliver the Client's Requirements as described in Section 1.5 of this RFS.

From Section 1.5 of the RFS

- Working with management of the OPC's Accounting Policy and Financial Reporting Branch (APFR), to provide actuarial services related to the following possible areas:
    - Review APFR's calculation of estimated accounting valuations based on actuarial input for pension plans reflected on the Province's consolidated financial statements (Ontario Public Service Employees Union Pension Plan, Ontario Teachers' Pension Plan, College of Applied Arts and Technology, Health Care of Ontario Pension Plan and Public Service Pension Plan) as well as post-retirement benefits
    - Conduct related sensitivity and/or scenario analysis as requested by APFR
    - Participate in discussions and meetings with internal and external stakeholders, as required

- Working with management of the OPC, through the (APFR), provide actuarial services related to the following possible areas relating to the Ontario Public Sector Employees Union Pension Plan and Ontario Teachers' Pension Plan:
    - Design and execute various valuation models, as requested by APFR, relating to the ceiling test requirements in the CPA Canada public sector accounting handbook (PS3250.050 to PS3250.059)
    - Conduct sensitivity and/or scenario analysis as requested by APFR
    - Provide advice to APFR, for accounting purposes, on the ceiling tests and sensitivity analysis
    - Participate in discussions and meetings with internal and external stakeholders, as required

Implementation – start of mandate

In order to start the mandate on a solid basis, we believe that a first initial meeting between Deloitte and OPC would be the best first step. As Martin, Trevor, and Matt, are all familiar in working with OPC, we suggest that these three team members join the meeting on behalf of Deloitte to ensure that the mandate starts on the right track and uses most optimal approach.

Having worked with OPC recently on a previous accounting mandate, we do have a good understanding of the process and approach that will help deliver the necessary results. Still, in this initial meeting, many elements of process and basic information will be covered like:

- Identify the key personnel on both sides and define their expected role
- Review the list of pension plans that are to be covered
- Identify the documents that are to be made available (valuation reports, plan texts, internal procedures, financial statement notes, assumption selection documents, APFR's calculations)

- Identify the list of issues that are currently foreseen
- Key Internal and External stakeholders that are foreseen to be involved in discussions and meetings
- Discuss the other elements that may be of concerned based on our experience
- Agree to the communication procedures for information
- Define the expected process for any formal advice / recommendation prepared

Although the scope of work description under 1.5 of the RFS does not clearly identify tangible deliverables or definite milestones and delivery dates, we have identified below how we would proceed to get the main activities to a conclusion. These activities are identified as follows:

- Review of calculations used for pension and other benefits reporting under PSAS
- Design and execute valuations models related to the ceiling test under PSAS
- Conduct sensitivity/scenario analysis
- Participate in meetings

Review of calculations used for pension and other benefits reporting under PSAS

This activity covers most of what our work is likely to focus on. Our goal is to act as an internal control for the APFR. By leveraging our expertise auditing plans under PSAS, we will provide in-depth analysis and give value-add feedback.

Step	Description
Initial discussion with the OPC	Identify the plans in scope Identify whether we are looking at calculations and /or assumptions Identify calculations that the APFR believes require more scrutiny Identify the documents required for the work to be performed Get initial reaction from OPC
Review of plan document	Review documents provided to ensure all necessary information is obtained Identify any constraints or missing information that needs to be requested
Discuss Work Papers (WPs) to be prepared	Identify what OPC would like to see as a deliverable from Deloitte Use or amend Deloitte templates that will be in line with OPC's expectations
Prepare and Perform review of APFR's calculations	Use Deloitte WPs to perform review Provide a work document summarizing findings and Deloitte WPs Identification of any issues Define the options available in regards to any possible issues Give advice / guidance on possible issue
Discuss the analysis with OPC	Send the Deloitte WPs to OPC Run through the main elements of the review performed and the conclusions Discuss the options available in regards to possible issues

Although the deliverable may differ somewhat in format based on the needs, it will contain these most likely elements:

- Summary of the work (background)
- Identification of the documents used and prepared
- Identification of any issues that have arose

- Summary of calculations and steps performed
- Summary of the conclusion reached

Design and execute valuations models related to the ceiling test under PSAS

This activity covers a very specific area of the pension accounting standards. It is an element that needs some judgment and also that needs a comprehensive analysis to document appropriately the position taken. The asset ceiling test will be required when the plan presents a surplus and shows an asset on the balance sheet. This is done on a plan by plan basis. It does encompass a notion of future economic benefit (FEB) that requires the Government to define what it believes can represent a benefit in form of either surplus withdrawal or future reduction in the Government contribution through contribution holiday. The asset ceiling is important since based on the accounting standards, it does have an immediate impact on the annual expense of the Government and thus may be a very volatile component when the asset ceiling applies. Here are the steps we think could be taken to provide expertise to the specific situation of the Government. Much of this work will be leveraged from our prior engagement with OPC as a starting basis.

Step	Description
Initial discussion with the OPC	Identify the plans that are to be modelled Determine the various components of the test and how it is to be applicable Discuss for the affected plans the initial view on whether the Government could take some contribution holiday, if so on what circumstances Identify if one approach applies to all plans or if different situations exist (ex a closed plan)
Obtain the necessary documents	Accounting results for the affected plans Supporting plan text/funding policy for contribution holiday judgment Initial analysis that exists at OPC
Prepare an analysis of the situation for the plans	Define and structure the valuation model Prepare the assumptions that will be included in the model Based on the elements defined above, determine the FEB components for the affected plans
Perform valuation models	Determine possible contribution holidays FEB calculation basis Impact of the asset ceiling
Discuss the valuation models with OPC	Send the valuation models documents to OPC Run through the main elements of the analysis performed and the conclusion
Prepare formal communication	Depending on the needs, could take the form of a revised analysis or more formal document to be used with Auditor General or other external stakeholders

Some key elements are really important to look at when preparing this analysis:

- Valuation basis used for plan assets (market-related value?)
- Possibility of Contribution holiday – what supports this and what are the constraints
- Well-defined process to calculate this since it is a very complex element of accounting that not all stakeholders fully understand and can appreciate the accounting requirements
- Actuarial assumptions to include in projection

Conduct Sensitivity/Scenario Analysis

The scope of this engagement is similar to internal audit procedures we have experience with. Internal audit typically encompasses an element of sensitivity testing as a form of checks and balances. A sensitivity test will lend another layer of review. For example, we may see that an assumption changed from year-to-year and we would like to better understand if the impact makes sense. If we perform a sensitivity analysis, and we see 100 bps movement results in an impact of 10%, then a 50 bps movement should result in an impact of approximately 5%. Sensitivity is also a useful tool for shedding light on elements of risk.

Stochastic projections performed in tandem with different liability projections is a very robust form of scenario testing that OPC can also consider when working with us. By running 1000's of different scenarios to project the asset position in future years, OPC will have a more complete picture of a plan position.

Step	Description
Initial discussion with the OPC	Identify OPCs goals from the tests performed Understand OPCs 2017/2018 budget concerns Identify calculations that sensitivity analysis could prove to add value Identify concerns OPC may have in regard to certain future changes Determine which sensitivity/scenario tests will be performed Identify the extent of sensitivity to test (level of assumption change)
Prepare Sensitivity/Scenario analysis	Determine the impact of each test on the 2017/2018 budget
Deloitte and OPC discuss the outcome	Discuss the results of the testing Link the testing results to the initial goals of OPC Identify subsequent needs, if any

Some key elements are really important to look at when preparing this analysis:

- Assumptions / scenarios to be tested, horizon for the test
- Impact of changes in assumptions
- Impact of changes in methodology such as determining the Market-Related Value of Assets

Participate in meetings

This activity covers our presence and participation to meetings. It can be for internal or external stakeholders. It can be for meetings where we are more receiving information (ex Auditor General providing its view on one key accounting element and asking questions) or were we are presenting results of our analysis. So depending on the needs, we will adjust our work accordingly. Below is one situation where we are presenting analysis. In this case, we would have worked through the advice and guidance steps to work the analysis (activity described just before) and here we just identify the specific steps for the meetings.

Step	Description
Initial discussion with the OPC	Identify the participants to the meeting and their level of expertise Identify the meeting date and the location, length of meeting, agenda Identify the expected outcome for OPC Identify the key messages that are to be delivered Identify the role that OPC and Deloitte play in the meeting Determine the presentation support needed (document, power point, one-pager)

Step	Description
Prepare the necessary documents based on the advice / guidance analysis performed	Prepare the document Keep it accessible Use an approach of building the understanding from basis up to the conclusion Use as much as possible standards reference to support the conclusion
Review with OPC the document prepared	Review document for content Clarify elements that need to be adjusted Identify new elements to be added as needed
Identify questions	Define queries that may come up Identify weaknesses of document that may be questioned Prepare for likely answers to these should they come up Identify who between OPC and Deloitte handles the question part
Present document at the meeting	Introduction of the people present and role Identification of the objective of the meeting Formal presentation, answer questions
Post-meeting discussion	Review with OPC how the meeting went Identify elements that may need to be improved in the analysis Determine if a follow-up document needs to be prepared Identify if some questions were not answered appropriately and need subsequent answer, if so identify timeline for it Identify if we are waiting for some feedbacks or comments after the meeting
Follow-up	If questions needed subsequent answers If feedbacks or comments were expected

Although the deliverable may differ somewhat in format based on the needs, we will ensure that the content will be prepared considering the following

- The expected level of understanding from the participants
- The time allowed for the presentation
- The goal of the meeting (what we want to achieve).

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Fw_ Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20).rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Fw: Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20)
Date: Monday, February 06, 2017 17:41:27
Attachment 1: image001.gif
Attachment 2: SOW - Actuarial Support Services.pdf

From: Sarah Anderton <Sarah.Anderton@ca.ey.com>
Sent: Monday, February 6, 2017 4:12 PM
To: Virani, Shyrose (TBS)
Cc: Uros Karadzic; Shayan Jafrani
Subject: RE: Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20)

Hi Shyrose,

Please see attached.

Thank you,

Sarah

--

Sarah Anderton | Executive Assistant | Enterprise Support Services | People Advisory Services

Ernst and Young LLP

Office: 416-943-3143 | sarah.anderton@ca.ey.com

From: Virani, Shyrose (TBS) [mailto:Shyrose.Virani@ontario.ca]
Sent: Monday, February 6, 2017 2:59 PM
To: Sarah Anderton <Sarah.Anderton@ca.ey.com>
Cc: Uros Karadzic <uros.karadzic@ca.ey.com>; Shayan Jafrani <Shayan.Jafrani@ca.ey.com>
Subject: RE: Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20)

Thanks, Sarah, can you please add Christina Chan's name in the SOW and then I will have Nadine sign off.

Thanks

Shyrose

From: Sarah Anderton [mailto:Sarah.Anderton@ca.ey.com]
Sent: February 6, 2017 1:33 PM
To: Petsche, Nadine (TBS)
Cc: Anna Pesme; Uros Karadzic; Virani, Shyrose (TBS)
Subject: Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20)

Hello,

Please see the draft SOW for Actuarial Support Services attached.

Thank you,

Sarah

--

Sarah Anderton | Executive Assistant | People Advisory Services

Ernst and Young LLP

Ernst and Young Tower, 222 Bay Street, P.O. Box 251, Toronto, ON M5K 1J7, Canada

Office: 416-943-3143 | sarah.anderton@ca.ey.com

Website: http://www.ey.com

From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Friday, February 03, 2017 11:08 AM
To: Anna Pesme <anna.pesme@ca.ey.com>
Cc: Virani, Shyrose (TBS) <Shyrose.Virani@ontario.ca>
Subject: Draft SOW for Actuarial Support Services (RFS # TBS-OTB-OPCD-20)

Ms. Pesme,

As discussed, please find attached the draft Statement of Work related to Actuarial Support Services.

We look forward to working with your team on this engagement.

Regards,

Nadine Petsche

Director, Accounting Policy and Financial Reporting

Office of the Provincial Controller Division

416 325 8027

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image001.pdf

SOW - Actuarial Support Services.pdf

FORM OF STATEMENT OF WORK – OPS ENTITY

Statement of Work for Management Consulting Services

This Statement of Work No. **RFS TBS-OTB-OPCD-20 made in duplicate and effective February 3, 2017 ending on September 30, 2017.**

Ernst & Young LLP (the vendor" or "EY") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of June 16, 2014 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$ $150,000 does not include HST

4. *Project Start Date:* February 3, 2017

5. *Project End Date:* September 30, 2017

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following

    1. Taking into account public sector accounting principles, advice and guidance on complex accounting and reporting matters related to accounting for pensions on the Working with management of the Office of the Provincial Controller's Accounting Policy and Financial Reporting Branch (APFR), the Vendor will provide actuarial services related to the following possible areas:
        - Review APFR's calculation of estimated accounting valuations based on actuarial input for pension plans reflected on the Province's consolidated financial statements (Ontario Public Service Employees Union Pension Plan, Ontario Teachers' Pension Plan, College of Applied Arts and Technology, Health Care of Ontario Pension Plan and Public Service Pension Plan) as well as post-retirement benefits.
        - Conduct related sensitivity and/or scenario analysis as requested by APFR.
        - Participate in discussions and meetings with internal and external stakeholders, as required.

    2. Working with management of the Office of the Provincial Controller, through the Accounting Policy and Financial Reporting Branch (APFR), provide actuarial services related to the following possible areas relating to the Ontario Public Sector Employees Union Pension Plan and Ontario Teachers' Pension Plan:
        - Design and execute various valuation models, as requested by APFR, relating

to the ceiling test requirements in the CPA Canada public sector accounting handbook (PS3250.050 to PS3250.059).
- Conduct sensitivity and/or scenario analysis as requested by APFR.
- Provide advice to APFR, for accounting purposes, on the ceiling tests and sensitivity analysis.
- Participate in discussions and meetings with internal and external stakeholders, as required.

7. *Ownership and Licences* – Attachment D of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Ernst & Young's working relationship with OPCD is vital to the success of their engagement. The Project Lead that will handle OPCD work is Uros Karadzic. Ernst & Young's communication strategy will be centred on periodic project update meetings, the frequency of which will be determined by the OPCD and Ernst & Young.

9. *Work Location* - All meetings will be within Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive.

    If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Fixed Price or Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Billing and Payment Process* – The Vendor shall provide the Client with quarterly billing statements that outline the per diem charges no later than 10 Business Days after the end of each quarter.

    Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Name of Individual	**Level**
Uros Karadzic	Senior Consultant/Project Lead
Shayan Jafrani	Intermediate Consultant/Sr. Analyst
Christina Chan	Consultant/Analyst

Note that participation of Uros Karadzic will commence only upon completion of his engagement with the Pension Asset Expert Advisory Panel.

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

    Client: Treasury Board Secretariat
    Office of the Provincial Controller Division

Branch: Accounting Policy and Financial Reporting
Representative: Nadine Petsche
Title: Director, Accounting Policy and Financial Reporting
Phone Number: 416 325 8027
Email: Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Client's designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Indemnity* – the indemnity set out in the Master Agreement applies to this assignment.

18. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416 325 8027**
E-mail:	**Nadine.petsche@ontario.ca**

19. *Vendor Representative and Receipt of Notices*

Uros Karadzic, Partner
Ernst & Yojng LLP
Ernst & Young Tower
P O Box 251
222 Bay Street
Toronto ON M5K 1J7

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

Her Majesty the Queen in right of Ontario as represented by The President of the Treasury Board

Per:

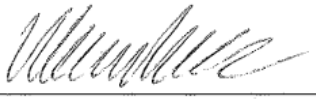
Signature:

Name: **Nadine Petsche**

Title: **Director, Accounting Policy and Financial Reporting**

Pursuant to delegated authority.

Per:

Signature: 

Name: UROS KARADZIC

Title: PARTNER

I have the authority to bind the Vendor.

Fw_ Expert Panel - end of work.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: Expert Panel - end of work
Date: Monday, March 27, 2017 11:09:17

Original Message
From: Uros Karadzic <uros.karadzic@ca.ey.com>
Sent: Monday, March 27, 2017 11:02 AM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani; Christina Chan
Subject: RE: Expert Panel - end of work

I am looking forward to it as well, Nadine!

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP
Office: +1 416 943 2087 | Mobile: +1 416 970 2087 | uros.karadzic@ca.ey.com
Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

-----Original Message-----
From: Petsche, Nadine (TBS) [mailto:Nadine.Petsche@ontario.ca]
Sent: Monday, March 27, 2017 10:50 AM
To: Uros Karadzic <uros.karadzic@ca.ey.com>
Cc: Shayan Jafrani <Shayan.Jafrani@ca.ey.com>; Christina Chan <Christina.Chan@ca.ey.com>
Subject: Re: Expert Panel - end of work

Good morning Uros. Thank you for your email. Since your work on the Panel is complete, we look forward to your participation on the pension engagement following your PSAB taskforce meetings.
Best regards,
Nadine

From: Uros Karadzic
Sent: Monday, March 27, 2017 9:14 AM
To: Petsche, Nadine (TBS)
Cc: Shayan Jafrani; Christina Chan
Subject: Expert Panel - end of work

Hi Nadine,

I've just submitted my timesheet to Nelson for the Expert Panel work. I believe we are now done, although my understanding is that the official mandate only ends on 31st.

I'm in all-day PSAB Taskforce meetings until Thursday, but following that please let me know if you're now comfortable with me joining Shayan and Christina.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7, Canada
Office: +1 416 943 2087 | Fax: +1 416 943 2201 |
uros.karadzic@ca.ey.com<mailto:uros.karadzic@ca.ey.com>
Mobile: +1 416 970 2087 | EY/Comm: 1685272
Website: http://www.ey.com/ca
Assistant: Sarah Anderton | Phone: +1 416 943 3143 |
sarah.anderton@ca.ey.com<mailto:sue.lentze@ca.ey.com>

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Any tax advice in this e-mail should be considered in the context of the tax services we are providing to you. Preliminary tax advice should not be relied upon and may be insufficient for US penalty protection. Tout conseil de fiscalité contenu dans le présent courriel doit être pris dans le contexte des services de fiscalité que nous vous offrons. Aucune décision ou position ne doit être prise à la lumière de conseils de fiscalité préliminaires, lesquels pourraient ne pas permettre d'éviter des pénalités aux États-Unis.

Fw_ Meeting to review proposed Cap and Trade accounting.rtf

From: Petsche, Nadine (TBS) []
To: Taylor, Heather (MOECC) [Heather.Taylor@ontario.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: Meeting to review proposed Cap and Trade accounting
Date: Wednesday, November 23, 2016 13:10:39
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx
Attachment 2: Cap and Trade accounting implications - memorandum to file v5 November 2....docx

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FYI. Would be great if you could join if you're available. Meeting will likely be 1 1/2 hours. Nadine
Attachments are ?privileged and confidential?

updated memo attached for tomorrow's discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

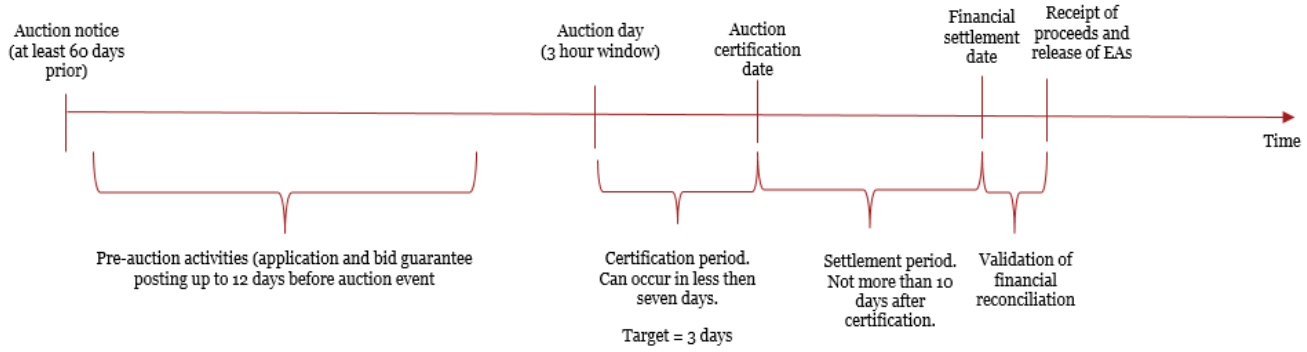
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

<table>
<tr><td>Indicator</td><td>Auction day</td><td>Auction Certification date</td><td>Financial Settlement date</td><td>Receipt of proceeds and delivery of EAs</td></tr>
<tr><td>Present right to payment</td><td>Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.</td><td>Yes. Under the contract payment must be received prior to delivery of EAs</td><td>N/A payment must be received before this date</td><td>N/A payment must be received before this date</td></tr>
<tr><td>Legal title to the asset</td><td colspan="3">Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.</td><td>However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.</td></tr>
<tr><td>The entity has transferred physical possession of the asset</td><td colspan="3">This indicator is not entirely relevant as EAs do not have physical form.</td><td>However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.</td></tr>
<tr><td>The customer has accepted the asset</td><td colspan="4">There are no customer acceptance clauses. This indicates is not relevant.</td></tr>
<tr><td>The customer has significant risks and rewards of ownership of the asset.</td><td colspan="4"></td></tr>
</table>

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

<u>Is there a liability created?</u>

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Cap and Trade accounting implications - memorandum to file v5 November 2....pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [INTD – *MOECC to provide comments on accuracy of background terminology*]

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The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: ~~There~~In accordance with the Regulations there are four auctions a year. ~~MOECC determines~~ EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, ~~and how many of each "the vintage"~~after the distribution of ~~the EAs is available.~~free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage~~", but more~~". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which

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case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value~~.~~, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

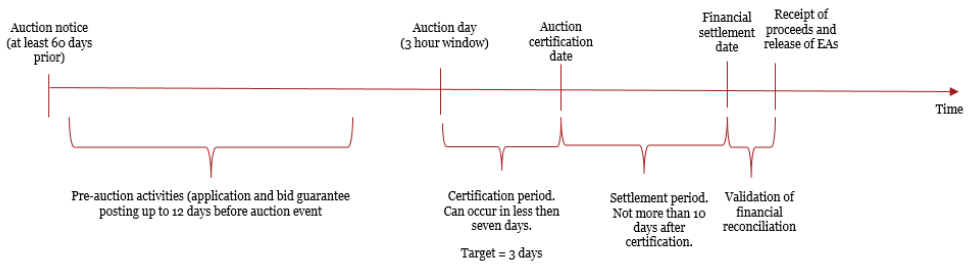
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB~~).~~.) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's regulations.~~regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices~~.~~ by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days~~, in~~ into their sub-account, which ~~case~~ is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once ~~payment has~~all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

~~[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]~~

Auction timeline illustration



Free allowances

~~Mandatory and capped~~Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant~~.~~ and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period~~.~~ (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations~~.~~ and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If

they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits ~~for early action~~" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall~~.~~, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities

of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

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- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

~~3.~~4. *Identification of assets relating to the cap and trade program as sponsoring government*

Summary of relevant guidance – See Appendix ~~A~~C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation ~~and sales~~ of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction~~transfer of funds into the Province's escrow settlement account.

   ~~On the~~After auction ~~date, a receivable~~certification cash from successful bidders is ~~recognized by the Province for the sale of EAs.~~transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized ~~in Revenue~~as deferred revenue until the contract is settled by the transfer of EAs to the participants (see ~~Part 5).~~section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

~~c)~~d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

~~d)~~e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

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Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date:*~~

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr ~~Receivable (from successful participants/Escrowed amounts)~~

~~Cr Revenue~~

~~Dr Cost of sales~~Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

~~*On settlement date:*~~

~~Dr Cash~~

~~Cr Receivable (~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants~~/Escrowed amounts~~

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

~~*Analysis*~~

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a) On creation ~~and sales~~ of free and auctioned EAs:

EAs are "goods" created to be sold or distributed to participants~~. These~~ (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. ~~Therefore despite being intangible in nature,~~ PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs ~~also~~therefore meet the definition of inventories held-for-sale ~~and~~as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

~~EAs that are returned to the government and not cancelled due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).~~ PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory. ~~[ASK MOECC CREATION PROCESS – EXPECTATION IS THAT NO FIXED PRODUCTION OVERHEADS EITHER – ALL WOULD BE GENERAL MANAGEMENT I.E. IF NO PRODUCTION OCCURRED WOULD ANY OVERHEAD COSTS BE ELIMINATED.]~~

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~ EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for

production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead to~~provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the ~~proceeds~~ cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids~~, or~~ and therefore if their bids are successful ~~and therefore whether~~. Only successful bids give the Province ~~has~~ any rights to the escrow proceeds ~~prior to the auction being held. Rather~~. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed ~~amounts. [NTD – to confirm]~~cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a~~

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[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

~~market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

~~*Measurement of receivable:* The receivable would be measured at the auction price, being the amount of consideration expected to be received from the sale. Due to the bid guarantees it would be expected that the full auction price would be received. [IF EXPOSED TO DB CREDIT RISK MAY NEED TO ADD SOMETHING REGARDING BAD DEBT EXPENSE]~~

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the

restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected: ~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province~~It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders~~, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued

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that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected: ~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

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~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

~~c)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can

deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs~~. This alternative view would be consistent with a~~ as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section ~~4~~5 below~~.~~ and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. ~~Therefore~~ The only exception is when EAs for a future compliance period are received as part of the ~~right to receive an EA is also not an asset. The~~3 for 1 increased compliance obligation as these may be

re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold ~~(i.e. those remitted~~ or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations~~) and so any~~. Any recognition of an asset for the right to receive back ~~was recognized for~~ applied to all EAs~~,~~ would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not ~~appropriate accounting~~a fair presentation.

~~d)~~e) Failure of participant to pay increased compliance obligation:

~~The~~An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations~~. As participants~~ as they can ~~settle their obligations with~~purchase additional EAs ~~that~~on the market at the market price. EAs do not enhance or create expected economic future benefits for the government~~. It~~ for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is ~~only when~~linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs ~~that~~and under legislation the Province has a right to demand cash as settlement of the compliance obligation~~.~~ (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: ~~The~~ There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues*. However, it would be consistent with PS 3510 and other standard to recognize the receivable ~~would be recognized~~ at the amount expected to ~~-~~be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

~~4.~~5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial ~~liability~~liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub-accounts.

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Analysis~~Loan guarantees and contingent liabilities: **EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent that there are escrowed proceeds held over a balance sheet date disclosures of the implicit loan guarantee should be made, if material.~~

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~
~~[NTD – position to be confirmed based on discussion of insolvency risk with DB~~

~~c)~~ Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once~~accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]~~

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~~*Analysis*~~

a) ~~Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.~~

a) ~~Once~~ the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them ~~in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed~~ for cash or any other financial asset, or ~~exchanged~~exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

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After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach ~~and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.~~. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

~~Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as~~

~~there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.~~

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to ~~deliver~~transfer "goods" (being the free EAs) in total or to specific participants. ~~Ultimately however, the~~The delivery of free EAs is a transition mechanism and is ~~at the discretion of the Province, rather than a contractual or constructive obligation~~non-reciprocal (as opposed to the ~~participants, as the Province retains discretion over the issuances~~sale of EAs which is a reciprocal transaction). The transfer of ~~free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC~~EAs is not ~~comfortable with the idea~~technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is ~~no~~an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs~~]~~. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

~~*Alternative positions considered and rejected:* It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the

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Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section ~~5~~6 below.

~~c) Loan guarantees and contingent liabilities: [TBD – To be supported by facts, if any, that indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]~~

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~5.~~6. Revenue recognition under the cap and trade program as sponsoring government

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This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix AC for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position – The sale of EAs are exchange transactions.

***Analysis*:**

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

***Alternative positions considered and rejected*:** An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in

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~~order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.~~

~~Revenue recognition for sale of EAs (Exchange transactions)~~

~~*Relevant guidance* - See Appendix A for details.~~

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the ~~auction~~ date of delivery of the EAs as ~~there are no further substantive~~this is when the performance ~~obligations~~obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation~~?~~ for the sale of EAs? A performance obligation is defined in IFRS 15~~/ASC 606~~ a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". ~~This~~The following analysis has applied the IFRS concept, as permitted under PS 1150.

~~a)~~ In both IFRS 15~~/ASC 606~~ and the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the ~~standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the~~

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~~enforceable rights and obligations that are entered into when an auction occurs.~~auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix ~~A~~C for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction~~,~~ as confirmed in the auction certification process. The Province has ~~only one~~ distinct performance ~~obligation~~obligations to deliver each EA to each successful bidder under ~~this contract, which is the delivery of the EAs~~these contracts.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in ~~4~~5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions~~.~~ as settlement of their compliance obligations. Therefore ~~this~~Ontario has no obligation to redeem ~~cannot arise~~an EA that arises from the original exchange transaction and ~~is~~ therefore ~~not a~~there is no performance obligation ~~of~~ that ~~transaction~~exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at

auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program~~,~~ and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written ~~of~~or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15~~/ASC 606~~ the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP proposes a "control" model similar to IFRS 15~~/ASC 606~~, so this approach has been applied in the analysis. Under IFRS 15~~/ASC 606~~ an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15~~/ASC 606~~ provides indicators of when a point-in-time obligation has been satisfied. These are also included in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP and have been considered in this analysis. See IFRS 15.38 in Appendix ~~A~~C. The indicators have been assessed as follows:

~~Present right to payment – As noted in Section 3 above, there is a present right to payment at the auction date.~~

~~Legal title to the asset – Legal title is transferred when the EAs are credited to the participants account. This occurs after the auction certification and settlement process is completed. [MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

~~The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.~~

~~The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the auction date. If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the auction. While EAs are credited to a~~

~~participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

~~The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.~~

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset. Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or	Possibly – the price	Yes – From this date	N/A already met	N/A already met

suffering from the fluctuations in the market price of EAs	that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.		

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the ~~auction date.~~date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected: ~~It was considered whether revenue should be recognized at a point in time when the EAs are credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

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Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for

participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.

- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix ~~A~~C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. ~~[NTD – to confirm that all interested parties agree with this statement]~~

~~6.~~7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

~~7.~~8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

~~8.~~9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

~~9.~~10. Implementation risks and audit considerations

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Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

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Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35~~-.37.~~.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not ~~defined under PSAS.~~specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and ~~OS~~PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). ~~After the adoption of PS 3450, which is currently effective for the Province for~~

~~fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.~~

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

~~PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).~~

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Formatted: Normal, Space Before: 0 pt, After: 0 pt, Line spacing: single

Fw_ PRIORITY - please amend SOW to add the noted individual.rtf

From: Petsche, Nadine (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: PRIORITY - please amend SOW to add the noted individual
Date: Sunday, October 16, 2016 23:44:14

From: Nadine.Petsche@ontario.ca
Sent: Sunday, October 16, 2016 11:42 PM
To: lucy.durocher@ca.pwc.com
Cc: Shyrose Virani
Subject: Re: Outline of position paper proposed allocations Oct 7.docx

Thanks Lucy. I am copying Shyrose on this response. I think we would likely just need his name and to get the necessary clearance in place. Shyrose will be in touch if further details are required.
Regards,
Nadine

From: lucy.durocher@ca.pwc.com
Sent: Sunday, October 16, 2016 11:22 AM
To: Petsche, Nadine (TBS)
Subject: Re: Outline of position paper proposed allocations Oct 7.docx

Hi Nadine,

In respect of one of the sections discussing the differences between the funding valuations/OTPP financial statements and the Province's financial statements, I think it would be helpful if I could get our actuary to read through the write up, particularly in respect of the funding valuation differences. Currently the SOW does not list our actuary as someone performing work (to date all my conversations with him have been high level and theoretical). However, I would like to get him added to the SOW as vendor personnel.

Individual's Legal Name
Individual's Role and Experience Level
Service Category
Per Diem Rate

Mario Chassé
General Consultant (Actuarial), Level 2
Service Category 2
See “charges on a per diem rate basis”

I can ask him to sign a confidentiality agreement.
What else should be done to ensure that the SOW reflects that he will be providing some work under the contract?

Thanks,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

From: "Petsche, Nadine (TBS)" <Nadine.Petsche@ontario.ca>
To: Lucy Durocher/CA/ABAS/PwC@Americas-CA
Date: 10/07/2016 04:02 PM
Subject: Outline of position paper proposed allocations Oct 7.docx

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Hi Lucy.
As discussed, the attached version of the paper outline includes proposed section allocations. Please let me know if any of the notes are inconsistent with your understanding.
Thanks and have a wonderful Thanksgiving weekend!
Nadine[attachment "Outline of position paper proposed alloations Oct 7.docx" deleted by Lucy Durocher/CA/ABAS/PwC]

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Fw_ Public Accounts Related Q’s.rtf

From: Petsche, Nadine (TBS) []
To: Shayan Jafrani [shayan.jafrani@ca.ey.com]
CC: Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Uros Karadzic [uros.karadzic@ca.ey.com]; Christina Chan [Christina.Chan@ca.ey.com]
Subject: Fw: Public Accounts Related Q's
Date: Monday, June 12, 2017 11:26:05

Shayan,
Below is the advice that we received from our legal services branch regarding liabilities for non-OPS employers. I think we should discuss implications to the analysis.
Nadine

From: Kaufman, Paul (TBS) <Paul.Kaufman@ontario.ca>
Sent: Thursday, June 8, 2017 4:09 PM
To: Petsche, Nadine (TBS)
Cc: Hatzis, Len (TBS); Compagnone, Lisa (TBS)
Subject: RE: Public Accounts Related Q's

Nadine, here is an analysis of the potential funding risks for the Crown relating to the participation of non-OPS employers in the OTPP and OPSEUPP. The discussion of the OTPP reflects input from EDU legal and staff who are familiar with the OTPP.

I have kept this high level given the urgency but can elaborate on specific areas as necessary. I haven't included a discussion of the general obligations of employers and members to contribute to Jointly Sponsored Pension Plans under the *Pension Benefits Act* (PBA), or discussed the implications of the exemption from solvency funding requirements under the PBA that I understand both of these plans enjoy, as I understood the focus of your question to be specific to the relationship between the Crown and other employers.

If you require anything further please let us know.

Paul

OTPP:

· The OTPP is governed by the *Teachers' Pension Act* (TPA), the Plan text for the OTPP (the "Plan Text"), a Partners' Agreement between the Minister of Education and the Ontario Teachers' Federation, and a Funding Management Policy ("FMP") that is an appendix to the Partners' Agreement.

· The OTPP is also subject to the *Pension Benefits Act* ("PBA"), under which the OTPP is a Jointly Sponsored Pension Plan (JSPP)

· Under Section 24(1) of the Plan Text, the Minister of Education is required to pay employer contributions in respect of certain active employees. These types of active employees include teachers at school boards and teachers at provincial schools (run by the Ministry of Education and where teachers are the employees of the Provincial Schools Authority).

· However, the Minister is not required to make employer contributions under the Plan Text in respect of some other employers whose employees may participate in the OTPP, including participating private schools.

· Nothing in the Plan Text (or any other applicable OTPP document or statute) expressly requires the Minister of Education to make contributions in place of private schools and other 'excluded' employers who have failed to make their own required contributions to the OTPP.

· However, the Crown could be exposed to a funding risk where a private school or similar employer fails to make their contributions in the following ways:

o Subsection 5(3) of the TPA requires the Province to make contributions to the OTPP fund if the assets in the fund are insufficient to make required payments in a particular year

o Private schools and other 'excluded employers' not making required payments could impact on the overall funded status of the plan, in turn affecting the ability of the Minister of Education and OTF to access surpluses in accordance with the FMP

OPSEUPP:

· The OPSEUPP is governed by a Sponsorship Agreement dated April 18, 1994, as amended, between Ontario and OPSEU ("Sponsorship Agreement"); a trust agreement dated October 25, 1994, as amended, the OPTrust Plan Text and the *Ontario Public Service Employees' Union Pension Act, 1994*.

· Like the OTPP, the OPSEUPP is also a JSPP under the PBA.

· A list of participating employers for the OPSEUPP is set out below (this information is derived from the OPSEUPP's most recent audited financial statements, but you may wish to verify it with the TBS Employee Relations Division). A number of the participating employers that are not part of the Province itself are nevertheless provincial agencies (AGCO, LCBO, OLGC, Public Health Ontario, etc.). The majority of the remaining employers are either public hospitals (that the Province funds) or public sector pension plan administrators. Therefore, the practical risk of a non-OPS employer failing to provide required contributions to the OPSEUPP seems quite low.

· However, in the event that such an employer did fail to make its contributions, and that failure resulted in a deficiency in the OPSEUPP fund, the Province (likely in conjunction with the other employers whose employees are members of the OPSEUPP), and the members would jointly be required to provide further contributions to the fund to address any such deficiency, pursuant to section 58 of the Sponsorship Agreement and section 6.3(5) of the OPTrust Plan Text.

• The Province of Ontario (civil servants and crown employees)

• Alcohol and Gaming Commission of Ontario

• Centre for Addiction and Mental Health

• Legislative Assembly of Ontario

• Liquor Control Board of Ontario

• Niagara Parks Commission

• North Bay Regional Health Centre (Northeast Mental Health Centre)

• Ontario Agency for Health Protection and Promotion

• Ontario Lottery and Gaming Corporation

• Ontario Pension Board

• Ontario College of Trades

• Ontario Public Service Employees Union (seconded or acting employees)

• Ontario Shores Centre for Mental Health Sciences

• Ontario Teachers' Pension Plan Board

• OPSEU Pension Plan Trust Fund (includes non-bargaining unit employees)

• Providence Continuing Care Centre

• St. Joseph's Care Group – Lakehead Psychiatric Hospital

• Waypoint Centre for Mental Health Care

• Workplace Safety and Insurance Appeals Tribunal

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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Fw_ Your Scan job has arrived..rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: Your Scan job has arrived.
Date: Tuesday, September 20, 2016 09:36:00
Attachment 1: NuanceScanDoc_09_20_16_09_34.pdf

Hi Nadine,

Please see the scanned signed SOW for your records

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca
----- Forwarded by Lucy Durocher/CA/ABAS/PwC on 09/20/2016 09:35 AM -----

From: DoNotReply@pwc.com
To: ldurocher002@casmtp.pwcinternal.com
Date: 09/20/2016 09:34 AM
Subject: Your Scan job has arrived.

Your Scan to My Email task has completed successfully.

Your completed document is attached here.

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dommages subis par une personne autre que le destinataire par suite de décisions ou de mesures fondées sur le contenu de cette communication ou autrement. Si vous avez reçu ce courriel par erreur, veuillez communiquer avec son expéditeur et en détruire toutes les copies.

NuanceScanDoc_09_20_16_09_34.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective September 16, 2016.

PricewaterhouseCoopers LLP (the "Vendor" or "PwC") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client" or the "Province") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of March 22, 2016 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$100,000.00, excluding HST.

4. *Project Start Date:* September 16, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide accounting advice (the "accounting advisory services") regarding the acceptability of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards. The accounting advice may include:

   - Review of background information, position papers developed by the Client or third parties that have been engaged by the Client to draft accounting positions on accounting for the recognition and measurement of pension assets for jointly-sponsored pension plans, and other supporting information.
   - Provide written or oral comments on draft position papers as provided by the Client with respect to the application of Canadian Public Sector Accounting Standards.
   - Participation in discussions with internal and external stakeholders and other parties as directed by the Client.

   During the course of this project, the Client will provide to PwC a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements with the Client's auditor. If an accounting opinion is to be provided, the Client's auditor will confirm to us in writing that the information the Client

has provided to PwC is complete and consistent with their knowledge of the facts and circumstances of the specific transaction.

If requested to by the Client during the course of the project, the Vendor shall provide an accounting opinion (the "accounting opinion"), prepared in accordance with Section 7600, *Reports on the application of accounting principles* of the CPA Canada Handbook – Assurance ("Section 7600"), regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards.

Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting advice or accounting opinion (if applicable), including discussions with the Office of the Auditor General.

The Client agrees that any accounting advisory services are solely for the information and use of the Client. Subject to the obligations in Article 27 (Privacy) of the Master Agreement and as required by law by the Client's independent auditors, the Client agrees that any written work product of PwC will not be made available to any other persons or entities. An accounting opinion prepared in accordance with Section 7600 will, in compliance with Canadian GAAS, include restriction of use language identifying the parties to whom use is restricted and a statement that the report is not intended to be and should not be used by anyone other than the specified parties or for any other purposes. However the Client may provide access to PwC's observations and an accounting opinion prepared under Section 7600 (if applicable) to the Client's independent auditors solely for their informational purposes. Except as provided for in the preceding sentence, the Client agrees to seek and obtain the Vendor's written consent before including our accounting opinion (if applicable) or referring to the Vendor in any document disclosed to third parties, including disclosure of a summary of the accounting opinion or publication of the opinion in documentation that may be accessible to or intended for the public. The Vendor may, in their own discretion, waive the requirement to obtain written consent. The Client agrees that prior to or as part of providing their independent auditors with any written work product of PwC, including an accounting opinion prepared under Section 7600, the Client will notify its independent auditors that it is PwC's desire to be notified of, and to consent to, the disclosure of any PwC written work product or reference to any PWC work product in any materials to be disclosed to third parties. PwC agrees that the Client's obligation is only to notify its independent auditors of PwC's desire to be notified about, and to consent to, disclosure, and that the Client is not making any representation or warranty that its independent auditors will notify PwC or seek PwC's consent.

Acknowledgements and agreements

The Client acknowledges and agrees to the following:

a. The performance of the accounting advisory services does not constitute an engagement to provide audit, compilation, review or attest services in accordance with professional standards issued by the Chartered Professional Accountants of Canada ("CPA Canada") and, therefore, PwC will not express an opinion or any other form of assurance with respect to the accounting advisory services.
b. The accounting advisory services and accounting opinion (if applicable) to be provided do not include the delivery of any verbal or written advice on the application of accounting principles to a hypothetical transaction.
c. This engagement cannot be relied on to disclose internal control deficiencies, errors or fraud, should they exist.

d. PwC has no responsibility for updating the accounting advisory services or accounting opinion or for performing any additional services, except as agreed to in writing with the Client.
e. The Client's purpose for engaging PwC to perform the accounting advisory services is to supplement management's own technical accounting resources in performing accounting analysis and to assist management in making its determination as to the application of accounting principles and not to obtain an opinion from PwC as to such application, unless an accounting opinion is requested by the Client.
f. The Client shall be solely responsible for, among other things: (a) making all management decisions and performing all management functions; (b) designating one or more individuals who possess suitable skill, knowledge and/or experience, preferably within senior management to oversee the accounting advisory services (c) evaluating the adequacy and results of the accounting advisory services; (d) accepting responsibility for the results of the accounting advisory services; and (e) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities.
g. All management decisions and final conclusions reached in connection with the accounting advisory services will be the responsibility of the Client. PwC will not perform any management functions, make management decisions, or perform in a capacity equivalent to that of an employee of the Client.
h. PwC has no responsibility related to the Client's accounting or disclosure conclusions, whether or not such conclusions of the Client are related to the accounting advisory services and PwC has no responsibility for any disagreements between the Client and its independent auditor related to the Client's accounting.
i. The Client will be solely responsible for all decisions regarding the accounting treatment of any item or transaction and acknowledges that the accounting advisory services do not include the recording of any amounts in the Client's books or records. All amounts derived from the performance of the accounting advisory services will be reviewed and approved by, and will be the responsibility of, the Client's management.
j. The nature, scope and design of the accounting advisory services and the accounting opinion are solely the responsibility of the Client. PwC will rely, without independent verification, on the facts, information and assumptions provided by the Client. PwC will make no representation nor provide any assurance with respect to the adequacy of the services for the Client's purposes. Furthermore, PwC has no responsibility to advise the Client of other procedures that might be performed.
k. The Client will be solely responsible for providing accurate and complete information requested by PwC. PwC has no responsibility for the accuracy or completeness of the information provided by or on behalf of the client.
l. PwC's accounting and technical assistance will be based on the existing public sector generally accepted accounting principles. Should those generally accepted accounting principles be amended, superseded or revised in any manner, PwC's advice might change. PwC has no responsibility to inform the Client of any changes in generally accepted accounting principles that may occur after the completion of the engagement or any other oral or written work product prepared hereunder that would impact PwC's advice on the appropriate application of generally accepted accounting principles or to update its recommendations or any other oral or written work produce to take any such changes into account.
m. This engagement does not create a relationship between PwC and any person or party other than the Client. This engagement is not intended for the express of implied benefit of any third party.

n. The Client will identify an appropriate individual to serve as the project manager, including overseeing the accounting advisory services.

7. *Ownership and Licences* - **Attachment D** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be Lucy Durocher who is the engagement leader.

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Charges On Per Diem Rate Basis*– The Vendor and the Client agree that Work performed under this Statement of Work will be charged on a Per Diem Rate basis. The Per Diem Rate will vary, based on the nature of the final deliverable, as follows:

Nature of final deliverable	Per Diem Rate	Service Category	Estimated hours	Per Diem Rate
Accounting Advisory	General Consultant, Level 2	Service Category 2	20-25	$390/hour
Accounting Opinion	General Consultant, Level 2	Service Category 2	30-35	$990/hour

13. *Billing and Payment Process* – The Vendor shall invoice the Client in accordance with the requirements of the Master Agreement. Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	Individual's Role and Experience Level	Service Category	Per Diem Rate
Lucy Durocher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Martin Boucher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Sean Cable (or alternative as agreed to by the Client)	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"
Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client: Treasury Board Secretariat,
Office of the Provincial Controller Division
Branch: Accounting Policy and Financial Reporting

Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Clients designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all Confidential information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

18. *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**PricewaterhouseCoopers LLP, PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2**
Vendor Representative:	**Lucy Durocher**
Telephone number:	**416-869-2311**
E-mail:	**Lucy.durocher@ca.pwc.com**
Backup Vendor Representative:	**Martin Boucher**
Telephone number:	**514-205-5415**
E-mail:	**Martin.boucher@ca.pwc.com**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: N. Petsche

Name: Nadine Petsche

Title: Director, Accounting Policy & Financial Reporting

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature: PricewaterhouseCoopers LLP

Name: LUCY DURCHER

Title: PARTNER

I have the authority to bind the Vendor.

Fw_ tax declaration form.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fw: tax declaration form
Date: Monday, October 31, 2016 16:17:27
Attachment 1: NuanceScanDoc_10_31_16_15_11.pdf

Hi Shyrose,

Please find attached our signed tax declaration for PwC.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca
----- Forwarded by Lucy Durocher/CA/ABAS/PwC on 10/31/2016 04:16 PM -----

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NuanceScanDoc_10_31_16_15_11.pdf

Appendix D – Tax Compliance Declaration Form

The Ontario Government expects all suppliers to meet their Ontario tax obligations on a timely basis. In this regard, proponents are advised that their Ontario tax obligations, if any, must be in good standing in order to be considered for a contract award (see Section 3.2.3 of the RFP). In order to be considered for a contract award, the proponent must submit the following tax compliance status statement and the following consent to disclosure:

Declaration

I/WE hereby certify that **PricewaterhouseCoopers LLP** (the "Proponent") at the time of submitting its proposal, is in full compliance with all applicable Ontario tax statutes, whether administered by the Treasury Board Secretariat or by the Canada Revenue Agency, and that, in particular, all returns required to be filed have been filed and all taxes due and payable under those statutes have been paid or satisfactory arrangements for their payment have been made and maintained; or the Proponent will take all necessary steps prior to being considered for contract award in order to be in full compliance with all applicable Ontario tax statutes.

(Please check applicable box)

The Proponent ☐ is / ☒ is not a corporation subject to Ontario corporate tax under the *Taxation Act, 2007* (Ontario).

(Please insert Proponent's Business Number) NO ONTARIO # FEDERAL 870576089

Consent to Disclosure

The Proponent consents to the Ministry of Finance releasing the taxpayer information to the Ministry of Finance as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

The Proponent consents to the Treasury Board Secretariat releasing taxpayer information to the Requesting Ministry as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

Dated at TORONTO, ONTARIO this 31ST day of OCTOBER 20 16

(Authorized signing officer)

KRISTIAN KNIBUTAT COO/CFO

(Print Name) **(Title)**

I have authority to bind the Proponent.

Fwd_ Mario Chasse - Accord de confidentialitØ (signØ).rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Fwd: Mario Chasse - Accord de confidentialité (signé)
Date: Monday, October 17, 2016 17:03:26
Attachment 1: Mario Chassé - Confidentiality agreement.pdf

Hi Shyrose,

Please see attached the signed confidentiality agreement for Mario Chassé.
Regards,
Lucy

Sent from my iPhone

Begin forwarded message:

From: "Julia Nita" <julia.nita@ca.pwc.com>
Date: October 17, 2016 at 2:52:13 PM CDT
To: "Lucy Durocher" <lucy.durocher@ca.pwc.com>
Cc: "Mario Chasse" <mario.chasse@ca.pwc.com>
Subject: Mario Chasse - Accord de confidentialité (signé)

Bonjour Mme Durocher,

Je vous transmets ci-joint l'accord de confidentialité signé par Mario. Veuillez nous indiquer svp si vous avez besoin du document original.

Merci et bonne journée.

(See attached file: Mario Chassé - Confidentiality agreement.pdf)

Julia Nita
PwC | Partner Assistant, Actuarial Services
T: +1 416 941 8383 ext. 16274
Email: julia.nita@ca.pwc.com
PwC Management Services LP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Mario ChassØ - Confidentiality agreement.pdf

Confidentiality Agreement

During and following the term of the Agreement between **Pricewaterhouse Coopers LLP** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **President of Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and OPS Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the Freedom of Information and Protection of Privacy Act ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: MARIO CHASSÉ Signature: Mario Chassé

Date: OCTOBER 17, 2016

Witness: JULIA NITA Signature: Julia Nita

Date; OCTOBER 17, 2016

forgot to ask.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]
Subject: forgot to ask
Date: Thursday, October 20, 2016 17:52:23

Have you received a request to release a copy of the accounting opinion to the Expert Panel? If not, then would a request worded similarly to the request to release to PwC suffice?

If not, please advise as to appropriate wording to include.

Thanks.

Nadine

fyi.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Paul, Joshua (EDU) [Joshua.Paul@ontario.ca]; Killoch, Alex (MOF) [Alex.Killoch@ontario.ca]
Subject: fyi
Date: Monday, September 19, 2016 12:38:22

Lucy,

In relation to some of your Q's on the call.

Contribution rates between the employee and employers are always equal, with one exception of 2008, when the OTF made a portion of the employee contribution. See table:

https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1-d22e3e50dbc3/How+Contribution+Rates+Have+Evolved.pdf

Note: the 1.1% was phased in over 3 years

Year

Up to CPP limit

Above CPP limit

Increase*

2011

10.4%

12.0%

N/A

2012

10.8%

12.4%

0.4%

2013

11.15%

12.75%

0.35%

2014

11.5%

13.1%

0.35%

Total increase

1.1%

* As a percentage of salary

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Veinot, Cindy (TBS); robert.siddall@metrolinx.com; Freeman, Ian (MTO)
Cc:	Sharda, Vinay (MTO); Jain, Sejal (MTO); "Jennifer Gray"; "lucy.durocher@ca.pwc.com"; "abrar.a.chowdhury@ca.pwc.com"; "lucy.durocher@pwc.com"; "David Gould"; "carol.devenny@pwc.com"
Subject:	follow up metrolinx meeting
Start:	December 15, 2016 1:00:00 PM
End:	December 15, 2016 1:30:00 PM
Location:	teleconference 416 212 8013 passcode 4950903#

Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Nadine Petsche
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100093008
Please include this number with payment

Invoice Date:	19 June 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

For services rendered 01 April 2017 to 31 May 2017:

- Preparation of letters documenting the calculation of future economic benefit and accrued benefit asset recognition for OTPP and OPSEUPP
- Advice and discussions related to accounting for various benefit provisions
- Assistance with pension plan accounting and analysis of year-end balance sheet adjustments

	Net	Tax	Rate	Tax Amount	CAD Total
Fee	65,000.00	HST	13 %	8,450.00	73,450.00
	65,000.00			**8,450.00**	**73,450.00**
Invoice summary	**65,000.00**				
Tax : 13% HST				8,450.00	
Total:	**65,000.00**			**8,450.00**	**73,450.00**

A member of Ernst & Young Global

Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

Electronic payment instructions:
Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

Wire transfer instructions: Transit #2411 Account #24111000237. Reference the name and address of remitter, invoice number and engagement number.

Electronic fund transfer instructions: Bank ID: 0001 Transit# 24112 Account# 1000237. To ensure accurate allocation of funds sent electronically, please email your remittance detail to gss.canadaaccountsreceivable@xe02.ey.com including the amount paid, the invoice number and your company name.

Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Nadine Petsche
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100093008
Please include this number with payment

Invoice Date:	19 June 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

For services rendered 01 April 2017 to 31 May 2017:

- Preparation of letters documenting the calculation of future economic benefit and accrued benefit asset recognition for OTPP and OPSEUPP
- Advice and discussions related to accounting for various benefit provisions
- Assistance with pension plan accounting and analysis of year-end balance sheet adjustments

	Net	Tax	Rate	Tax Amount	CAD Total
Fee	65,000.00	HST	13 %	8,450.00	73,450.00
	65,000.00			**8,450.00**	**73,450.00**
Invoice summary	**65,000.00**				
Tax : 13% HST				8,450.00	
Total:	**65,000.00**			**8,450.00**	**73,450.00**

A member of Ernst & Young Global

Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

Electronic payment instructions:
Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

Wire transfer instructions: Transit #2411 Account #24111000237. Reference the name and address of remitter, invoice number and engagement number.

Electronic fund transfer instructions: Bank ID: 0001 Transit# 24112 Account# 1000237. To ensure accurate allocation of funds sent electronically, please email your remittance detail to gss.canadaaccountsreceivable@xe02.ey.com including the amount paid, the invoice number and your company name.

Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Mark Donaldson
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100109767
Please include this number with payment

Invoice Date:	19 October 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

Final billing for professional services rendered: 03 August 2017 to 30 September 2017

- Completion of the final reviewed versions of the projection models for OTPP, OPSEU, PSPP, HOOPP and CAATT pension plans
- Preparation and delivery of training material (Pension 101, PS 3250, Use of Models) to Ontario TBS employees on September 12, 14 and 15.
- Summary description document of the work performed by EY related to the projection models

		Net	Tax	Rate	Tax Amount	CAD Total
Fee		22,970.00	HST	13 %	2,986.10	25,956.10
		22,970.00			**2,986.10**	**25,956.10**
Invoice summary		**22,970.00**				
Tax :	13% HST				2,986.10	
Total:		**22,970.00**			**2,986.10**	**25,956.10**

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Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

Ernst & Young LLP
Toronto, ON

Electronic payment instructions:
Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

Wire transfer instructions: Transit #2411 Account #24111000237. Reference the name and address of remitter, invoice number and engagement number.

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2016-17 Public Accounts

Technical Briefing

September 7, 2017

CONFIDENTIAL DRAFT

Purpose of today's briefing

1. Provide an overview of the results for fiscal 2016-17
2. Highlight the changes made in the 2016-17 financial statements:
   a) Classification of third-party revenues for hospitals, colleges and school boards
   b) Accounting basis for Ontario Power Generation and Hydro One
   c) Accounting for the Independent Electricity System Operator (IESO) and market accounts
   d) Accounting for net pension assets of jointly sponsored pension plans

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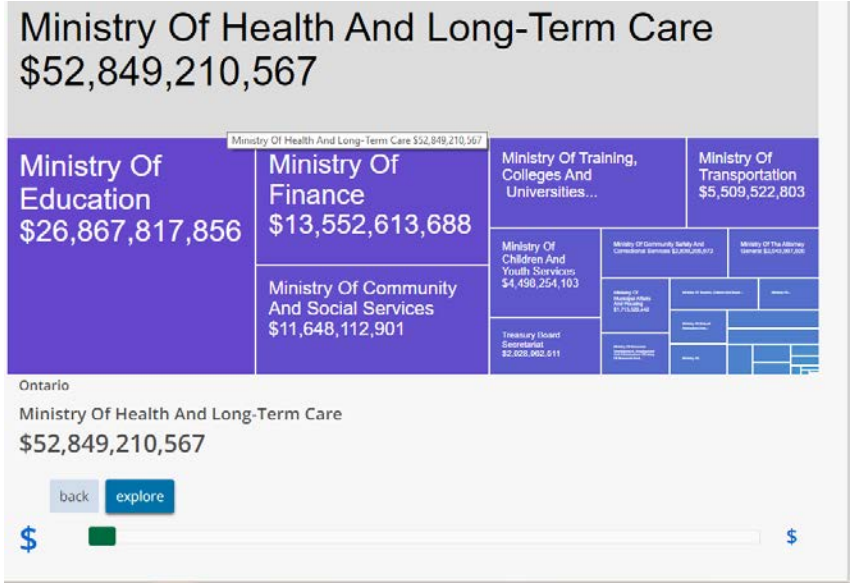
2016-17 Highlights

- New digital tools have been developed that present the Public Accounts data in innovative, visual formats.
- This year, Ontario has:
  - Released six new downloadable data sets
  - Created new data visualizations tools
  - Published the web page under the Open Ontario Licence



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Ontario

2016-17 Highlights

- Ontario has beaten its deficit target eight years in a row. The 2016-17 Public Accounts of Ontario show that Ontario's deficit is $1 billion - $3.3 billion lower than projected in the 2016 Ontario Budget.
- In the 2016-17 fiscal year (April to March):
  - revenue was $140.7 billion – $2.2 billion more than expected in the 2016 Budget
  - expenses were $141.7 billion – $0.01 billion less than planned in the 2016 Budget
  - Some of the top spending areas included

$56B Health

$26.6B Education

$12.9B Infrastructure

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Ontario

2016-17 Highlights

Other highlights include:

- Ontario's real gross domestic product (GDP) was 2.7%, up from 2.2% in the 2016 Budget. Over the last three years, Ontario's GDP growth has outpaced that of all G7 countries.
- Net debt-to-GDP continues to be forecasted lower than expected for 2016-17 at 37.8%, an improvement over the 2016 Budget of 39.6%.

Visit **Ontario.ca/publicaccounts** for more highlights and digital tools that help make Ontario's finances easier to understand, access and use.

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Summary 2016-17 Results

2016-17 Actual Results					
$ Billions	2016-17 Budget[1]	2016-17 Actual	2015-16 Actual [1 2]	Change from Budget	% Change
Revenues	138.5	**140.7**	136.1	2.2	1.6%
Expenses	141.8	**141.7**	139.7	(0.1)	-0.1%
Reserve	1.0	**-**	-	(1.0)	
Annual Deficit	(4.3)	**(1.0)**	(3.5)	3.3	-76.7%
Net Debt		**(301.6)**	(295.4)		
Accumulated Deficit		**(193.5)**	(192.0)		

[1] 2015-16 Actuals and 2016-17 Budget have been reclassified to reflect the change in presentation for third party revenues of hospitals, colleges and school boards (no change to deficit)

[2] 2015-16 Actual has been restated to reverse the impact of regulated accounting for pensions

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Preparation of the Financial Statements

- The consolidated financial statements are prepared by the Government of Ontario in accordance with the accounting principles for governments recommended by the Public Sector Accounting Board (PSAB).
- PSAB independently establishes accounting standards for the public sector in Canada.
- The objective of PSAB standards is to meet the needs of users of financial statements by providing the information needed for accountability and decision making.
- PSAB standards specify how transactions and other events are to be recognized, measured, presented and disclosed in a public sector entity's financial statements.
- PSAB recognizes that their standards cannot address every potential situation, and that it may be necessary to refer to other sources of guidance.
  - *No rule of general application can be phrased to suit all circumstances or combinations of circumstances that may arise. As a result, matters may arise that are not specifically addressed in the primary sources of GAAP. It is necessary to refer to other sources when the primary sources do not deal with the accounting and reporting in financial statements of transactions or events that a public sector reporting entity encounters, or when additional guidance is needed to apply a primary source to specific circumstances. (Section PS 1150.07 from the PSA Handbook)*

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Accounting Changes for 2016-17

- The Province adopted several new accounting changes for the 2016-17 Public Accounts to better reflect the financial position and activities of the government during the fiscal year
- These changes included:
  a) Classification of third-party revenues for hospitals, colleges and school boards
  b) Accounting basis for Ontario Power Generation and Hydro One
  c) Accounting for the Independent Electricity System Operator (IESO) and market accounts
  d) Accounting for net pension assets of jointly sponsored pension plans

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Classification of Third-Party Revenues for Hospitals, Colleges and School Boards

- 2016-17 Public Accounts present third-party revenues for hospitals, school boards and colleges with provincial revenue.
- In prior years, these revenues were netted against the expenses of the respective sectors (health, education, post-secondary).
- This is a change in presentation only.
- The changes increases total revenues and expenses by approximately $8 billion.
- There is no impact to the Province's deficit, net debt or accumulated deficit.
- This change is consistent with PSAB standards and the reporting practices of other senior Canadian governments.
- This change was recommended by the Office of the Auditor General in prior years.

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Accounting basis for Ontario Power Generation and Hydro One

- The 2016-17 Public Accounts include the financial results of Ontario Power Generation (OPG) and Hydro One using International Financial Reporting Standards (IFRS).
- These two government business enterprises currently report their stand-alone financial results using Generally Accepted Accounting Principles in the United States (US GAAP).
- In prior years, the reported results of OPG and Hydro One were included in the results of the Province based on US GAAP.
- This change does not have a material impact on this year's Public Accounts.
- This change was recommended by the Office of the Auditor General in prior years.

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Accounting for Independent Electricity System Operator and Market Accounts

- Independent Electricity System Operator (IESO) is a not-for-profit, non-taxable corporation established pursuant to Part II of the *Electricity Act, 1998*.
- IESO prepares its financial statements in accordance with PSAB standards.
- IESO's financial statements are audited by KPMG LLP, which issued an unqualified opinion on the December 31, 2016 financial statements.
- IESO is a party to agreements with market participants for which are there are amounts due *to* the entities that provide electricity to the market (e.g. power generators) and due *from* those who consume electricity (e.g. local distribution companies on behalf of their consumers).
- In 2016, IESO changed the accounting for the market accounts, recognizing the amounts to be settled as assets and liabilities, equal in amount. In prior years, these amounts were not reflected in the financial statements of IESO.
- IESO made the change to be better reflect its' administration of $17 billion in amounts due to and from the market participants.
- This change has no impact to the province's annual deficit, net debt or accumulated deficit.

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Accounting for Independent Electricity System Operator and Market Accounts

- The Ontario Power Authority (which was merged with the IESO on January 1, 2015) included market accounts in its financial statements, which were not subject to qualification from the Office of the Auditor General at that time
- Additional background on IESO:
  - On January 1, 2015, IESO was amalgamated with Ontario Power Authority (OPA) and continued as IESO.
  - Prior to the amalgamation, OPA prepared its financial statements in accordance with PSAB standards.
  - OPA's last financial statements prior to amalgamation were audited by KPMG LLP, which issued an unqualified opinion on the December 31, 2014 financial statements.
  - OPA's audited financial statements included a segment of the market accounts.
- The Province consolidates the financial statements of the IESO (and the OPA until it amalgamated with the IESO)

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IESO Market Accounts

- Based on professional staff's interpretation of PSAB standards, the government believes that reporting the IESO's market accounts in the consolidated financial statements of Province is more transparent accounting.
- The IESO is a party to agreements with each market participant, and each market participant either owes an amount to the IESO or is owed an amount from the IESO.
- For example:
  - Ontario Power Generation has a receivable from IESO recorded on its financial statements related to power generated, and historically, IESO did not have a payable recorded to Ontario Power Generation – now it does
  - Hydro One has a payable to IESO recorded on its financial statements related to power purchases, and historically, IESO did not have a receivable recorded from Hydro One – now it does
- The amounts due from market participants meet the definition of an asset and the amounts due to market participants meet the definition of a liability under PSAB standards.
- KPMG reviewed the accounting for eight other independent system operators in North America, and all but one recognize market accounts in the financial statements.
- IESO management, their Audit Committee, their Board of Directors, their external auditor and the Office of the Provincial Controller support the change in accounting.
- A qualified opinion was issued by the Office of the Auditor General on the 2016-17 consolidated financial statements regarding the change in Independent Electricity System Operator's accounting for the "market accounts".

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Accounting for Net Pension Assets of Jointly Sponsored Pension Plans

- Ontario Public Service Employee's Union Pension Plan (OPSEUPP) and Ontario Teachers' Pension Plan (OTPP) are jointly sponsored pension plans (JSPPs) where the Government of Ontario is a co-sponsor.
- The plans are funded on a 50/50 basis, co-managed by the sponsors, and decisions regarding benefits and contributions require negotiation and agreement between them.
  - On June 12, 2017, the co-sponsors of OTPP (Ontario Teachers Federation and the Government) announced a 1.1% reduction in contributions effective January 1, 2018
- Under PSAB standards, an asset arises when the government's total contributions to a plan, including interest earned thereon, are greater than the pension expense recognized since the start of the plan.
- Since 2001-02, the Province's share of pension assets reflected on the audited consolidated financial statements of the Province has been based on a policy considered to be consistent with PSAB standards related to accounting for retirement benefits. The standards have not changed since their issuance in 2001.
- In 2016, the government passed a time-limited regulation to require the full write-off of the net assets of both of these plans for the 2015-16 Public Accounts.

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Pension Accounting

- Based on professional staff's interpretation of PSAB standards, the government believes that pension assets for OPSEUPP and OTPP should be reported in order to fairly present the Province's financial position.
- The Province has shared control over the pension plan and the existing agreements in place between the sponsors support the recognition of the pension asset.
- The professional staff does not believe that the Government has the right to withdraw any surplus from the plan, and has supported the value of the pension asset solely on the basis of being able to reduce contributions in the future.
- The Province has recorded the pension assets for OTPP and OPSEUPP in its 2016-17 consolidated financial statements and has restated the 2015-16 consolidated financial statements to recognize the pension assets.
- With respect to the Healthcare of Ontario Pension Plan (HOOPP) and Colleges of Applied Arts and Technology Pension Plan (CAATPP), based on the difference in governance structure between these plans and OTPP and OPSEUPP, the Province has recorded a valuation allowance for CAATPP in the year (amount is not material). The HOOPP plan is not in a net asset position for accounting purposes at March 31, 2017.

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Pension Accounting

- The professional staff's interpretation of PSAB standards is supported by its own research and analysis as well as:
  - The report of the Pension Asset Expert Advisory Panel (https://www.ontario.ca/page/pension-asset-expert-advisory-panel-report) released on February 13, 2017 stating that the Government should record an asset for its share of the surplus reported in the accounting valuations for each plan and that no valuation allowance is required.
  - An opinion from Deloitte LLP on aspects of the Province's accounting as at March 31, 2016 for the OTPP, a summary of which is included in Appendix A. The opinion, which was dated October 2, 2016, concluded that it was permissible to recognize a pension asset under Canadian Public Sector Accounting Standards, even though the Province did not have under a unilateral right to reduce contributions.
  - Analysis completed by EY as to whether any valuation allowance is required to be recorded for OTPP or OPSEUPP as of March 31, 2017. EY confirmed no valuation allowance was required for either plan.
- A qualified opinion was issued by the Office of the Auditor General on the 2016-17 consolidated financial statements regarding the Province's accounting for the net pension assets of OTPP and OPSEUPP.

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Appendix A – Deloitte Summary of Accounting Opinion Issued on Pension Accounting

Deloitte was engaged to provide a report ("Deloitte Report") on the application of accounting standards by the Ontario Treasury Board Secretariat. Our report, which was issued on October 2, 2016, was prepared under professional standards for such reports set out by CPA Canada.

The subject of this report was the application of Public Sector Accounting Standards (PSAS), as established by CPA Canada, in the recognition of a pension asset in the Province of Ontario's financial statements. Pension accounting is subject to professional judgement and interpretation, and involves significant accounting estimates. The Deloitte Report focused on a specific aspect of this complex area as it relates to the Province of Ontario's accounting for the Ontario Teachers' Pension Plan (OTPP).

OTPP is a pension plan that is jointly sponsored by the Ontario government (or the Province) and the Ontario Teachers' Federation (OTF). Based on the Province's application of PSAS, OTPP is in a plan surplus position. We accepted this aspect of the Province's application of PSAS as a matter of fact in developing our report.

The Deloitte Report addressed the question of whether it was possible to record a pension asset related to the plan surplus in the Province's financial statements, given that the plan is jointly sponsored. We concluded that, based on the information provided to us by the Province and our professional judgement, that it was permissible under PSAS to record a pension plan asset, even though the Province's ability to benefit from any plan surplus, through future contribution reductions for example, would need to be negotiated with and agreed between the Province and OTF.

It is to be noted that even if a pension asset is recorded, PSAS would also require that consideration should be given to limiting the recorded amount of this pension asset to an amount that would be less than the calculated amount of the pension surplus. The Deloitte Report did not express a view on whether any limit to the recorded amount of the asset is needed in the case of the Province's accounting for the pension asset related to OTPP. Therefore, our report did not express a view on the amount of the pension asset that should be recorded in the Province's financial statements as at March 31, 2016 or at any other date.

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Appendix B: Panel Members

- Patricia O'Malley (Chair) – former Chair of Canadian Accounting Standards Board, former member of International Accounting Standards Board, Chair of the Canadian Actuarial Standards Oversight Council, former technical partner KPMG
- Murray Gold – Leading practitioner and senior pension and benefits partner at Koskie Minsky LLP
- Uros Karadzic – Pension actuary, member of the PSAB's Employment Benefit Taskforce, partner at EY
- Paul Martin – Comptroller with the Government of New Brunswick, member of the PSAB's Employment Benefit Taskforce and previously a partner with the national accounting firm of Grant Thornton LLP

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From:	Provis, Ian (TBS)
To:	Jim Keates (jimkeates@hotmail.com); Virani, Shyrose (TBS); Lugo, Grace (MECP); Hurdman, Jeff (MECP); Pearson, Heather (MECP); Sharp, Tim (MECP); Wang, Holly (MECP); Djakonovic, Marina (MECP); Chau, Gladys (MECP); Hewitt, Myra (MECP); Chen, Doris (MECP); Lau, Lucia (MECP); Graham, Helen (TBS); Veinot, Cindy (TBS)
Cc:	Keates, James (TBS); Petsche, Nadine (TBS)
Subject:	FW: Review draft Cap and Trade Accounting Documents
Start:	October 25, 2016 11:30:00 AM
End:	October 25, 2016 1:30:00 PM
Location:	7 Queens Park APFR boardroom 2nd floor - teleconference 416-212-8014 passcode 1474532#
Attachments:	Cap and Trade accounting implications - memorandum to file v3 October 13....docx

---

Jim,

Please plan to attend this meeting tomorrow. N

-----Original Appointment-----
From: Provis, Ian (TBS)
Sent: October 14, 2016 6:11 PM
To: Provis, Ian (TBS); Lugo, Grace (MOECC); Hurdman, Jeff (MOECC); Pearson, Heather (MOECC); Sharp, Tim (MOECC); Wang, Holly (MOECC); Djakonovic, Marina (MOECC); Chau, Gladys (MOECC); Hewitt, Myra (MOECC); Chen, Doris (MOECC); Lau, Lucia (MOECC); Virani, Shyrose (TBS); Graham, Helen (TBS); Veinot, Cindy (TBS)
Cc: Keates, James (TBS); Petsche, Nadine (TBS)
Subject: Review draft Cap and Trade Accounting Documents
When: October 25, 2016 11:30 AM-1:30 PM (UTC-05:00) Eastern Time (US & Canada).
Where: 7 Queens Park APFR boardroom 2nd floor - teleconference 416-212-8014 passcode 1474532#

Heather I am missing some of your team – could you forward to anyone you think is appropriate to this meeting.

The names were taken from the last invite. Please let us know if you are attending in person – we will order in some lunch and I will pre-register you with the OPP

Here is a draft document from PwC for review at the meeting. We are looking to engage OAG staff in late November and these are the section to finalize to ensure we have a good plan for PRRT revenue recognition

There are still some outstanding questions regarding how the cap and trade system works. If possible, if MOECC could provide answers to questions in the document in advance of the meeting that would be ideal.

Let me know if you have any questions

Thanks

Ian

Heads up.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Heads up
Date: Friday, September 23, 2016 12:59:01

Hi Lucy. In briefings now and firming up timing on key actions to try to get to signoff on the Public Accts for early nest week, if possible.
Cindy and I will be working on a position paper and will need your help, likely over the weekend as there will likely be a desire to review it on Sat pm or Sunday so it can be shared with the AG on late Sun/Monday. Hoping that's OK with you? N

IMPT - please send pension docs Thursday.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]; Colavecchia, Pina (CA - Toronto) (pcolavecchia@deloitte.ca) [pcolavecchia@deloitte.ca]
Subject: IMPT - please send pension docs Thursday
Date: Wednesday, November 30, 2016 23:41:06

Matt/Pina,

Sorry to bug you but we need the revised OPSEUPP and HOOPP docs tomorrow (Thursday) at the latest.

We were also hoping to receive the CAATPP draft document for review.

Thanks. Nadine

Internal Doc for your review_consideration.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Internal Doc for your review/consideration
Date: Monday, September 19, 2016 10:38:29
Attachment 1: Govt Partnerships and JDPP to DT.docx

Hi Lucy.

One of our staff have prepared the following analysis of PSAB's guidance on the government partnership standard and sec. 3250's reference to joint defined benefit plans.

I think you'll find it of interest.

Nadine

Govt Partnerships and JDPP to DT.pdf

Comparison of the definition of a government partnership and a joint defined benefit plan

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, paragraph PS 3060.06. GOVERNMENT PARTNERSHIP, Section PS 3060 was introduced into the PSA Handbook in October 1999.

The definition of a joint defined pension plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. RETIREMENT BENEFITS, Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined pension plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership while the definition of a JDBP focuses on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and	Consistent in concept with the wording in the GP definition being more general.

	partnership on an ongoing basis; and	to the level of benefits and contributions on an ongoing basis; and	
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

In addition to the wording being consistent, the concepts in the definitions of a government partnership and of a joint defined pension plan are similar.

While similar in concept and wording, the definition of a joint defined pension plan is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a

general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including joint defined pension plans.

As Section PS 3250 was introduced into the PSA Handbook after Section PS 3060, the PSAB would have had a few options on approval of Section PS 3250. The PSAB would have been aware of the interaction between the two standards as demonstrated by the similarity in the GP and JDBP definitions. PSAB could have as a consequential amendment:

a. Scoped out JDBP from Section PS 3060 if the requirements in Section PS 3250 were more specific or alternatively in conflict with those in Section PS 3060; or
b. Explicitly list JDBP in Section PS 3060 as a type of government partnership.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method in Section PS 3060.

Listing specific types of government partnerships in Section PS 3060 would not be typical as users of the PSA Handbook would question why certain types of GP have been mentioned while others were not. The standard is meant to be more principle based.

Based on the actions of PSAB, it would suggest the Board felt both the general and specific standards in both Section PS 3060 and PS 3250 respectively were applicable for a JDBP.

Invoice - pension panel. .rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Invoice - pension panel.
Date: Thursday, April 06, 2017 20:39:43

Hi Shyrose,

The invoice was in my inbox for approval. I approved it today and you should receive it shortly.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Invoice.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Gregory Winston [gregory.winston@ca.ey.com]
Subject: Invoice
Date: Friday, June 22, 2018 16:07:17
Attachment 1: image002.jpg

Hi Shyrose,

Hope all is well.

I would like to advise you that we are preparing the invoice for EY services from 1 March 2018 to 15 June 2018. We will provide you with a copy early next week.

Thanks,

Christina

Christina Chan, FSA | People Advisory Services | Manager

Ernst & Young LLP
EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
Christina.Chan@ca.ey.com
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image002.pdf

Invoice.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Donaldson, Mark (TBS) [Mark.Donaldson@ontario.ca]
CC: Christina Chan [Christina.Chan@ca.ey.com]; Gregory Winston [gregory.winston@ca.ey.com]
Subject: Invoice
Date: Thursday, October 19, 2017 14:05:28
Attachment 1: image001.gif
Attachment 2: Invoice-C100109767.pdf

Hi Cindy and Mark,

We have issued our final invoice today, and I am attaching a soft copy of it here for your convenience. This invoice covers the period to the conclusion of our contact, at 30 September 2017. You will note that the sum of all of our invoices (approx. $268k) has come in under the overall budget for the contract (approx. $299k).

Cindy, as you and I discussed last month, I believe there is a need and an opportunity to further improve pension reporting by the province. In particular, we discussed the work around assumption setting processes and documentation. This is the most important and strategic piece, but I think there is also further work that needs to be done on variance reconciliation and reporting, improvements how actuarial information is obtained and used, and further work related to OPEB plans.

Most of this work is continuation of the work we've been doing so far, and we would be available to continue supporting you in this regard. I recall that you were going to set up a meeting with Nancy Kennedy – please let me know if that still makes sense.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

EY Tower, 100 Adelaide Street West, PO Box 1, Toronto, ON M5H 0B3, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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image001.pdf

Invoice-C100109767.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100109767.pdf (244653 Bytes).

Invoices for EY pension services .rtf

From: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Christina Chan [Christina.Chan@ca.ey.com]; Uros Karadzic [uros.karadzic@ca.ey.com]
Subject: Invoices for EY pension services
Date: Thursday, August 03, 2017 10:17:10
Attachment 1: image001.png
Attachment 2: Invoice-C100100766.pdf
Attachment 3: Invoice-C100100765.pdf
Attachment 4: Invoice-C100100764.pdf

Hi Nadine/Shyrose,

Please find attached invoices for our pension services from 1 June 2017 – 2 August 2017.

Please let us know if you have any questions.

Regards,

Shayan

Shayan Jafrani, FSA, FCIA | Senior Manager | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 2975 | Cell Phone: +1 647 885 9630
EY/Comm: 1675237 | Shayan.Jafrani@ca.ey.com
Thank you for considering the environmental impact of printing e-mails.

From: Shayan Jafrani
Sent: Wednesday, March 22, 2017 3:45 PM
To: Virani, Shyrose (TBS) <Shyrose.Virani@ontario.ca>
Cc: Petsche, Nadine (TBS) <Nadine.Petsche@ontario.ca>; Christina Chan <Christina.Chan@ca.ey.com>
Subject: Invoices for EY pension services in February and March.

Hi Shyrose,

As requested, attached are the invoices for EY services in the amounts of $37,500 for services in February 2017 and $37,500 for services in March 2017.

Are these pdf attachments satisfactory or do you require hard copies?

Let us know if you have any questions.

Regards,

Shayan

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fiscalité préliminaires, lesquels pourraient ne pas permettre d'éviter des pénalités aux États-Unis.

image001.pdf

EY

Invoice-C100100766.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100100766.pdf (242657 Bytes).

Invoice-C100100765.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100100765.pdf (243014 Bytes).

Invoice-C100100764.stub.pdf

Security settings or invalid file format do not permit using Invoice-C100100764.pdf (242996 Bytes).

Letter and Agreement - Uros Karadzic.rtf

From: Sarah Anderton [Sarah.Anderton@ca.ey.com]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Uros Karadzic [uros.karadzic@ca.ey.com]
Subject: Letter and Agreement - Uros Karadzic
Date: Tuesday, December 05, 2017 16:33:15
Attachment 1: Confidentiality Agreement - Signed by Uros Karadzic.pdf
Attachment 2: SOW - Signed by Uros Karadzic.pdf
Attachment 3: Tax Declaration Form - Signed by Alan Smith.pdf

---

Hi Shyrose,

Please see the signed documents attached.

1. Confidentiality Agreement
2. Signed SOW
3. Tax Declaration Form

Thank you,
Sarah

--
Sarah Anderton | Executive Assistant | Enterprise Support Services

Ernst and Young LLP
Office: 416-943-3143 | sarah.anderton@ca.ey.com

-----Original Message-----
From: Virani, Shyrose (TBS) [mailto:Shyrose.Virani@ontario.ca]
Sent: Friday, December 1, 2017 1:53 PM
To: Anna Pesme <anna.pesme@ca.ey.com>
Cc: Uros Karadzic <uros.karadzic@ca.ey.com>
Subject: letter and agreement

Hi Anna:

Attached, please find:

1. Covering letter
2. Agreements (2 copies)
3. Tax Declaration Form
4. Confidentiality Agreement

Kindly have Uros sign the agreement and e-mail it back to me at your earliest. Original agreements are in the mail, once you receive it, please have Uros sign the original and send it to me via mail. Also, please have Uros sign the Tax Declaration form and Confidentiality Agreement, Christina has to sign Confidentiality Agreement as well.

Thanks
Shyrose Virani

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Confidentiality Agreement - Signed by Uros Karadzic.pdf

CONFIDENTIALITY AGREEMENT

Confidentiality Agreement

During and following the term of the Agreement between **Ernst & Young LLP** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and Listed Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the *Freedom of Information and Protection of Privacy Act* ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: UROS KARADZIC

Signature:

Date: Dec 4, 2017

Witness: Sarah Anderton

Signature:

Date: Dec 4, 2017

SOW - Signed by Uros Karadzic.pdf

Treasury Board Secretariat

Office of the Treasury Board
Office of the Provincial Controller Division
Accounting Policy & Financial Reporting Branch
Frost Building South, 2nd Floor
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel. (416) 325-8027

Secrétariat du Conseil du Trésor

Bureau du Conseil du Trésor
Bureau du contrôleur provincial
Direction de la méthode comptable et des rapports financiers
Édifice Frost Sud, 2e étage
7 Queen's Park Cr.
Toronto ON M7A 1Y7
Téléphone: 416-325-8027

Ontario

December 1, 2017

Ms. Anna Pesme
Ernst & Young LLP
222 Bay Street
Toronto ON
M5K 1J7

Ms. Pesme

RE: RFS-TBS-OTB-OPCD-22

The Ministry is pleased to advise that you are the selected proponent pursuant to the above-noted procurement process.

Enclosed please find two (2) copies of the Agreement for your signature. Please return one copy of the executed Agreement within five (5) business days of receipt of this notice:

Please be advised that this notice of selection letter should not be construed as permission from the Ministry to begin the work detailed in the Agreement. The Ministry will not be responsible or liable for any expenses related to the Deliverables, and the selected proponent is not to accept work requests prior to the execution of the Agreement by the Ministry. Work may begin pursuant to the Agreement when:

(a) the Agreement signed by both parties is returned to the selected proponent, and

(b) written permission is expressly given to the Supplier by the Ministry Representative to begin work under the Agreement.

.../2

If you have any questions concerning this process, please feel free to contact me at 416-325-8027.

Sincerely,

Mark Donaldson
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller Division

FORM OF STATEMENT OF WORK – OPS ENTITY

Statement of Work for Management Consulting Services

This statement of Work No. **RFS-TBS-OTB-OPCD-22** made in **duplicate and effective December 11, 2017 ending on June 15, 2019.**

Ernst & Young LLP (the "vendor" or "EY") and her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of June 16, 2014 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* – The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term of provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* – The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price* - C$75,000.00 does not include HST.

4. *Project Start Date* – December 11, 2017

5. *Project End Date* – June 15, 2019

6. *Scope of Services and Deliverables* – The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

    - Working with management of the Office of the Provincial Controller's Accounting Policy and Financial Reporting Branch (APFRB), the provider will provide actuarial/accounting services related to the following possible areas:
        - Review the economic assumptions (i.e. management best estimates) used for the accounting valuations of the pension plans and non-pension benefits reported by the Province.
        - Review the actual and forecast numbers prepared by APFR staffs for the Province's various pension and non-pension benefits, including assessing the reasonableness

and completeness of assumptions used by APFRB staff in the models, including any sensitivity analysis as required.
    - From time to time provide recommendations, if any on improvements in the pension and non-pension benefits accounting models.
    - Perform ceiling test requirements in accordance with PS3250.50 to PS3250.59 for all sole sponsor or joint sponsor pension plans that are in an accrued benefit asset position.
    - Provide advice on any accounting issues related to pension and non-pension benefits, as required.
    - Participate in discussions with internal and external stakeholders, as required.

- The Vendor will participate in meetings as necessary to support the engagement objectives.

7. *Ownership and Licenses* – Attachment D of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* – The structure of Ernst & Young's working relationship with OPCD is vital to the success of their engagement. The Project Lead that will handle OPCD work is Uros Karadzic. Ernst & Yong's communication strategy will be centered on periodic project update meetings, the frequency of which will be determined by the OPCD and Ernst & Young.

9. *Work Location* – All meetings will be within Greater Toronto.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:30 a.m. to 4:30 p.m. Monday to Friday inclusive.

    If required by the Client, the Vendor must provide Services outside of the normal working hours and/or non-Business days. The Vendor will not be entitled to charge more than the Fixed Price or Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Billing and Payment Process* – The Vendor shall provide the Client with quarterly billing statements that outline the per diem charges no later than 10 Business Days after the end of each quarter.

    Billing statements should include all billing information as set out in the Master Agreement.

13. Names of Roles of Vendor's Personnel:

Name of Individual	**Level**
Uros Karadzic	Senior Consultant/Project Lead
Christina Chan	Intermediate Consultant/Project Analyst

14. *Invoices* – Invoices for payment of any charges under this Statement of Work shall be sent to:

    Client: Treasury Board Secretariat
    Office of the Provincial Controller
    Accounting Policy and Financial Reporting Branch
    Mark Donaldson
    Director, Accounting and Policy Reporting
    Tel: 416 325 8027
    E mail: mark.donaldson@ontario.ca

15. *Knowledge Transfer* – The Vendor will work closely with the Client to ensure knowledge transfer to the Client's designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* – The Vendor shall destroy all information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Indemnity* – the indemnity set out in the Master Agreement applies to this assignment.

18. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	Treasury Board Secretariat
Client Representative:	Mark Donaldson
Telephone Number:	416 325 8027
E-mail:	mark.donaldson@ontario.ca

19. *Vendor Representative and Receipt of Notices*

    Uros Karadzic, Partner
    Ernst & Young LLP
    Ernst & Young Tower
    P O Box 251
    222 Bay Street
    Toronto ON M5K 1J7

    IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

Her Majesty the Queen in right of Ontario as
represented by the President of the Treasury Board

Per:

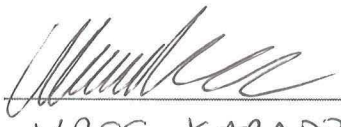
Signature:

Name: Mark Donaldson

Title: Director, Accounting Policy and
Financial Reporting

Pursuant to delegated authority

Per:

Signature: 

Name: UROS KARADZIC

Title: PARTNER

I have the authority to bind the Vendor

Tax Declaration Form - Signed by Alan Smith.pdf

Appendix D – Tax Compliance Declaration Form

The Ontario Government expects all suppliers to meet their Ontario tax obligations on a timely basis. In this regard, proponents are advised that their Ontario tax obligations, if any, must be in good standing in order to be considered for a contract award (see Section 3.2.3 of the RFP). In order to be considered for a contract award, the proponent must submit the following tax compliance status statement and the following consent to disclosure:

Declaration

I/WE hereby certify that **Ernst & Young LLP** (the "Proponent") at the time of submitting its proposal, is in full compliance with all applicable Ontario tax statutes, whether administered by the Treasury Board Secretariat or by the Canada Revenue Agency, and that, in particular, all returns required to be filed have been filed and all taxes due and payable under those statutes have been paid or satisfactory arrangements for their payment have been made and maintained; or the Proponent will take all necessary steps prior to being considered for contract award in order to be in full compliance with all applicable Ontario tax statutes.

(Please check applicable box)

The Proponent ☐ is / ☐ is not a corporation subject to Ontario corporate tax under the *Taxation Act, 2007* (Ontario).

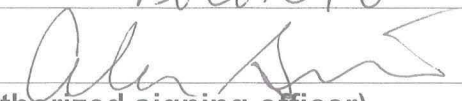
(Please insert Proponent's Business Number) _____

Consent to Disclosure

The Proponent consents to the Ministry of Finance releasing the taxpayer information to the Ministry of Finance as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

The Proponent consents to the Ministry of Finance releasing taxpayer information to the Requesting Ministry as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

Dated at Toronto this 5th day of December 20 17.



(Authorized signing officer)

ALAN SMITH CFO

(Print Name) **(Title)**

I have authority to bind the Proponent.

Master agreement attached.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Master agreement attached
Date: Friday, September 23, 2016 13:20:46
Attachment 1: Scanned from a Xerox multifunction device.pdf

Scanned from a Xerox multifunction device.pdf

MASTER AGREEMENT
FOR MANAGEMENT CONSULTING SERVICES
June 16, 2014

HER MAJESTY THE QUEEN in right of Ontario

as represented by the Minister of Government Services

AND:

«Proponent_Name»

(referred to as the "Vendor")

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THIS MASTER AGREEMENT FOR MANAGEMENT CONSULTING SERVICES is made in duplicate as of June 16, 2014.

BETWEEN:

HER MAJESTY THE QUEEN in right of Ontario
as represented by the Minister of Government Services

AND:

«Proponent_Name»

(referred to as the "Vendor")

In consideration of their respective agreements set out below, the parties agree as follows:

ARTICLE 1. DEFINITIONS

1.1 Definitions

In this Master Agreement and in each Statement of Work, these words and expressions have these meanings:

"**Attachment**" means an attachment to this Master Agreement listed in Section 2.14 (Attachments).

"**Authority**" means any government authority, agency, body or department, whether federal, provincial or municipal, having or claiming jurisdiction over this Master Agreement or the Statement of Work; and "Authorities" means all such authorities, agencies, bodies and departments.

"**Business Day**" means any working day, Monday to Friday inclusive, excluding statutory and other Ontario provincial government holidays, namely: New Year's Day; Family Day; Good Friday; Easter Monday; Victoria Day; Canada Day; Civic Holiday; Labour Day; Thanksgiving Day; Remembrance Day; Christmas Day; Boxing Day and any day which the government of the Province of Ontario has elected to be closed for business.

"**Change Order**" means, in respect of a Statement of Work, a written amendment executed by the Parties, which specifies the changes agreed, as further described in Section 11.2 (Change Orders).

"**Client**" means, in respect of a request for services or a Statement of Work:

(a) Ontario, as represented by a ministry of Ontario over which a minister of the Crown, as appointed by the Lieutenant Governor under the Executive Council Act, R.S.O. 1990, c. E.25, presides, or any combination of such ministries, if that ministry or combination of ministries has or have entered into the request for service or Statement of Work on behalf of Ontario; and

(b) the OPS Entity, if that OPS Entity has entered into the request for service or Statement of Work.

"**Client Representative**" means, in respect of a Statement of Work, one of the individuals designated as the Client Representative or the Backup Client Representative in the Statement of Work or, if not designated in it, any other individual designated as such pursuant to Section 2.9.

"**Client Work Information**" means (a) all audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, Technical Information, techniques, templates, and working papers, recorded in any form and on any media, and all other assets, materials, recorded information, and products of any kind, in all forms and however recorded; that are created, developed, generated, prepared or produced by the Client or by one or more of the Personnel of the Client; and (b) any contribution made by one or more of the Personnel of the Client to any Joint Work Material.

"**Client Work Invention**" means: (a) any Invention conceived, or conceived and developed, solely or jointly by one or more of the Personnel of the Client; and (b) any contribution made by one or more of the Personnel of the Client to any Joint Work Invention.

"**Confidential Vendor Information**" means:

(a) in connection with this Master Agreement, all information of the Vendor and its Subcontractors that is confidential by its nature or in the circumstances in which it is received and is identified as confidential or as a trade secret and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge or possession of Ontario in connection with this Master Agreement but, for certainty, excluding all information of the Vendor and its Subcontractors which comes into the knowledge, possession or control of Ontario in connection with any request for services issued pursuant to this Master Agreement or in connection with any Statement of Work;

(b) in connection with any request for services issued pursuant to this Master Agreement, all information of the Vendor and its Subcontractors that is confidential by its nature or in the circumstances in which it is received and is identified as confidential or as a trade secret and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Issuer or any contractor or subcontractor at any tier of the Issuer in connection with the request for services; or

(c) in connection with any Statement of Work, all information of the Vendor and its Personnel that is confidential by its nature or in the circumstances in which it is received and is identified as confidential or as a trade secret and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Client or its Personnel in connection with the Statement of Work;

including: (a) information relating to designs, drawings, flowcharts, Intellectual Property Rights, Inventions, patterns, plans, procedures, processes, reports, schematics, specifications, templates, and working papers; and (b) electronic data, other than Ontario Data, stored or processed by the Vendor; but Confidential Vendor Information shall not include: (c) Confidential Work Information; (d) information that ceases to benefit from protection as confidential information or as a trade secret under legislation or at law as a result of Ontario's or the OPS Entity's use or disclosure of Deliverables for any purpose whatsoever that is not expressly excluded by the Statement of Work; (e) information that is or becomes generally available to the public without fault or breach by Ontario or the OPS Entity, but only after that information becomes generally available to the public; (f) information that Ontario or the OPS Entity can demonstrate to have been rightfully obtained by it, without any obligation of confidence of any kind, from a third party who had the right to transfer or disclose it to Ontario or the OPS Entity free of any obligation of confidence; (g) information that Ontario or the OPS Entity can demonstrate to have been rightfully known to it or in its possession, free of any obligation of confidence, when disclosed; (h) information that is independently developed by Ontario or the OPS Entity without the use of any Confidential Vendor Information; (i) Vendor Evaluation Information; or (j) the Statement of Work document and its contents.

"**Conflict of Interest**" includes, but is not limited to, any situation or circumstance where: (a) in relation to the RFP process, the proponent has an unfair advantage or engages in conduct, directly or indirectly, that may give it an unfair advantage, including (i) having, or having access to, information in the preparation of its Proposal that is confidential to Ontario or OPS Entities and not available to other proponents; (ii) communicating with any person with a view to influencing preferred treatment in the RFP process, including the giving of a benefit of any kind, by or on behalf of the proponent to anyone employed by, or otherwise connected with, Ontario or OPS Entities; or (iii) engaging in conduct that compromises, or could be seen to compromise, the integrity of the open and competitive RFP process and render that process non-competitive and unfair; or (b) in relation to the performance of its contractual obligations in a contract with Ontario or the OPS Entity, the Vendor's and its Personnel's other commitments, relationships or financial interests (i) could, or could be seen to, exercise an improper influence over the objective, unbiased and impartial exercise of its independent judgement; or (ii) could or could be seen to compromise, impair or be incompatible with the effective performance of its contractual obligations.

"**Deliverables**" means anything and everything, in all forms and however recorded, that has been or will be created, developed, generated, prepared or produced in the performance of Services, or delivered or provided at any time during the Project Term or following the termination of the Statement of Work, by the Vendor (or its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors or others for whom it is responsible at law) as a result of the Statement of Work, as may be more fully described in the Statement of Work (including: (a) all assets, audio and video recordings, databases, designs, documents, drawings, images, know-how, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, Technical Information, templates, and working papers, of any kind; (b) data and information (whether or not contained in or on any database or electronic information storage system or media); (c) data collected as part of the Services; (d) all contributions made by one or more of the Personnel of the Vendor to any Joint Work Material; (e) all Vendor Materials; and (f) all Confidential Work Information). "Deliverables" include all developments and modifications to the foregoing developed or produced by the Vendor (or its Personnel, Subcontractors or others for whom it is responsible at law) from time to time under the Statement of Work, and copies of the above.

"**Effective Date**" means, as to this Master Agreement, the date first specified above.

"**Encumbrance**" means any encumbrance of any kind whatsoever, and includes an assignment, charge, hypotec, hypothecation, lien, mortgage, pledge, security interest, trust or deemed trust (whether contractual, statutory or otherwise arising), or other right or claim of others.

"**Executive Council**" means the council of that name comprising persons appointed by the Lieutenant Governor pursuant to the Executive Council Act R.S.O. 1990, c. E.25, as amended or replaced from time to time.

"**FIPPA**" means the Freedom of Information and Protection of Privacy Act, R.S.O. 1990, c. F.31, as amended or replaced from time to time.

"**Fiscal Year**" means the period running from April 1 in one calendar year to and including March 31 in the next calendar year.

"**Fixed Price**" means, in respect of particular Services performed and/or particular Deliverables provided and subject to Article 13 (Limits on Charges under Statements of Work) of the Master Agreement, the amount set out in the Statement of Work which the Vendor may charge for particular Services performed and/or particular Deliverables provided, which amount is fixed and not subject to change unless otherwise agreed to in a Change Order. For certainty, the "Fixed Price", as it relates to the particular Services performed and/or Deliverables provided, includes all labour and material costs, insurance costs, carriage and transportation costs, and other overhead, including any fees or other charges required by law; but excludes: (i) all applicable duties and taxes (including Harmonized Sales Tax (HST); (ii) all travel and accommodation expenses; and (iii) amounts that are charged on a Per Diem Rate basis.

"**Indemnified Parties**" means each of the following and their directors, officers, advisors, agents, appointees and employees: (i) Ontario; (ii) the members of the Executive Council; (iii) officers of the Legislative Assembly and officers of the Ontario Legislature, and their respective offices; and (iv) the OPS Entities.

"**Insolvency Event**" means, in respect of any Person: the making of an assignment by such Person for the benefit of its creditors; the failure of such Person to pay its debts generally as they become due; the filing or commencement of a petition or other proceeding in respect of such Person under any bankruptcy, reorganization, moratorium, arrangement of debt or insolvency law; the appointment of a receiver, receiver and manager, or interim receiver in respect of such Person or any material part of its assets or business; the declaration of bankruptcy or insolvency of such Person; the acknowledgement (in writing or otherwise) by such Person of its insolvency or inability to pay its debts generally as they become due; the suspension of business by such Person; the making by such Person of any proposal, arrangement or compromise with its creditors under the Bankruptcy and Insolvency Act (Canada), any other statute, or otherwise; or the taking of any action for the purposes of any of the foregoing.

"**Intellectual Property Rights**" means any intellectual or industrial property rights protected or protectable under the laws of Canada, any foreign country, or any political subdivision of any country, including any intellectual

property rights protected by legislation (such as legislation governing copyrights, industrial designs, integrated circuit topographies, patents or trademarks) or by common law (such as confidential information and trade secrets); and at any time in the future, with respect to any licence to exercise Intellectual Property Rights, includes any intellectual or industrial property rights protected or protectable at such time under the laws of Canada, any foreign country, or any political subdivision of any country.

"**Invention**" means any new and useful art, process, machine, manufacture or composition of matter, or any new and useful improvement to any of them, whether or not patentable.

"**Issuer**" means, in respect of a request for services referred to in: (a) the definition of "Confidential Vendor Information" in Article 1 (Definitions); (b) subsection 28.1(b) (Confidentiality - Request for Services); or (c) subsection 28.2(b) (Restrictions on Copying – Request for Services Process); the Client that issues the request for services.

"**Joint Work Invention**" means any Invention conceived, or conceived and developed, by one or more of the Personnel of the Vendor in the performance of Services with one or more of the Personnel of the Client.

"**Joint Work Material**" means anything and everything in all forms and however recorded that is created, developed, generated, prepared or produced by one or more of the Personnel of the Vendor in the performance of Services with one or more of the Personnel of the Client; but does not include any Joint Work Inventions. The foregoing includes all audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, Technical Information, techniques, templates, and working papers, of any kind; but does not include Inventions.

"**Losses**" means liabilities, losses, costs, damages and expenses (including legal, expert and consulting fees).

"**Master Agreement**" means this Master Agreement for Management Consulting Services, together with all Attachments and all agreements amending or supplementing this Master Agreement.

"**Master Agreement Expiry Date**" means June 15, 2017 (unless extended in accordance with Section 6.1).

"Maximum Price" means the maximum total amount, in Canadian funds, as set out in the Statement of Work, that the Vendor may charge the Client under that Statement of Work, including:

(a) all Fixed Price amounts;

(b) all amounts for Work performed on a Per Diem Rate basis;

(c) all applicable duties and taxes (including Harmonized Sales Tax (HST)); and

(d) all travel and accommodation expenses.

"**MGS**" means the Ministry of Government Services.

"**MGS Representative**" means one of the individuals designated as the MGS Representative or the Backup MGS Representative in Section 2.9, and any other individual designated as such pursuant to Section 2.9.

"**Minister (Client)**" means: (i) where the Client is a ministry of Ontario that has entered into the Statement of Work on behalf of Ontario, the minister that presides over the ministry, or any other person authorized to act on behalf of that minister; or (ii) where the Client is an OPS Entity, the individual with authority to enter into contracts on behalf of the OPS Entity, or any other person authorized to act on behalf of that person. For certainty, Minister (Client) may mean the Minister (MGS) where the Statement of Work is entered into by MGS on behalf of Ontario.

"**Minister (MGS)**" means the Minister of Government Services, or any other person authorized to act on behalf of the Minister of Government Services.

"**Moral Rights**" has the same meaning as in the Copyright Act, R.S.C. 1985, c. C-42, as amended or replaced from time to time, and includes comparable rights in applicable jurisdictions.

"**Ontario**" means Her Majesty the Queen in right of Ontario.

"**Ontario Data**" means: (1) all data (including all information whether or not Personal Information, and whether or not contained in or on any database or electronic information storage system or media owned by or in the custody or control of the Client and, if the Client is an institution that is subject to FIPPA, recorded in any Record) of any kind and in any form, provided by Ontario or the OPS Entity, to the Vendor to enable the Vendor to perform the Services or otherwise owned by or in the custody or control of Ontario or the OPS Entity; (2) all Personal Information collected by the Vendor as part of the Services; and (3) all such data that are created, developed, generated, prepared or produced as a result of any compilation (whether combined or compiled with other data or not) or developments or modifications to the data described above, but where the Vendor's data are combined or compiled with Ontario Data, excluding the Vendor's data that are proprietary to the Vendor immediately prior to the Project Start Date or are proprietary to the Vendor but are not first created or produced in the performance of Services.

"**Ontario Government Insignia**" means the visual identity of the Government of Ontario and any Ontario government design, domain name, geographical indication, insignia, logo, official mark or other designation, indication, symbol or trademark, including any developments and modifications of them.

"**Ontario Materials**" means, in respect of a Statement of Work: (a) all audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, Technical Information, templates, and working papers, recorded in any form and on any media, that are: (i) proprietary to Ontario or the OPS Entity, and provided to the Vendor to enable the Vendor to perform the Services; or (ii) created, developed, generated, prepared or produced by the Client or by one or more of the personnel of the Client (including any contribution made by one or more personnel of the Client to any Joint Work Material); and all such materials that are created, developed, generated, prepared or produced as a result of any developments or modifications to the material described in this subparagraph (a); (b) all second stage selection documents issued by Ontario or the OPS Entity; (c) all materials described in the Statement of Work as remaining the property of Ontario or the OPS Entity; and (d) all Third-Party Ontario Materials.

"**Ontario Public Service**" means the ministries and other administrative units of Ontario over which ministers of Ontario preside, and for the purposes of this Master Agreement, request for services issued pursuant to this Master Agreement and each Statement of Work includes its agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature, and OPS Entities, and "OPS" has the same meaning.

"**OPS Confidential Information**" means all information of the Ontario Public Service and of the Client's Subcontractors that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the OPS, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor or its Subcontractors in connection with this Master Agreement, a request for services issued pursuant to this Master Agreement or a Statement of Work, including: (a) information relating to designs, drawings, flowcharts, Intellectual Property Rights, Inventions, patterns, plans, procedures, processes, reports, schematics, Technical Information, templates, and working papers; (b) electronic data stored or processed by the OPS; (c) all Confidential Work Information; (d) new information derived at any time from any such information whether created by the OPS, the Vendor or any third party; and (e) information that the OPS is obliged, or has the discretion, not to disclose under provincial or federal legislation; but OPS Confidential Information shall not include information that: (f) is or becomes generally available to the public without fault or breach by the Vendor, but only after that information becomes generally available to the public; (g) the Vendor can demonstrate to have been rightfully obtained by the Vendor, without any obligation of confidence of any kind, from a third party who had the right to transfer or disclose it to the Vendor free of any obligation of confidence; (h) the Vendor can demonstrate to have been rightfully known to or in the possession of the Vendor, free of any obligation of confidence, when disclosed; or (i) is independently developed by the Vendor without the use of any OPS Confidential Information.

"**OPS Entity**" means: (a) an advisory, adjudicative, regulatory (including those with governing boards) or operational services agency of the Province of Ontario; or (b) an entity designated by MGS as an OPS Entity, which designation may be amended from time to time at the sole discretion of MGS.

"**Party**" in respect of this Master Agreement, means Ontario or the Vendor, and "Parties" means both of them; but in respect of a Statement of Work, means: (i) Ontario, if the Statement of Work is entered into by a ministry or any combination of ministries; or (ii) the OPS Entity, if the Statement of Work is entered into by an OPS Entity; or the Vendor, and "Parties" means both of them.

"Per Diem Rate" means, in respect of a Role in a Statement of Work and subject to Article 13 (Limits on Charges under Statements of Work) of the Master Agreement, an amount set out in a Change Order to the Statement of Work, which the Vendor may charge for Services performed by an individual in a Role on one calendar day, which includes all labour and material costs, insurance costs, carriage and transportation costs, and other overhead, including any fees or other charges required by law; but excludes: (i) all applicable duties and taxes (including Harmonized Sales Tax (HST)); and (ii) all travel and accommodation expenses.

"**Performance Management Process**" means the process used by Ontario to evaluate and rate the performance of the Vendor and other vendors.

"**Permitted OPS Assignee**" means: (a) any OPS Entity; (b) any office of an officer of the Legislative Assembly or of the Ontario Legislature; (c) any Provincially Funded Organization; and (d) any non-governmental entity, where assignment to such non-governmental entity is necessitated by alternative service delivery, backward or forward integration, outsourcing, privatization, partnering, procurement endeavours, or similar activity.

"**Person**" includes if the context allows, an individual, company, corporation, limited liability company, limited liability partnership, partnership, unincorporated association, government or government agency, authority or entity however designated or constituted and includes successors to the foregoing.

"**Personal Information**" at all times, has the same definition as in subsection 2(1) of FIPPA, which, at the date first written above, is recorded information about an identifiable individual, and includes all such information obtained by the Vendor under or created by the Vendor pursuant to this Master Agreement or the Statement of Work.

"**Personal Knowledge**", in connection with any Personnel, means concepts, ideas or know-how acquired by the individual that are not retained in any electronic, optical, printed, written or other recorded form, which relate to information technology and are of a generic technical nature, and not specific to the operation and activities of Ontario or the OPS Entity, that amount to no more than an enhancement of that individual's personal knowledge, skill or expertise.

"**Personnel**" means (a) collectively, in the case of the Vendor, individuals who provide services to the Vendor or any of its Subcontractors in connection with a Statement of Work, whether as employees or independent contractors, and individuals who are assigned by the Vendor to perform Services pursuant to a Statement of Work; and (b) collectively, in the case of the Client, individuals who provide services to the Client or any of its Subcontractors, whether as employees or independent contractors, but excludes all individuals described under (a).

"**Privacy Provisions**" means, collectively, Article 27 (Privacy) and the provisions, if any, set out in the Statement of Work that relate to (a) the collection, use, disclosure or transfer of personal information; (b) compliance with FIPPA; (c) compliance with the Personal Information Protection and Electronic Documents Act, S.C. 2000, c.5, as amended or replaced from time to time; and (d) compliance with any other legislation that would address the management of personal information or other privacy issues.

"**Proceeding**" means any action, claim, demand, lawsuit, or other proceeding.

"**Project Start Date**" means, in respect of a Statement of Work, the Project Start Date set out in the Statement of Work. For certainty, a Project Start Date cannot be a date that is earlier than the Effective Date of this Master Agreement.

"**Project End Date**" means, in respect of a Statement of Work, the Project End Date set out in the Statement of Work, subject to termination under Section 6.2 (Term of Statement of Work).

"**Project Term**" means, in respect of a Statement of Work, the term of such Statement of Work commencing on the Project Start Date and continuing in effect until the Project End Date, unless otherwise terminated in accordance with this Master Agreement or the Statement of Work.

"**Proposal**" means all of the documentation submitted by the Vendor in response to the RFP, including any clarifications provided by the Vendor at the request of MGS.

"**Proprietary Vendor Materials**" means all audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, and templates, and any other recorded information in any form or on any medium, that are proprietary to the Vendor immediately prior to the Effective Date or are proprietary to the Vendor but are not first created or produced in the Performance of Work, and that are incorporated into, provided or used in conjunction with any Deliverables or that are used by the Vendor to provide the Services.

"**Provincially Funded Organization**" means: (a) any public sector entity of the Province of Ontario; or (b) any other entity designated by MGS as a Provincially Funded Organization, which designation may be amended from time to time at the sole discretion of MGS; but excludes (i) Ontario, as represented by a ministry of Ontario over which a minister of the Crown, as appointed by the Lieutenant Governor under the Executive Council Act, R.S.O. 1990, c. E.25, presides, or any combination of such ministries; and (ii) OPS Entities.

"**Provincially Funded Organization Notice**" shall have the meaning ascribed to the capitalized term in Section 4.3.

"**Provincially Funded Organization Agreement**" means an agreement between the Vendor and a Provincially Funded Organization as defined in Section 4.1.

"**Record**" means any recorded information, including any Personal Information, in any form: (a) provided by Ontario to the Vendor, or provided by the Vendor to Ontario, for the purposes of this Master Agreement; (b) provided by Ontario or the OPS Entity to the Vendor, or provided by the Vendor to Ontario or the OPS Entity, for the purposes of the Statement of Work; or (c) created by the Vendor in the performance of the Statement of Work; and shall exclude any "Records" described in the Statement of Work as not being in the custody or control of MGS or the Client.

"**Requirements of Law**" mean all applicable requirements, laws, statutes, codes, acts, ordinances, orders, decrees, injunctions, by-laws, rules, regulations, official plans, permits, licences, authorisations, directions of, and agreements with, all Authorities that now or at any time hereafter may be applicable to this Master Agreement, the Statement of Work, the Vendor, Ontario, the OPS Entity, the Services, or the Deliverables, or any part of them.

"**RFP**" means the Request for Proposals dated December 4, 2013 for Management Consulting Services, reference number OSS-00426611 issued by Ontario, as represented by the Minister (MGS), and any addenda to it.

"**Role**" means one role set out in Attachment A, restricted to one experience level in one service category for that role as set out in Attachment A.

"**Security Clearance Checks**" has the meaning set out in Article 10.

"**Services**" means all services and work to be provided or performed pursuant to a Statement of Work and includes everything that is necessary to be done, supplied or delivered by: (a) the Vendor; (b) the Vendor's Personnel; (c) the Vendor's Subcontractors; and (d) those for whom the Vendor is responsible.

"**Statement of Work**" means a contract for the performance of Services constituted by a document substantially in the form of Attachment B (Form of Statement of Work - Ministries) or Attachment C (Form of Statement of

Work – OPS Entity), as applicable, entered into by the Parties pursuant to this Master Agreement, which incorporates by reference the terms of this Master Agreement, and which identifies the Client, the Vendor, the Services and the other information set out in that Attachment. A "Statement of Work" includes all Change Orders made to it.

"**Subcontractor**" means, in the case of each Party, any contractor of that Party or any of its subcontractors at any tier of subcontracting.

"**Technical Information**" means recorded information of a technical nature as it relates to management consulting in any form and on any media, including any designs, drawings, know-how, methods, methodologies, patterns, plans, procedures, processes, schematics, specifications, techniques, templates, and working papers, but does not include data, databases, documentation, Inventions or software.

"**Term**" means: (a) in respect of this Master Agreement, the period of time commencing on the Effective Date and ending on the earlier of: (i) the Master Agreement Expiry Date; or (ii) the date of termination of this Master Agreement if it is terminated in accordance with its terms; or (b) in respect of a Statement of Work, the Project Term.

"**Third-Party Ontario Materials**" means any audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, Technical Information, templates, and working papers, and any other recorded information in any form and on any media, and any components of the Ontario Materials, that are not proprietary to Ontario or the OPS Entity; and that are licensed by Ontario or the OPS Entity from any third parties; but only to the extent that they are protected by Intellectual Property Rights or are not to be disclosed pursuant to obligations of confidentiality.

"**Third-Party Vendor Materials**" means all audio and video recordings, data, databases, designs, documents, drawings, images, information, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, and templates, and any other recorded information in any form or on any medium, that are not proprietary to the Vendor; that are licensed by the Vendor from any third parties and that are not to be assigned, sold or transferred to the Client; that are not first created or produced in the performance of Work; and that are incorporated into, provided or used in conjunction with the Deliverables or are used by the Vendor to provide Services.

"**Vendor Evaluation Information**" means any information about the Vendor in respect of the quality, timeliness in the delivery of Services and other qualitative measures of the Vendor and any of its Personnel and of any Work performed by the Vendor and any of its Personnel.

"**Vendor Materials**" means, in respect of a Statement of Work, all Proprietary Vendor Materials and all Third-Party Vendor Materials. For certainty, "Vendor Materials" excludes all Joint Work Inventions, Joint Work Material, Ontario Data, Ontario Materials, Vendor Work Inventions, and Vendor Work Information (and if Attachment D applies, Non-Technical Work and Other Work Inventions).

"**Vendor Representative**" means one of the individuals designated as the Vendor Representative or the Backup Vendor Representative in Section 2.9, and any other individual designated as such pursuant to Section 2.9.

"**VOR Anniversary Date**" means the 16th day of June of each calendar year.

"**Work**" means work performed under, or as a result of, the Statement of Work.

"**WSIA**" means the Workplace Safety and Insurance Act, 1997, S.O. 1997, c.16, Sch. A., as amended or replaced from time to time.

"**WSIB**" means Workplace Safety and Insurance Board of Ontario.

ARTICLE 2. INTERPRETATION

2.1 Interpretation

In this Master Agreement and each Statement of Work, unless it is otherwise clear from the context, the following terms shall have the following meanings:

(a) "**development and modification**" includes enhancement, improvement, and revision; "developments and modifications" includes all of these terms in the plural; and, "**development or modification**" and "**developments or modifications**" includes, and "**develop and modify**", "**develop or modify**" and "**developed or modified**" have corresponding meanings.

(b) "**including**" means "including without limitation" and "**includes**" means "includes without limitation"; the use of the word "including" or "includes" is not intended to limit any statement that precedes it to the items immediately following it.

2.2 No Indemnities from Ontario or OPS Entities

Despite anything else in: (i) this Master Agreement; (ii) any Statement of Work; or (iii) any document referenced in a Statement of Work relating to the Deliverables or Services; any express or implied reference to Ontario or any OPS Entity providing an indemnity or any other form of indebtedness or contingent liability that would directly or indirectly increase the indebtedness or contingent liabilities of Ontario or any OPS Entity, whether at the time of execution of this Master Agreement or any Statement of Work or at any time during the Term of this Master Agreement or the Project Term of any Statement of Work, shall be void and of no legal effect.

2.3 Entire Agreement

This Master Agreement embodies the entire agreement between the Parties with regard to its subject matter and supersedes any prior understanding or agreement, collateral, written or otherwise, related to the subject matter of this Master Agreement that exists between the Parties at the date of execution of this Master Agreement. Subject to the terms and conditions of this Master Agreement, each Statement of Work embodies the entire agreement between the Parties with regard to the provision of the Services subject to the Statement of Work and supersedes any prior understanding or agreement, collateral, written or otherwise, related to the subject matter of the Statement of Work that exists between the Parties at the date of execution of the Statement of Work.

2.4 Amendments

Any changes to this Master Agreement shall only be made by written amendment signed by the Minister (MGS) and the Vendor, except where this Master Agreement expressly provides for a deemed amendment. Any changes to a Statement of Work shall only be made by written amendment signed by the Minister (Client) and the Vendor, except where this Master Agreement expressly provides for a deemed amendment. No changes shall be effective or shall be carried out in the absence of such an amendment.

2.5 Severability

If any term or condition of this Master Agreement or any Statement of Work, or the application thereof to the Parties or circumstances, is to any extent invalid or unenforceable, the remainder of this Master Agreement and the Statement of Work, as the case may be, and the application of such term or condition to the Parties or circumstances other than those to which it is held invalid or unenforceable, shall not be affected by it.

2.6 Conflict in Documents

In the event of a conflict or inconsistency in any provisions in this Master Agreement, the RFP and the Proposal, or any of them, this Master Agreement shall govern over the RFP and the Proposal; and the RFP shall govern over the Proposal. In the event of any conflict or inconsistency between the terms and conditions of this Master

Agreement and a Statement of Work or a Change Order, or any other document issued to put into effect the terms and conditions of the Statement of Work, this Master Agreement shall prevail.

2.7 Headings

The division of this Master Agreement into Articles, Sections and subsections and the insertion of headings are for convenience of reference only and shall not affect the construction or interpretation of this Master Agreement or any Statement of Work. The Article and Section headings in this Master Agreement are not intended to be full or accurate descriptions of the text to which they refer. References in this Master Agreement to an Article, Section, subsection or Attachment refer to the applicable Article, Section, subsection or Attachment of this Master Agreement unless otherwise stated.

2.8 Force Majeure

No Party shall be liable for damages caused by delay or failure to perform its obligations under a Statement of Work where such delay or failure is caused by an event beyond its reasonable control. The Parties agree that an event shall not be considered beyond one's reasonable control if a reasonable business person applying due diligence in the same or similar circumstances under the same or similar obligations as the provisions of the Statement of Work would have put in place contingency plans to either materially mitigate or negate the effects of such event. Without limiting the generality of the foregoing, the Parties agree that force majeure events shall include acts of God, natural disasters, acts of war, riots, plagues, epidemics, insurrection and terrorism but shall not include shortages or delays relating to supplies or services. If a Party seeks to excuse itself from its obligations under the Statement of Work due to a force majeure event, that Party shall immediately notify the other Party of the delay or non-performance, the reason for such delay or non-performance and the anticipated period of delay or non-performance. If the anticipated or actual delay or non-performance exceeds fifteen (15) Business Days, the other Party may immediately terminate the Statement of Work by giving notice of termination and such termination shall be in addition to the other rights and remedies of the terminating Party under the Statement of Work, at law or in equity.

2.9 Notices by Prescribed Means

Notices shall be in writing and shall be delivered by postage-prepaid envelope, e-mail, or personal delivery as follows:

(a) Notices to MGS shall be addressed to the attention of an individual designated as the MGS Representative at:

Ministry of Government Services
Supply Chain Ontario
Enterprise Procurement Branch
222 Jarvis Street, 8th Floor
Toronto, ON M7A 0B6

(b) Notices to the Vendor shall be addressed to the attention of an individual designated as the Vendor Representative at:

«Proponent_Name»
«Address_1_UnitStreet_Street_Name_P_»
«Address_2_City_Province__Postal_Code»

(c) Notices to the Client shall be addressed to the attention of an individual designated as the Client Representative in the Statement of Work at the address designated for service in the Statement of Work.

Notices by postage-prepaid envelope shall be deemed to have been given on the fifth Business Day after mailing. Notices by personal delivery or e-mail shall be deemed to have been given on the first Business Day after receipt by the other Party (except as provided for in Section 9.4). In the event of a

postal disruption, notices must be given by personal delivery or e-mail. Unless the Parties expressly agree in writing to additional methods of notice, notices may only be provided by the methods contemplated in this Section.

MGS Representative: Title: E-Mail:	**Wes Lapish** **Director, Enterprise Procurement Branch** **Wes.Lapish@Ontario.ca**
Backup MGS Representative: Title: E-Mail:	**Eric Smith** **Manager, Services Procurement; Enterprise Procurement Branch** **Eric.T.Smith@Ontario.ca**
Vendor Representative: E-Mail:	**«Contact_Name»** **«Email»**

Each Party may change its address or designated representative for receipt of notices by providing notice to the other Party.

2.10 Governing Law

This Master Agreement and each Statement of Work shall be governed by the laws in effect in the Province of Ontario and the applicable federal laws of Canada. The Parties irrevocably and unconditionally submit to the non-exclusive jurisdiction of the courts of the Province of Ontario and all courts competent to hear appeals from them. The Parties agree that the United Nations Convention on Contracts for the International Sale of Goods does not apply to this Master Agreement or to any Statement of Work and is strictly excluded.

2.11 Currency

All amounts set out in this Master Agreement and any Statement of Work and all payments shall be in Canadian funds.

2.12 Rights and Remedies

The rights and remedies of the Parties under this Master Agreement and under each Statement of Work are cumulative, and are in addition to and not in substitution for any rights or remedies provided at law or in equity, and shall not merge upon termination of this Master Agreement or of any Statement of Work.

2.13 No Waiver

No provision of this Master Agreement or any Statement of Work shall be deemed waived, amended, or modified by either Party unless such waiver, amendment, or modification is in writing and signed by the Party against whom it is sought to enforce the waiver, amendment, or modification.

2.14 Attachments

The following attachments form part of this Master Agreement:

(a) Attachment A to Master Agreement – Service Categories and Roles

(b) Attachment B to Master Agreement – Form of Statement of Work - Ministries

(c) Attachment C to Master Agreement – Form of Statement of Work - OPS Entity

(d) Attachment D to Master Agreement – Vendor/Client Ownership Provisions

(e) Attachment E to Master Agreement – Client Ownership Provisions

(f) Attachment F to Master Agreement – Assignment of Copyright

(g) Attachment G to Master Agreement – Waiver of Moral Rights

(h) Attachment H to Master Agreement – Confidentiality Agreement

(i) Attachment I to Master Agreement – Invention Disclosure Form

(j) Attachment J to Master Agreement – Provincially Funded Organization Acknowledgement

ARTICLE 3. SCOPE

3.1 General

This Master Agreement sets out terms and conditions applicable to the acquisition and performance of Services pursuant to the RFP.

3.2 Acquisition of Services

Each Client may, pursuant to the terms and conditions of this Master Agreement, acquire Services based on the role(s) corresponding to the service category(s) specified in Attachment A at any time prior to the Master Agreement Expiry Date, but only by entering into a Statement of Work. Services shall be performed only pursuant to a Statement of Work. It shall be a term of each Statement of Work that the Vendor agrees to provide, subject to the terms of this Master Agreement and the applicable Statement of Work, all of the Services that fall within the scope of each Statement of Work.

3.3 Statements of Work

Each Statement of Work shall include the terms and conditions of this Master Agreement by reference and shall constitute a separate contract from every other Statement of Work. No term or condition set out in any Statement of Work shall have any effect upon any other Statement of Work. Each Statement of Work shall be governed by all of the terms and conditions of this Master Agreement and such additional terms and conditions as may be set out in the Statement of Work that are not inconsistent with the terms of this Master Agreement.

3.4 No Obligation to Enter into any Statement of Work

Neither Ontario nor any OPS Entity is under any obligation to enter into any Statement of Work with the Vendor.

3.5 Work Volumes; Non-Exclusivity

The Vendor acknowledges and agrees that Ontario makes no representation, warranty, guarantee or other agreement regarding the volume of services to be acquired from the Vendor pursuant to this Master Agreement. The Vendor acknowledges that it enters into this Master Agreement and each Statement of Work on a non-exclusive basis. Ontario and each OPS Entity reserves the right to contract with other parties, regardless of whether such other party was selected within or outside a process initiated by a request for proposals, for the same or similar services as those provided by the Vendor and reserves the right to obtain the same or similar services internally.

3.6 Exclusions

Under a Statement of Work, the Vendor and the Vendor's Personnel shall not:

(a) develop or modify any computing programming code or software programs; or

(b) unless otherwise agreed to by the Client in the Statement of Work pursuant to Section 21.1 (Request for Consent) (if Attachment D applies to the Statement of Work) or Section 19.1

(Request for Consent) (if Attachment E applies to the Statement of Work), provide to the Client or incorporate into any Deliverables any Vendor Materials.

3.7 No Restrictive Material

Without limiting any other provisions of this Master Agreement or the Statement of Work, the Vendor shall not provide or incorporate (or permit those for whom it is responsible, including its Subcontractors and Personnel to incorporate) into any Deliverables, or request a Client to consent to the Vendor providing or incorporating into any Deliverables, and shall not use or permit the use in the provision of the Services, any Restrictive Material. In this Article, "Restrictive Material" means:

(a) any art, process, machine, manufacture or composition of matter, or any improvement in any of the foregoing; or

(b) any recorded information of any nature in any form, including any assets, audio and video recordings, data, databases, designs, documents, drawings, images, information, know-how, materials, methodologies, plans, procedures, processes, products, records, reports, specifications, techniques, Technical Information, templates or working papers, including any modification to any of the foregoing;

that would:

(i) in any way restrict the ability to exercise the Intellectual Property Rights or permissions granted under this Master Agreement or any Statement of Work;

(ii) prevent the Vendor from licensing the Deliverables on the terms and conditions of this Master Agreement or any Statement of Work;

(iii) interfere with the rights granted under the Statement of Work resulting from incompatibility between the terms and conditions applicable to components of the Deliverables;

(iv) violate any licences that apply to any part of the Deliverables when the Deliverable is used in accordance with this Master Agreement or the Statement of Work; or

(v) prevent the Client at any time from entering into any contract with any contractor other than the Vendor for the development or modification or other use of the Deliverables.

ARTICLE 4. PROVINCIALLY FUNDED ORGANIZATIONS

4.1 Provincially Funded Organization Agreements

If the Vendor wishes to provide products and services to Provincially Funded Organizations, the Vendor may only do so under a separate agreement with a Provincially Funded Organization. If the Vendor receives a request from any Provincially Funded Organization to supply products and services to the Provincially Funded Organization that are the same as the Deliverables and the Services, the Vendor shall: (a) prior to engaging in negotiations with that Provincially Funded Organization, provide the Provincially Funded Organization with a copy of the acknowledgement as attached as Attachment J to this Master Agreement ("**Provincially Funded Organization Notice**"); and (b) subject to the Vendor's compliance with subsection (a) above, use commercially reasonable efforts to negotiate with that Provincially Funded Organization for the purpose of entering into a mutually agreeable agreement for the supply to the Provincially Funded Organization of products and services that are the same as the Deliverables and the Services ("**Provincially Funded Organization Agreement**") based on the same or similar terms (including price and the length of the term) of this Master Agreement.

The Vendor agrees that the Vendor and the Provincially Funded Organization remain solely responsible for negotiating the terms and conditions (including all business, legal and other terms as may be necessary or desirable for the Vendor and the Provincially Funded Organization) of the Provincially Funded Organization

Agreement and for any resulting or related relationships and agreements between the Vendor and the Provincially Funded Organization.

4.2 Status of Provincially Funded Organizations

Provincially Funded Organizations cannot enter into any Statement of Work or any other subordinate agreement to this Master Agreement to acquire any Deliverables or Services or any other products and services under this Master Agreement.

4.3 Ontario Not Liable for Vendor's Relationship with Provincially Funded Organizations

The Vendor acknowledges and agrees as follows:

(a) Ontario does not endorse, recommend or approve the suitability of: (i) any Provincially Funded Organization as a customer of the Vendor; and (ii) the terms and conditions of this Master Agreement (or any subordinate agreement under this Master Agreement) as a basis for, in whole or in part, any Provincially Funded Organization Agreement or any other resulting or related relationships or agreements between the Vendor and any Provincially Funded Organization. The Vendor is solely responsible for conducting its own independent assessment (including obtaining its own professional advice as may be necessary and appropriate in the Vendor's specific circumstances) to determine the suitability of the above.

(b) Ontario makes no representation, assurance, warranty, or guarantee: (i) that any Provincially Funded Organizations will acquire products or services from or consider the products or services of the Vendor; or (ii) of the value or volume of products or services that may or will be ordered, if any, by any or all Provincially Funded Organizations.

(c) Ontario will not, in respect of any Provincially Funded Organization Agreement or any resulting or related relationships or agreements between the Vendor and any Provincially Funded Organization: (i) be or be deemed to be a party to, or a guarantor of any obligations or liability of any party under, any Provincially Funded Organization Agreements or any such relationships or agreements; or (ii) be responsible or liable to the Vendor or any third party for any costs, obligations, liabilities or covenants of the Provincially Funded Organization, and nothing in any agreement between the Vendor and any Provincially Funded Organization shall have the effect of imposing or resulting in the imposition of any costs, obligations, liabilities or covenants on Ontario.

(d) The Vendor shall not, in relation to or under any Provincially Funded Organization Agreement or under any resulting or related relationships or agreements between the Vendor and any Provincially Funded Organization, bring any Proceedings against Ontario or any of its Personnel or any Indemnified Party as a result of: (i) any act, error or omission of the parties to the Provincially Funded Organization Agreement; or (ii) any act, error or omission of Ontario or any of its Personnel.

(e) The Vendor is solely responsible for its own contract administration with each Provincially Funded Organization and shall not direct any issues that may arise with any Provincially Funded Organization to Ontario.

(f) For the purposes of any Provincially Funded Organization Agreement, the Vendor acknowledges that Provincially Funded Organizations have no power or authority to bind Ontario or to assume or create any obligation or responsibility, express or implied, on behalf of Ontario.

(g) Despite any provision in this Master Agreement to the contrary, the Vendor shall be responsible for any and all Losses suffered by any Indemnified Party arising out of or in connection with any Provincially Funded Organization Agreement or any breach by the Vendor of this Article 4 (Provincially Funded Organizations).

4.4 Disclosure of Information

(a) Ontario may, from time to time and at its sole discretion, inform any or all Provincially Funded Organizations of: (i) the Vendor's status as a vendor of record; (ii) the products and services of the Vendor that are available to Ontario under this Master Agreement; and (iii) the Vendor's obligation under this Section 4.4 and under Section 4.1. In addition, Ontario and any OPS Entity may disclose, and the Vendor consents to the disclosure, to Provincially Funded Organizations of this Master Agreement or any part of it (including pricing), as amended. For certainty, the Vendor agrees that neither this Master Agreement or any part of it is considered Confidential Vendor Information and no notice to or further consent of the Vendor is required prior to disclosure to any Provincially Funded Organization.

(b) If the Vendor is requested by a Provincially Funded Organization to do so, the Vendor shall provide to that Provincially Funded Organization the following documents and information: (i) the RFP and other related procurement documents that were publicly issued; and (ii) the Vendor's proposal in response to the RFP, but only to the extent that it does not include OPS Confidential Information.

(c) The Vendor agrees to provide to Ontario, at Ontario's request, data and information regarding Provincially Funded Organization access to and acquisition of products and services from the Vendor.

(d) The Vendor consents to Ontario receiving data and information from a Provincially Funded Organization of such Provincially Funded Organization's request for access to and acquisition of products and services from the Vendor.

ARTICLE 5. LEGAL RELATIONSHIPS AMONGST THE PARTIES & THIRD PARTIES

5.1 Vendor and its Personnel Not an Agent, Employee or Partner

The Vendor shall have no power or authority to bind Ontario or any OPS Entity or to assume or create any obligation or responsibility, express or implied, on behalf of Ontario or any OPS Entity. The Vendor shall not hold out itself, or any of its Personnel, as an agent, employee or partner of Ontario or of any OPS Entity. Nothing in this Master Agreement or any Statement of Work shall have the effect of creating an agency, employment or partnership relationship between Ontario or any OPS Entity and the Vendor (or any of the Vendor's directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors), or constitute an appointment under the Public Service of Ontario Act, 2006, S.O. 2006, Chapter 35, as amended. The Vendor is solely responsible for all legally required employer and employee contributions and deductions, compensation and benefits for itself and its Personnel.

5.2 Responsibility of Vendor

The Vendor agrees that it is liable for the acts and omissions of its and of its Subcontractors' directors, officers, Personnel, agents, partners, affiliates, and volunteers. The Vendor shall advise these individuals and entities of its obligations under this Master Agreement and under the Statement of Work and, without limiting the generality of the foregoing, shall take appropriate action to ensure compliance with (a) this Master Agreement and the Statement of Work generally, (b) the requirements of Article 26 (OPS Confidential Information), and (c) the Privacy Provisions. Ontario and the OPS Entities shall have no liability (vicarious or otherwise) for any acts or omissions of the Vendor's and its Subcontractors' directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors. This Section is in addition to any and all of the Vendor's liabilities under this Master Agreement, each Statement of Work and under the general application of law. This Section shall survive the termination or expiry of this Master Agreement and every Statement of Work.

5.3 Subcontracting or Assignment

The Vendor shall not subcontract or assign the whole or any part of this Master Agreement without the prior written consent of the Minister (MGS). Such consent shall be in the sole discretion of the Minister (MGS) and

subject to the terms and conditions that may be imposed by the Minister (MGS). The Vendor shall not subcontract or assign the whole or any part of any Statement of Work or any monies due under it without the prior written consent of the Minister (Client). Such consent shall be in the sole discretion of the Minister (Client) and subject to the terms and conditions that may be imposed by the Minister (Client). Without limiting the generality of the conditions which the Minister (Client) may require prior to consenting to the Vendor's use of a Subcontractor, every contract entered into by the Vendor with a Subcontractor shall adopt all of the terms and conditions of this Master Agreement and the Statement of Work as far as applicable to those parts of the Services provided by the Subcontractor. Nothing in this Master Agreement or any Statement of Work shall create a contractual relationship between any Subcontractor or its employees and Ontario or any OPS Entity.

5.4 Assignment of Statement of Work by the Client

Provided that the Vendor has received prior written notice of the Client's intent to assign: (a) where the Client is Ontario, the Minister (Client) may assign without the consent of the Vendor all or any part of a Statement of Work to any OPS Entity, any office of an officer of the Legislative Assembly or of the Ontario Legislature, any Provincially Funded Organization, or where such assignment is necessitated by outsourcing, privatizing, partnering or similar activity, to a non-governmental entity; and (b) where the Client is an OPS Entity, the Minister (Client) may assign without the consent of the Vendor all or any part of a Statement of Work to Ontario, or where such assignment is necessitated by outsourcing, privatizing, partnering or similar activity, to a non-governmental entity.

5.5 Duty to Disclose Change of Control

If the Vendor undergoes a change in control, the Vendor shall disclose such change in control to the MGS Representative within fourteen (14) calendar days of such change in control and shall comply with any reasonable terms and conditions subsequently prescribed by MGS resulting from the disclosure.

5.6 Conflict of Interest

The Vendor shall, and shall require each of its Personnel to: (a) avoid any Conflict of Interest in the performance of its contractual obligations; (b) disclose to MGS and the Client without delay any actual or potential Conflict of Interest that arises during the performance of its contractual obligations; and (c) comply with any requirements prescribed by MGS or the Client to resolve any Conflict of Interest. In addition to all other contractual rights or rights available at law or in equity, the Minister (MGS) may, at its sole discretion, immediately terminate this Master Agreement, and the Minister (Client) may, at its sole discretion, immediately terminate any or all Statements of Work, upon giving notice to the Vendor where (i) the Vendor fails to disclose an actual or potential Conflict of Interest; (ii) the Vendor fails to comply with any requirements prescribed by MGS or the Client, as the case may be, to resolve a Conflict of Interest; or (iii) the Vendor's Conflict of Interest cannot be resolved. This Section shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

5.7 Binding Nature

This Master Agreement and each Statement of Work is binding upon, and enures to the benefit of, the Parties and their respective successors and permitted assigns.

ARTICLE 6. TERM

6.1 Term of Master Agreement

This Master Agreement shall be in effect from and including the Effective Date and shall remain in force until and including the Master Agreement Expiry Date, unless terminated earlier in accordance with the terms of this Master Agreement or unless extended by the Minister (MGS), in its sole discretion, on the same terms and conditions (excluding any option to further extend this Master Agreement during the extension period) for an additional period of twelve months by written notice from MGS to the Vendor given not less than sixty (60) days prior to the Master Agreement Expiry Date.

6.2 Term of Statement of Work

The Project Term with respect to a Statement of Work shall commence on the applicable Project Start Date, and shall continue until the Project End Date, unless terminated earlier in accordance with the terms of this Master Agreement or the Statement of Work. Except as provided for in Section 6.3, a Project End Date may only be extended by a Change Order.

For certainty, a Project End Date in a Statement of Work can be a date that is up to twelve months past the end of the Term of the Master Agreement. Despite anything to the contrary in any Statement of Work or any Change Order, any Statement of Work, which is in effect on the last day of the twelve-month period commencing immediately after the end of the Term of the Master Agreement, shall terminate on that day.

6.3 Extension of Project End Dates Due to Labour Disruption

If there is a labour disruption (e.g. a lawful or unlawful strike or a lock-out) or threatened labour disruption by Crown employees, the Client may notify the Vendor of the Client's intent to, among other things, extend the Project End Date. In such notice, the Client shall specify the anticipated time period of the impact or potential impact of the labour disruption or threatened labour disruption ("**Anticipated Disruption Period**"). Upon such notice being provided to the Vendor, the Project End Date and any dates set out in the Statement of Work which specify when obligations must be met (including any milestone dates, payment dates, etc.) shall be deemed to be amended to a later date that is equal to the number of days of the Anticipated Disruption Period, as set out in the Client's notice. If any of such amended date(s) falls on a non-Business Day, the Project End Date shall be deemed to be the next Business Day. The Client may revise any such Anticipated Disruption Period at any time and from time to time prior to the end of the Anticipated Disruption Period.

If the Anticipated Disruption Period exceeds fifty (50) consecutive Business Days, the Vendor may terminate the Statement of Work at any time effective after the fiftieth (50^{th}) Business Day by giving notice no less than five (5) Business Days prior to the Vendor's intended date of termination. If a Statement of Work is terminated by the Vendor pursuant to this Section 6.3 (Extension of Project End Dates Due to Labour Disruption), the Client shall be liable to the Vendor only for payment for Services properly performed and Deliverables delivered to and accepted by the Client up to and including the effective date of the termination, unless the Client and the Vendor agree otherwise in an agreement signed by both parties that expressly references this Section 6.3 (Extension of Project End Dates Due to Labour Disruption). For certainty, if a Statement of Work provides that payment will be due and owing upon the meeting of a specified milestone (such as, for example, delivery and/or acceptance of a specified Deliverable) and the effective date of the termination of the Statement of Work passes prior to the specified milestone being met, the Client is not liable to the Vendor for payment for Services performed and/or Deliverables delivered and/or accepted in relation to that specified milestone, unless the Client and the Vendor agree otherwise in an agreement signed by both parties that expressly references this Section 6.3 (Extension of Project End Dates Due to Labour Disruption). Termination shall not relieve the Vendor of its warranties and other responsibilities relating to the accepted Deliverables, the Services performed or money paid, or of its obligations upon termination of the Statement of Work. In addition to its other rights of hold back, the Client may hold back payment or set off against any payments owed if the Vendor fails to comply with its obligations on termination. The provisions of this Section 6.3 (Extension of Project End Dates Due to Labour Disruptions) shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 7. SECOND STAGE SELECTION PROCESS

7.1 Requests for Services

Any Client may issue a written request for services to the Vendor and to other vendors selected pursuant to the RFP, setting out a brief description of the services required, the timeframes, and any other requirements.

7.2 Proposals

If the Vendor wishes to respond to a request for services issued to the Vendor, it shall prepare, at no cost, a written proposal delivered to the Client setting out the list and description of the Deliverables, a list of the Roles (including experience levels) required, the names and resumes of the Personnel that it proposes to assign to each of the Roles, its proposed pricing, and the estimated duration of each position required to achieve completion of the proposed services within the timeframe specified in the request for services. The Vendor shall

comply with the submission requirements and other requirements in the request for services. The Vendor shall ensure that each individual proposed by the Vendor is qualified for the proposed Role. The Vendor shall provide the Client or its representatives with the opportunity to interview its proposed Personnel, at no cost. If the Vendor receives a request for services but does not intend to submit a proposal, it shall notify the Client that it will not do so.

The Client shall have the right in its absolute discretion to disqualify the Vendor, or reject all or any part of its proposal: (i) if the same individual is proposed by the Vendor and any other vendor; (ii) if an individual is proposed by the Vendor that Ontario or any OPS Entity determines is not suitable based on information provided by references, based on past performance on previous contracts or previous employment with the OPS, or based on Security Clearance Checks; or (iii) if any information provided by the Vendor is materially inaccurate or the Vendor makes a material misrepresentation or omission; and this right is in addition to any other express rights or any other rights which may be implied in the circumstances. Neither Ontario nor any OPS Entity shall be liable for any expenses, costs, losses or any direct or indirect damages incurred or suffered by the Vendor or any third party resulting from exercising any of its express or implied rights under this Section.

ARTICLE 8. PERFORMANCE BY VENDOR

8.1 Performance

Under each Statement of Work, the Vendor shall diligently carry out and complete the Services in accordance with the Statement of Work and Requirements of Law, and the Vendor shall:

(a) provide any and all labour, supplies, equipment and other goods or services that are necessary and can reasonably be understood or inferred to be included within the scope of the Statement of Work or customarily furnished by Persons providing services of the type provided under the Statement of Work in similar situations in the Province of Ontario; and

(b) adhere to commonly accepted norms of ethical business practices, including establishing, and ensuring adherence to, precautions to prevent its employees or agents from providing or offering gifts or hospitality of greater than nominal value to any person acting on behalf of or employed by the Client.

8.2 Use and Access Restrictions

The Vendor acknowledges that unless it obtains specific written preauthorization from the Client, any access to or use of OPS property, technology or information that is not necessary for the performance of its contractual obligations under a Statement of Work is strictly prohibited. The Vendor further acknowledges that Ontario and, if the Client is an OPS Entity, the OPS Entity, may monitor the Vendor to ensure compliance with this Section. This Section is in addition to and shall not limit any other obligation or restriction placed upon the Vendor.

8.3 Completion of Services

If any of the Services or Deliverables provided is not in accordance with the requirements of the Statement of Work and is not to the satisfaction of the Client, the Client may reject it or may issue a rectification notice to the Vendor setting out the manner and time-frame for rectification. Within seven (7) Business Days of receipt of a rectification notice, the Vendor shall either comply with that rectification notice at its own expense or provide a rectification plan satisfactory to the Client. If the Vendor fails to either comply with that rectification notice or provide a rectification plan that is satisfactory to the Client, the Client may immediately:

(a) accept all or any part of the Services or Deliverables (even if of diminished value) provided to the Client by the date specified by the Client, but the Client shall be liable to the Vendor only for payment for Services properly performed and Deliverables delivered to and accepted by the Client;

(b) terminate the Statement of Work; or

(c) do both (a) and (b) above.

If the Vendor has been given a prior rectification notice, the same subsequent type of non-compliance by the Vendor shall allow the Client to immediately terminate the Statement of Work.

8.4 Performance Management Process

The Vendor agrees to participate in, and comply with the terms of, the Performance Management Process. The Vendor acknowledges that the Performance Management Process may be changed from time to time by Ontario at Ontario's sole discretion. Without limiting the foregoing, the Vendor acknowledges and agrees:

(a) to adhere to any guidelines and processes issued in respect of the Performance Management Process;

(b) to respond to requests from MGS or a Client for information or feedback arising out of or about the Performance Management Process (including responding to Vendor Evaluation Information), within the time frame specified in the request (or in the absence of a time frame, within a reasonable period of time);

(c) to meet with MGS or the Client, whether remotely or in person, at no charge to MGS or the Client, to discuss performance and other evaluations (including Vendor Evaluation Information) or any other issues arising out of or about the Performance Management Process;

(d) that performance ratings, performance feedback and other information about the Vendor and its Personnel gathered or obtained through the Performance Management Process (including Vendor Evaluation Information) may be made available to the OPS (including OPS Entities), as well as Provincially Funded Organizations;

(e) in addition to and without limiting any provision, statutory or otherwise, that protects employees or other personnel of Ontario or any OPS Entity from actions or proceedings for damages, the Vendor agrees that no action or proceeding for damages may be brought against any Personnel of Ontario or of any OPS Entity for any acts done in good faith in connection with the Performance Management Process (including any evaluation of the Vendor by any such Personnel) or for any alleged neglect or default in the execution in good faith of such Personnel's duty as it relates to the Performance Management Process; and

(f) that performance ratings and performance and other evaluations prepared or obtained through the Performance Management Process (including Vendor Evaluation Information) may be used by Ontario or OPS Entities under this VOR arrangement or any other vendor of record arrangement, as well as in other procurements, whether or not related to this VOR arrangement.

ARTICLE 9. PERSONNEL

9.1 Personnel Qualifications

The Vendor shall provide qualified Personnel under each Statement of Work. The Vendor shall not permit any individual to perform any Services in any Role if the individual does not have the experience level specified in the Statement of Work for that Role, or does not have the qualifications for that Role (other than the experience levels) as set out in Attachment A.

9.2 Performance by Named Individuals Only

The Parties agree that only those individuals named in a Statement of Work shall perform the Services on behalf of the Vendor. The Parties agree that each Statement of Work shall specify the Role for each named individual. The Vendor shall use commercially reasonable efforts to maintain continuity under a Statement of Work by using the same Personnel to perform the Services throughout the Project Term. The Vendor shall not

replace or substitute any of the individuals named in the Statement of Work without the prior written approval of the Client, which may not be arbitrarily or unreasonably withheld.

9.3 Replacement of Personnel

If the Client, in its sole discretion, deems any of the Vendor's Personnel to be inappropriate, the Client may require the Vendor to replace such Personnel. The Vendor shall immediately, upon receipt of the Client's request, remove any individual from performing any Services under the Statement of Work. The Vendor shall submit to the Client the name and resume of a suitable replacement for each of the Personnel deemed inappropriate by the Client. The Vendor shall provide the Client with the opportunity to interview its proposed Personnel, at no cost to the Client. The Vendor agrees that any proposed replacement Personnel must be qualified in the same Role and must possess similar or greater qualifications than the individual being replaced, and that the Client's approval may, at the Client's discretion, be subject to Article 10 (Security Clearance Checks). The Vendor shall not charge the Client more for the replacement under the Statement of Work, even if the replacement Personnel holds a more senior position or has more experience than the individual being replaced. If the Vendor fails to propose any replacement Personnel within three (3) Business Days, or proposes replacement Personnel who the Client deems, in its sole discretion, to be inappropriate or not available in a timely manner, the Minister (Client) may immediately terminate the Statement of Work by giving notice of termination and such termination shall be in addition to the other rights and remedies under the Statement of Work, at law or in equity. Neither Ontario nor any OPS Entity shall have any liability to the Vendor or any of its Personnel arising out of or in connection with such termination of the Statement of Work or with any replacement or request for replacement of any Personnel.

9.4 Substitution or Replacement Prior to or Shortly After Project Start Date

(a) If:

(i) prior to the Project Start Date, the Vendor notifies the Client of its intent to replace or substitute any individual named in a Statement of Work; or

(ii) on or within five (5) Business Days after the Project Start Date, the Vendor notifies the Client of its intent to replace or substitute any individual named in a Statement of Work within ten (10) Business Days after the Project Start Date;

the Client may, at its sole discretion, immediately terminate the Statement of Work by giving notice of termination and such termination shall be in addition to the other rights and remedies under the Statement of Work, at law or in equity. For certainty, the Client is not obligated to consider the replacement or substitute offered by the Vendor, or any individual proposed by the Vendor but not selected by the Client during the Second Stage Selection process for the Statement of Work, before exercising the right to terminate under this section.

(b) Termination under this Section 9.4 shall be in writing ("Termination Email Notice") and may be delivered via e-mail to the Vendor's representative identified in the Statement of Work or to the individual designated as the Vendor Representative in Section 2.9(b). The Termination E-mail Notice is considered delivered to the Vendor one (1) hour after it was sent.

(c) Payment, if any, for any Services performed or Deliverables delivered and accepted prior to the effective date of termination of the Statement of Work when terminated under this Section 9.4 shall be made in accordance with Section 36.4 (Payment to Vendor Upon Termination) of this Master Agreement.

ARTICLE 10. SECURITY CLEARANCE CHECKS

10.1 Definition

For the purposes of this Master Agreement, the following capitalized terms mean:

"**Company Level Check**" is a security screening check, which requires checks to be conducted on all directors and officers of the company, regardless of whether they will have direct involvement in the work associated with the procurement which was deemed to require security screening. In order to be issued a company level clearance, all directors and officers of the company and the Company Security Officer (CSO) must consent to security screening and obtain clearances. Company-level screening checks are conducted only where the security risk assessment indicates the necessity.

"**Company Security Officer**" is a person who holds that standing in the Contractor Security Screening Program. A Company Security Officer (or CSO) plays an administrative role in the security screening process on behalf of his or her company and must hold a valid security clearance issued by the Employee Relations Division of MGS (ERD, MGS) prior to performing that role. The CSO is responsible for the verification of identity for workers requiring screening for contracted work, where required.

"**Criminal Record Check**" is a search of the Canadian Police Information Centre (CPIC) database maintained by the RCMP, using an individual's name, date of birth and any other information necessary to verify identity, for information about the individual relating to:

- Convictions under the offense provisions of federal statutes recorded in the CPIC system;
- Records of discharges (absolute and conditional) which have not been removed from the CPIC system, in accordance with the *Criminal Records Act (Canada)*. Note: Information about absolute discharges will not be collected after one (1) year from the date of disposition. Information about conditional discharges will not be collected after three (3) years from the date of disposition;
- Charges that have been laid but are not resolved (unresolved charges) under the offense provisions of federal statutes; and
- Records of judicial orders in effect (e.g. warrants) that are related to federal offence charges or convictions.

"**Driver's Record Check**" is conducted where driving is a requirement for the contract where a valid driver's licence is required. It involves a check of provincial databases for information regarding driving history using the individual's driver licence number. This check provides a three year history of *Highway Traffic Act (Ontario)* and *Criminal Code* of Canada convictions and any current suspensions, along with the driver's current listed address and licence status.

"**General Level Security Screening Check**" requires the individual to obtain a Criminal Record Check (see the definition for Criminal Record Check for additional information). A general level security screening check may also include a Driver's Record Check, and/or an Out-of-Country Police Certificate (US and/or international), where required.

"**Other/Enhanced Level Security Screening Check**" is a higher level check that is required when the duties or tasks establish a risk level greater than can be addressed through a General Level Security Screening Check. Other/Enhanced level security screening checks include one or more of the following check types in addition to the General Level Security Screening Check: fingerprint-based criminal record check, personal history investigation, local police records check, family interview and/or financial background check.

"**Out-of-Country Driver's Record Check (US and/or International)**" is when the individual has lived outside Canada for more than six (6) months within the last five (5) years, an out of country driver records check from the jurisdiction(s) in which they have resided is required. This check includes information such as current suspensions, along with the driver's current listed address and licence status. Driver's record check is conducted where driving is a requirement for a Statement of Work where a valid driver's licence is required. If the certificate is not in French or English, the individual is to provide an English translation along with the original certificate.

"**Out of Country Police Certificate (US/International)**" is a summary of an individual's criminal record or a declaration of the absence of any criminal record from a law enforcement agency in another country outside of Canada. Police certificates are different in each state/country and may be called police clearance certificates, good conduct certificates, judicial record extracts, etc. Where an individual has lived outside of Canada for more than six (6) months within the last five (5) years, an out-of-country police certificate from the jurisdiction(s) in which they resided is required. If the certificate is not in French or English, the individual is to provide an English translation along with the original certificate.

"**Security Screening Check**" is the process conducted by the Vendor to gather information on designated persons for submission to the Client in order to obtain a Security Clearance and includes all of the following:

1. A written declaration by an individual disclosing any unresolved charges and previous convictions under the offence provisions of federal statutes, including but not limited to the *Criminal Code (Canada)*, for which a pardon under the *Criminal Records Act (Canada)* has not been granted;

2. a General Level Security Screening Check; and

3. Other/Enhanced Level Security Screening Check (if required, as determined by the Client or ERD, MGS).

"**Security Clearance**" means a decision made by ERD, MGS following receipt of the Security Screening Check documents that will permit the person being cleared to engage in the performance of the services.

10.2 Security Screening Check

(a) Security Clearances are not provided in perpetuity and are subject to revocation by MGS or the Client at its sole discretion at any time. Security Screening Checks shall be renewed at the intervals as may be specified by ERD, MGS.

(b) On notification from MGS, the Vendor shall, prior to entering into a Statement of Work or otherwise during the Term, provide to the ERD, MGS, completed Security Screening Checks for all persons engaged in the performance of the services who are either not cleared or for whom a renewal is required. All documents shall be provided through the Vendor's designated Company Security Officer.

(c) All Security Screening Checks shall be provided in form and content acceptable to the ERD, MGS and shall include all required consents.

(d) If a person or company has been deemed by the Ministry to require a Security Clearance they shall not engage in the performance of the services unless they have been provided a Security Clearance by the ERD, MGS.

10.3 Changes

(a) During the Term of this Master Agreement or a Statement of Work, or an agreement arising from it, the Vendor shall report to the ERD, MGS, within five Business Days thereof, any change to:

(i) any information provided as part of a Security Screening Check process;

(ii) employees, agents and subcontractors or, where a Company Level Check is required, partners, directors, officers and shareholders, who are or will be engaged in providing the security screening documents or engaged in the performance of the services.

(b) The ERD, MGS shall assess the above information and may instruct the Vendor to comply with any instructions arising which may include requests for provision of information to amend existing Security Clearances or provide for new Security Clearances.

10.4 Default under Agreement

During the Term of this Master Agreement and any Statement of Work, the Vendor shall be in default under this Master Agreement and the applicable Statement of Work if they fail to comply with the requirements of this Article.

ARTICLE 11. CHANGE MANAGEMENT

11.1 Change Requests and Impact Assessments

A Client may request a change to a Statement of Work by submitting to the Vendor a written change request reasonably detailing the scope and priority of the desired changes. The Vendor shall promptly evaluate each change requested by the Client. The Vendor shall promptly provide the Client with a written impact assessment which addresses relevant factors, including the implications for Roles, Personnel, deadlines, milestones, costs and any other terms and conditions of the Statement of Work. Such evaluation and assessment by the Vendor shall be made without charge to the Client. If the Vendor does not have sufficient resources to perform any requested changes in accordance with any time limits set out in the change request, the Vendor shall promptly notify the Client.

11.2 Change Orders

Each Change Order must contain:

(a) an effective date;

(b) a description of any additional Services to be performed or Deliverables to be provided, the names of the Vendor's Personnel necessary to perform such additional Services, and specifying the Role (including the experience level) for each named individual, and the availability of such Personnel over the relevant time period;

(c) a description of any Services, Roles or named individuals deleted from the Statement of Work, if applicable;

(d) a description of any other changes to the performance required of either Party, if applicable;

(e) a statement of the impact of the changes on the Services, Deliverables, deadlines, milestones, costs or other requirements of the Statement of Work;

(f) any new Maximum Price or Project End Date, if applicable;

(g) any new Fixed Price, if applicable;

(h) the Per Diem Rate for each additional Role, if applicable; and

(i) signatures of the duly authorized signing officers of each Party.

11.3 Changes to Milestones

If there is any change to the ability of the Vendor to meet an applicable milestone set out in the Statement of Work, the Vendor shall promptly notify the Client. Any changes to the applicable milestone set out in the Statement of Work and any terms and conditions of the Statement of Work resulting from the change must be effected by a Change Order.

11.4 Pricing for Requested Changes

(a) *Changes Impacting Fixed Price* - Where the change request results in an increase or a reduction to a Fixed Price, the Client and the Vendor shall negotiate: (i) the amount of the additional charge or reduction to the Fixed Price resulting from the change request, if

applicable; and (ii) the change to the Maximum Price under that Statement of Work resulting from the change request, if applicable. The increase or decrease to the Fixed Price and/or Maximum Price shall be set out in the Change Order.

Where the Client and the Vendor are unable to agree to a fixed amount of the increase to a Fixed Price resulting from a change request, the Vendor agrees that, at the Client's option, the Client may require that the Work be performed by the Vendor under the change request on a Per Diem Rate basis in accordance with subsection (b) (Per Diem Rate for Change Requests) of this Section 11.4.

(b) *Per Diem Rate for Change Requests* - Where a Per Diem Rate stated in the Statement of Work applies to a Role (at the same experience level) contemplated in the change request, the Per Diem Rate applicable to the change request shall be the Per Diem Rate for that Role as set out in the Statement of Work, or any lesser Per Diem Rate agreed to by the Client and the Vendor. Where Per Diem Rates stated in the Statement of Work do not apply to a Role (at the same experience level) contemplated in the change request, the Per Diem Rate for each individual in such Role may be negotiated between the Client and the Vendor within a reasonable period of time, provided that the Per Diem Rate complies with the provisions of the Master Agreement and this Section 11.4.

(c) *Changes Impacting Work Done on a Per Diem Rate Basis* - Where the change request results in a change impacting Work being done on a Per Diem Rate basis, the Client and the Vendor shall negotiate the change to the Maximum Price under the Statement of Work resulting from the change request. Where the change request results in the addition of a Role, the Per Diem Rate for that Role shall be determined in accordance with subsection (b) (Per Diem Rate for Change Requests) of this Section 11.4.

11.5 No Payment Without Executed Change Order

No change request shall be implemented or incorporated as part of a Statement of Work unless and until a Change Order has been executed by both the Minister (Client) and the Vendor. Under no circumstances will the Vendor be entitled to payment for any goods or services provided pursuant to a change request that have not been described in a Change Order.

ARTICLE 12. REPORTS

12.1 Monthly Usage Reports

The Vendor shall prepare a usage report (referred to in this Article as a "Usage Report") for each calendar month for: (a) every Statement of Work (including any extension to a Statement of Work) and every Change Order entered into by the Vendor pursuant to this Master Agreement; and (b) the value and volume of all services acquired by Provincially Funded Organizations from the Vendor under Provincially Funded Organization Agreements that are the same as the Services under this Master Agreement. If no Statements of Work or Change Orders are entered into during a calendar month, the Vendor shall submit a NIL report. In each Usage Report, the Vendor shall set out the name of the Vendor, the month and year covered, and all other information described below in this Article. The Vendor shall provide each Usage Report to the MGS Representative within ten (10) Business Days of the end of the applicable month.

12.2 Contents of Usage Report

In each Usage Report, the Vendor shall include the following information: (1) in respect of each Statement of Work in effect during the applicable calendar month: (a) vendor of record (VOR) number; (b) ministry/cluster/OPS Entity; (c) branch; (d) contract signing date; (e) contact information (name, e-mail address, phone) of the ministry or OPS Entity for which the Statement of Work is being performed; (f) Statement of Work number; (g) description of Services; (h) purchase order number (optional additional information field for Vendor); (i) Project Start Date; (j) Project End Date (or anticipated completion date of project); (k) consultants' roles; (l) Service Category in which consultants are working; (m) estimated cost (contract value); (n) contract extension

information; and (o) such other information as MGS may require; and (2) the value and volume of all services acquired by Provincially Funded Organizations from the Vendor under Provincially Funded Organization Agreements that are the same as the Services under this Master Agreement. The Vendor shall include the total dollar amount of all Statements of Work issued during that month (excluding Harmonized Sales Tax) to all Clients, and any other information that is reasonably requested by MGS. Any extension or change to a Statement of Work, including dollar amount, must be reported during the month that extensions or changes took place.

12.3 Format of Usage Report

The Usage Form must be provided in the form available for downloading as an Excel file from: http://www.doingbusiness.mgs.gov.on.ca/mbs/psb/vordb.nsf/english/home_page?openDocument&login, or from such other web address as MGS may notify the Vendor. The Vendor shall send each Usage Report by electronic mail to the MGS Representative at the email address stipulated by notice from MGS to the Vendor.

12.4 Costs

The Vendor shall be solely responsible for all costs associated with establishing, preparing, supporting and producing each Usage Report and all other reports covered by this Article.

12.5 Other Documentation

The Vendor shall provide the MGS Representative from time to time with any other documentation that the MGS Representative requests or which is required by this Master Agreement.

ARTICLE 13. LIMITS ON CHARGES UNDER STATEMENTS OF WORK

13.1 Charges under a Statement of Work

The amount that can be charged under a Statement of Work shall be set out in the Statement of Work.

13.2 Charges on a Fixed Price Basis

If the Statement of Work specifies a charge on a Fixed Price basis, the Vendor shall not charge more than the Fixed Price, even if the Work requires additional time to complete that would otherwise have brought the cost to the Client to an amount in excess of the Fixed Price specified in the Statement of Work. Any amount charged in excess of the Fixed Price shall be deemed to be an overpayment.

The Client shall pay such portion of the Fixed Price in accordance with the payment schedule set out in the Statement of Work.

13.3 Charges on a Per Diem Rate Basis

If the Statement of Work specifies a charge on a Per Diem Rate basis, the following shall apply to that portion of the Statement of Work that is charged on a Per Diem Rate basis:

(a) *Charges for Services Performed During One Day* - The Vendor shall not be paid more than the applicable Per Diem Rate for Services performed by an individual in a Role on one calendar day.

The Vendor shall invoice the Client for the actual number of hours worked in one calendar day where the Services performed by the individual under a Statement of Work totals less than 7.25 hours in a Role for a calendar day. The Vendor shall invoice the Client for no more than the applicable Per Diem Rate where an individual in a Role has performed Services totalling 7.25 hours or more in one calendar day. For example, if an individual works 8 hours in a Role on one calendar day, the Vendor shall not be paid overtime for the time worked in excess of 7.25 hours. If an individual works less than 7.25 hours in a Role on a calendar day, the Vendor's

charge for the individual's Services in that Role on that calendar day shall be pro-rated against the applicable Per Diem Rate. For example, if an individual works 6 hours in a Role on one calendar day, the applicable Per Diem Rate shall be pro-rated by dividing it by 7.25 and multiplying it by 6. Any amount paid in excess of the pro-rated amount is deemed to be an overpayment.

(b) *Per Diem Rates and Experience Levels* - Under a Statement of Work, the Per Diem Rate for a Role shall not increase as a result of an individual gaining experience in performing that Role under that Statement of Work. In respect of a Statement of Work, the experience level of each individual shall be deemed to be fixed for the Assignment Term upon entering into the Statement of Work.

(c) *Separate Timesheet* - The Vendor shall maintain a timesheet for the Work performed on a Per Diem Rate basis that is separate from the timesheet for Work performed on a Fixed Price basis.

13.4 Travel, Meal and Accommodation Expenses

The Client is not responsible for any travel or accommodation expenses incurred by the Vendor that are not pre-approved in writing by the Client and charged in accordance with Management Board of Cabinet's Travel, Meal and Hospitality Expenses Directive, as may be amended or replaced from time to time. Accommodation arrangements may only be made with those facilities listed in the Ontario government's Accommodations Directory, as may be amended or replaced from time to time. The Vendor shall list travel and accommodation expenses as separate line items on its invoices, and shall support all such expenses with receipts.

The Client is not responsible for and the Vendor shall not charge for any meal, hospitality or incidental expenses incurred by the Vendor.

13.5 Maximum Prices

If the Statement of Work specifies a Maximum Price, the Vendor shall not invoice the Client for more than the applicable Maximum Price. Any amount paid in excess of a Maximum Price is deemed to be an overpayment.

13.6 Overpayments

The Vendor agrees to repay any overpayment immediately upon demand by the Client.

13.7 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 14. PAYMENT FOR PERFORMANCE

14.1 Payment Subject to Limits

Subject to Article 13 (Limits on Charges Under Statement of Work), the provisions of this Article, and the Vendor's compliance with the provisions of this Master Agreement and the Statement of Work, the Client shall pay the Vendor for Services and/or Deliverables provided as set out in the Statement of Work. Services and/or Deliverables may not be pre-paid.

14.2 Billing and Payment Process

Unless the Vendor and the Client expressly set out an alternative billing and payment process in the Statement of Work, the following process shall govern:

(a) the Vendor shall provide the Client with a billing statement in accordance with the payment schedule set out in the Statement of Work and that billing statement shall include:

(i) the reference number assigned to the Statement of Work by the Client;

(ii) a brief description of the Deliverables and Services provided for the period covered by the billing statement;

(iii) the amount payable under the Statement of Work, and the amount of applicable taxes (such as HST), if payable by the Client, identified as separate items;

(iv) a brief description of the event giving rise to the amount payable (such as, for example, identifying the particular milestone that was successfully completed); and

(v) any travel and accommodation expenses, identified as separate items, that are pre-approved in accordance with Section 13.4 (Travel, Meal and Accommodation Expenses) of the Master Agreement;

(b) if the Statement of Work also specifies particular charges on a Per Diem Rate basis, the Vendor shall also provide the Client with a monthly billing statement that applies to charges on a Per Diem Rate basis no later than ten (10) Business Days after the end of each month and that billing statement shall include:

(i) the reference number assigned to the Statement of Work by the Client;

(ii) a brief description of the Services provided on a Per Diem Rate basis for the relevant month;

(iii) the Per Diem Rate applicable to each Role, and the amount of applicable taxes (such as HST), if payable by the Client, identified as separate items;

(iv) the total billable time worked by each individual in each Role; and

(v) any travel and accommodation expenses, identified as separate items, that are pre-approved in accordance with Section 13.4 (Travel, Meal and Accommodation Expenses) of the Master Agreement;

(c) the Client shall approve or reject each billing statement within fifteen (15) Business Days of its receipt. If the Client rejects the billing statement, it shall so advise the Vendor promptly in writing and the Vendor shall provide additional information as required by the Client to substantiate the billing statement; and

(d) each billing statement is subject to approval of the Client before any payment is released. Payment shall be made within thirty (30) Business Days of such approval.

14.3 Certification of Acceptance

Payment of invoices under the Statement of Work is subject to acceptance in accordance with the process set out in Section 8.3 (Completion of Services) of this Master Agreement.

14.4 Holdback

If, in the opinion of the Client acting reasonably, the Vendor has failed to complete any Services, or deliver any Deliverables, by any applicable completion, delivery or milestone date set out in the Statement of Work (including any Change Order) or established by mutual agreement pursuant to the Statement of Work, the Client may hold back up to 15 percent of the Maximum Price for the Statement of Work until the Vendor completes such Services, or delivers such Deliverables, as the case may be. The holdback will be released no more than 45 calendar days after completion of such Services or delivery of such Deliverables, as the case may be. The Client may specify additional holdback rights in a Statement of Work.

14.5 No Expenses or Additional Charges

There shall be no other charges payable by the Client to the Vendor under any Statement of Work other than (a) the amount(s) expressly set out in the Statement of Work or Change Order, (b) the harmonized sales tax (HST) if the provision of Deliverables and Services is subject to it, and (c) any travel and accommodation expenses pre-approved in accordance with Section 13.4 (Travel, Meal and Accommodation Expenses).

14.6 Payment of Taxes and Duties

The Vendor shall pay or charge and remit, as required, all applicable taxes, including excise taxes incurred by or on the Vendor's behalf with respect to the Statement of Work.

14.7 Withholding Tax

The Client shall withhold any applicable withholding tax from amounts due and owing to the Vendor under the Statement of Work and shall remit it to the appropriate government in accordance with applicable tax laws.

14.8 Interest on Late Payment

In no event shall payment be in arrears prior to the expiry of 45 Business Days after delivery of an invoice that conforms to the requirements of the Statement of Work and the expiry of 45 Business Days after the date that the invoice is due and payable. If a payment is in arrears through no fault of the Vendor, the interest charged by the Vendor, if any, for any late payment is subject to required approvals under the Financial Administration Act, R.S.O. c. F-12 and shall not exceed the pre-judgment interest rate established under subsection 127(2) of the Courts of Justice Act, R.S.O. 1990, C45, in effect on the date that the payment went into arrears.

14.9 Document Retention and Audit

During and for seven (7) years after the Term of each Statement of Work, the Vendor shall, at its cost (a) maintain all necessary records to substantiate (i) all charges and payments under each Statement of Work and (ii) that the Services were provided in accordance with each Statement of Work and with Requirements of Law; and (b) permit and assist MGS and each Client in conducting audits of the operations of the Vendor to verify (i) and (ii) above. MGS or a Client shall provide the Vendor with at least ten (10) Business Days prior notice of its requirement for such audit.

14.10 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 15. INTELLECTUAL PROPERTY OWNERSHIP AND LICENSING

15.1 General

Attachment D (Vendor/Client Ownership Provisions) or Attachment E (Client Ownership Provisions), but not both, shall apply to each Statement of Work. If the Statement of Work specifies that Attachment D applies to the Statement of Work, then Attachment E does not apply to the Statement of Work. If the Statement of Work specifies that Attachment E applies to the Statement of Work, then Attachment D does not apply to the Statement of Work.

15.2 Default Vendor Ownership Model

If the Statement of Work is silent about whether Attachment D (Vendor/Client Ownership Provisions) or Attachment E (Client Ownership Provisions) applies to it, then the provisions of Attachment D (Vendor/Client Ownership Provisions) shall apply to the Statement of Work.

[See Attachment D (Vendor/Client Ownership Provisions) and Attachment E (Client Ownership Provisions) for Article 16 to Article 25]

ARTICLE 26 OPS CONFIDENTIAL INFORMATION

26.1 Confidentiality

During and following the Term of this Master Agreement and the Project Term of each Statement of Work, the Vendor shall keep all OPS Confidential Information confidential. The Vendor shall keep all OPS Confidential Information secure and shall provide or return OPS Confidential Information to the Client on demand and, in any event, shall provide or return all OPS Confidential Information to the Client before the termination or expiry of the Statement of Work, with no copy or portion kept by the Vendor in any form or on any media. The Vendor shall limit the disclosure of OPS Confidential Information to only those of its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors who have been specifically authorized to have such disclosure and who have a need to know it in order to respond to a request for service pursuant to this Master Agreement or to perform the Services under the Statement of Work. The Vendor agrees that the Vendor, its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors shall not directly or indirectly disclose, destroy, exploit or use any OPS Confidential Information (except in order to respond to a request for services pursuant to this Master Agreement or to perform the Services, or except if required by order of a court or tribunal), without first obtaining:

(a) the written consent of the Client, and

(b) in respect of any OPS Confidential Information about any third party, the written consent of such third party.

26.2 Restrictions on Copying

The Vendor shall not copy any OPS Confidential Information, in whole or in part, unless necessary or materially advantageous for the performance of the Services. On each copy made by the Vendor, the Vendor must reproduce all notices which appear on the original.

26.3 Injunctive and Other Relief

The Vendor acknowledges that breach of any provisions of this Article may cause irreparable harm to Ontario, the OPS Entity or any third party to whom Ontario or the OPS Entity owes a duty of confidence, and that the injury to Ontario, the OPS Entity or any third party, may be difficult to calculate and inadequately compensable in damages. The Vendor agrees that Ontario and the OPS Entity and any third party to whom Ontario or the OPS Entity owes a duty of confidence are each entitled to obtain injunctive relief (without proving any damage sustained by it or by any third party) and any other remedy for any actual or potential breach of the provisions of this Article.

26.4 Notice and Protective Order

If the Vendor or any of its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors become legally compelled to disclose any OPS Confidential Information, the Vendor will provide Ontario or the OPS Entity, as appropriate, with prompt notice to that effect to allow Ontario or the OPS Entity to seek one or more protective orders or other appropriate remedies to prevent or limit such disclosure, and it shall co-operate with Ontario and/or the OPS Entity and their respective legal counsel to the fullest extent. If such protective orders or other remedies are not obtained, the Vendor will disclose only that portion of OPS Confidential Information which the Vendor is legally compelled to disclose, only to such person or persons to which the Vendor is legally compelled to disclose, and the Vendor shall provide notice to each such recipient, in co-operation with legal counsel for Ontario and/or the OPS Entity, that such OPS Confidential Information is confidential and subject to non-disclosure on terms and conditions substantially similar to and not materially less protective than those in this Master Agreement, and not materially less protective than any more protective terms and conditions set out the Statement of Work, and, if possible, shall obtain each recipient's written agreement to receive and use such OPS Confidential Information subject to those terms and conditions.

26.5 Vendor's Directors, Officers, Personnel, Agents, Partners, Affiliates, Volunteers and Subcontractors

The Vendor shall advise its directors, officers, Personnel, agents, partners, affiliates, volunteers and Subcontractors of the requirements of this Article and take appropriate action to ensure their compliance with its terms. In addition to any other liabilities of the Vendor pursuant to this Master Agreement or the Statement of Work or otherwise at law or in equity, the Vendor shall be liable for any and all liability, losses, costs, damages, expenses (including all reasonable legal, expert and consultant fees, and reasonable disbursements), causes of action, and Proceedings arising from any non-compliance with this Article by the Vendor's directors, officers, Personnel, agents, partners, affiliates, volunteers and Subcontractors. The Vendor understands and agrees that, prior to allowing any of them to perform any Services under a Statement of Work, the Vendor shall cause its directors, officers, Personnel, agents, partners, affiliates, volunteers and Subcontractors to execute a confidentiality agreement in the form set out in Attachment H and the Vendor shall deliver it to the Client.

26.6 Conflict with Privacy Provisions

If a conflict or inconsistency arises between any provision in this Article and the Privacy Provisions, the Privacy Provisions shall govern.

26.7 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 27 PRIVACY

27.1 Default Privacy Provisions

FIPPA applies to and governs all Records and may require the disclosure of such Records to third parties.

Unless the Parties expressly set out alternative privacy provisions in the Statement of Work, the following provisions shall govern:

The Vendor agrees:

(a) to keep Records secure;

(b) to provide Records to Ontario or the OPS Entities within seven (7) calendar days of being directed to do so by Ontario or the OPS Entity for any reason including an access request or privacy issue;

(c) not to access any Personal Information unless Ontario or the OPS Entity determines, in its sole discretion, that access is permitted under FIPPA and is necessary in order to provide the Services;

(d) not to directly or indirectly use, collect, disclose or destroy any Personal Information for any purposes that are not authorized by Ontario or the OPS Entity;

(e) to ensure the security and integrity of Personal Information and keep it in a physically secure and separate location safe from loss, alteration, destruction or intermingling with other records and databases and to implement, use and maintain the most appropriate products, tools, measures and procedures to do so;

(f) to restrict access to Personal Information to those of its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors who have a need to know it for the purpose of providing the Services and who have been specifically authorized by the MGS Representative or the Client Representative to have such access for the purpose of providing the Services;

(g) to implement other specific security measures that in the reasonable opinion of Ontario or the OPS Entity would improve the adequacy and effectiveness of the Vendor's measures to ensure the security and integrity of Personal Information and Records generally;

(h) that any confidential information supplied to Ontario or the OPS Entity may be disclosed by Ontario or the OPS Entity where it is obligated to do so under FIPPA, by an order of a court or tribunal or pursuant to a legal proceeding; and

(i) any provision set out above that is not expressly replaced in a Statement of Work with an alternative provision shall remain in full force and effect.

27.2 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 28 CONFIDENTIAL VENDOR INFORMATION

28.1 Confidentiality

(a) Confidentiality - Master Agreement - During and following the Term of this Master Agreement, Ontario shall keep confidential all Confidential Vendor Information that comes into the knowledge or possession of Ontario under this Master Agreement, subject to: (i) the Privacy Provisions; and (ii) any right of Ontario under this Master Agreement to disclose. Ontario agrees to limit the disclosure of Confidential Vendor Information which comes into the knowledge or possession of Ontario under this Master Agreement to only: (1) those of its advisors, personnel and subcontractors, (2) those OPS Entities, offices of officers of the Legislative Assembly or of the Ontario Legislature, and Provincially Funded Organizations, and their respective advisors, staff and subcontractors, and (3) those members of the Executive Council of Ontario, and their advisors, staff and subcontractors; who have a need to know it and who have been specifically authorized to have such disclosure. Ontario agrees that: (A) it and its advisors, personnel and subcontractors, (B) those OPS Entities, offices of officers of the Legislative Assembly or of the Ontario Legislature, and Provincially Funded Organizations, and their respective advisors, staff and subcontractors; and (C) those members of the Executive Council of Ontario, and their advisors, staff and subcontractors; shall not directly or indirectly disclose, destroy, exploit or use any Confidential Vendor Information (except to enable Ontario to exercise its rights under this Master Agreement or any Statement of Work, or except if required by order of a court or tribunal), without first obtaining:

(i) the written consent of the Vendor, and

(ii) in respect of any Confidential Vendor Information about any third party, the written consent of such third party.

(b) Confidentiality - Request for Services - In connection with a request for services issued pursuant to this Master Agreement, the Issuer shall keep confidential, in accordance with the terms and conditions of the request for services, all Confidential Vendor Information that comes into the knowledge, possession or control of the Issuer or any contractor or subcontractor at any tier of the Issuer.

(c) Confidentiality - Statements of Work – During and following the Term of each Statement of Work entered into by the Client, the Client shall keep confidential all Confidential Vendor Information that comes into the knowledge, possession or control of the Client or its Subcontractors in connection with the Statement of Work, subject to: (i) the Privacy Provision; or (ii) any right of the Client under the Statement of Work, to disclose. The Client agrees to limit the disclosure of Confidential Vendor Information which comes into the knowledge or possession of the Client in connection with the Statement of Work to only: (1) those of its

advisors, personnel and subcontractors, (2) Ontario and those of its advisors, personnel and subcontractors; (3) those OPS Entities, offices of officers of the Legislative Assembly or of the Ontario Legislature, and Provincially Funded Organizations, and their respective advisors, staff and subcontractors, and (4) those members of the Executive Council of Ontario, and their advisors, staff and subcontractors; who have a need to know it and who have been specifically authorized to have such disclosure. The Client agrees that: (A) it and its advisors, personnel and subcontractors, (B) Ontario and those of its advisors, personnel and subcontractors; (C) those OPS Entities, offices of officers of the Legislative Assembly or of the Ontario Legislature, and Provincially Funded Organizations, and their respective advisors, staff and subcontractors; and (D) those members of the Executive Council of Ontario, and their advisors, staff and subcontractors; shall not directly or indirectly disclose, destroy, exploit or use any Confidential Vendor Information (except to enable the Client to exercise its rights under this Master Agreement or any Statement of Work, or except if required by order of a court or tribunal), without first obtaining:

(i) the written consent of the Vendor, and

(ii) in respect of any Confidential Vendor Information about any third party, the written consent of such third party.

For certainty and without limiting the exclusion of the Statement of Work itself as part of the definition of "Confidential Vendor Information", the Statement of Work is not considered the confidential or proprietary information of the Vendor and it and its contents may be publicly disclosed without notice and without the prior consent of the Vendor.

(d) Limitation - Despite anything to the contrary in this Master Agreement, the Vendor and Ontario agree that: (i) Ontario shall have no obligation to control, and no liability to the Vendor for failure to control, any Confidential Vendor Information that is received by, or is in the knowledge, possession or control of, any OPS Entity, or any contractor or subcontractor at any tier of any OPS Entity: (A) in connection with any request for service issued by any OPS Entity; or (B) under any Statement of Work; and (ii) for certainty, Ontario shall have no obligation or liability to the Vendor for any breach of this Article 28 (Confidential Vendor Information) to the extent that Ontario does not have knowledge or possession of the relevant Confidential Vendor Information prior to the breach.

28.2 Restrictions on Copying

(a) Restrictions on Copying - Master Agreement - Ontario shall not copy, in whole or in part, any Confidential Vendor Information that comes into the knowledge or possession of Ontario under this Master Agreement, unless necessary or materially advantageous to enable Ontario to exercise its rights under this Master Agreement. On each copy made by Ontario, Ontario must reproduce all notices which appear on the original.

(b) Restrictions on Copying – Request for Services Process - In connection with a request for services issued pursuant to this Master Agreement, the Issuer shall not copy, in whole or in part, any Confidential Vendor Information that comes into the knowledge, possession or control of the Issuer unless necessary or materially advantageous to enable the Issuer to exercise its rights in accordance with the terms and conditions of the request for services. On each copy made by the Issuer, the Issuer must reproduce all notices which appear on the original.

(c) Restrictions on Copying - Statements of Work - The Client shall not copy, in whole or in part, any Confidential Vendor Information that comes into the knowledge, possession or control of the Client in connection with any Statement of Work entered into by the Client unless necessary or materially advantageous to enable the Client to exercise its rights under any Statement of Work entered into by the Client. On each copy made by the Client, the Client must reproduce all notices which appear on the original.

28.3 Declaratory Order and Other Relief

Ontario acknowledges, and it is a term of each Statement of Work that the Client acknowledges, that breach of any provisions of this Article may cause irreparable harm to the Vendor or to any third party to whom the Vendor owes a duty of confidence, and that the injury to the Vendor or to any third party may be difficult to calculate and inadequately compensable in damages. Ontario agrees, and it is a term of each Statement of Work that the Client agrees, that the Vendor is entitled to obtain an order declaratory of the rights of the Parties (without proving any damage sustained by it or by any third party) or any other remedy available at law against any actual or potential breach of the provisions of this Article.

28.4 Conflict with Privacy Provisions

If a conflict or an inconsistency arises between any provision in this Article and the Privacy Provisions, the Privacy Provisions shall govern.

28.5 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 29 REPRESENTATIONS, WARRANTIES AND COVENANTS AS TO THIS MASTER AGREEMENT

29.1 Representations and Warranties of the Vendor

The Vendor makes the following representations and warranties to Ontario as of the date of execution of this Master Agreement, and acknowledges that Ontario is relying upon them:

(a) the Vendor is duly incorporated, or, if a partnership, formed, and validly subsisting under the laws of its governing jurisdiction with full power, right and authority to enter into this Master Agreement, and to perform its obligations under this Master Agreement;

(b) the individual executing this Master Agreement on behalf of the Vendor is duly authorized to do so;

(c) this Master Agreement constitutes a legal, valid and binding agreement of the Vendor enforceable in accordance with its terms;

(d) there is no agreement with any other Person which would in any way interfere with the rights of Ontario under this Master Agreement; and

(e) to the extent that any right, title or interest in or to any Deliverables or Intellectual Property Rights vests in Ontario, upon such vesting all such rights, title and interest will be transferred to Ontario free and clear of any Encumbrances.

Throughout the Term of this Master Agreement, the Vendor covenants to take any actions required to ensure that the foregoing representations and warranties continue to be true and covenants not to take any actions that would cause any of the foregoing representations and warranties not to be true, and acknowledges that Ontario and OPS Entities are relying upon such covenants.

29.2 Representations and Warranties of Ontario

Ontario makes the following representations and warranties to the Vendor as of the date of execution of this Master Agreement, and acknowledges that the Vendor is relying upon them:

(a) the execution and delivery of this Master Agreement has been duly authorized; and

(b) this Master Agreement constitutes a legal, valid and binding agreement of Ontario enforceable in accordance with its terms.

29.3 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work

ARTICLE 30 REPRESENTATIONS, WARRANTIES AND COVENANTS AS TO STATEMENTS OF WORK

30.1 Representations and Warranties of the Vendor

In addition to any representations and warranties of the Vendor made under a Statement of Work, the Vendor makes the following representations and warranties to the Client as of the date of execution of each Statement of Work, and acknowledges that the Client is relying upon them:

(a) the Vendor is duly incorporated or, if a partnership, formed, and validly subsisting under the laws of its governing jurisdiction with full power, right and authority to enter into the Statement of Work, and to perform its obligations under the Statement of Work;

(b) the execution, delivery and performance of the Statement of Work by the Vendor have been duly authorized;

(c) the Statement of Work constitutes a legal, valid and binding agreement of the Vendor enforceable in accordance with its terms;

(d) there is no agreement with any other Person which would in any way interfere with the rights of the Client (and, in the case of a Client that is an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies, also the rights of Ontario) under the Statement of Work;

(e) all Services will be performed: (i) in a professional and competent manner by persons qualified and skilled in their occupations; and (ii) in accordance with, and not in violation of, Requirements of Law;

(f) the Vendor:

(i) has entered into a written agreement, or will have entered into a written agreement prior to the performance of any Services under the Statement of Work, with each of its employees performing Services under the Statement of Work, or has established and published employee policies binding on its employees performing Services under the Statement of Work; or

(ii) has entered into a written agreement, or will enter into a written agreement prior to the performance of any Services under the Statement of Work, with each of its Subcontractors performing Services under the Statement of Work;

which contains the following minimum terms: (1) the employee or Subcontractor, as applicable, irrevocably assigns to the Vendor, to the extent necessary for the Vendor to grant, assign, transfer or otherwise convey to the Client the rights, title or interests in and to the Deliverables in accordance with the terms of this Master Agreement and the Statement of Work, all of its Intellectual Property Rights to work created, developed, generated, prepared or produced in the course of employment or performing its obligations under a contract with the Vendor, as applicable; (2) the employee or Subcontractor, as applicable, irrevocably waives its Moral Rights in favour of the Vendor and the Vendor's assignees in and to any work created by the employee or Subcontractor in the course of employment or performing its obligations under a contract with the Vendor, as applicable; (3) terms and conditions that protect the confidentiality

of the Vendor's confidential information, including any confidential information of the Vendor's customers, on terms that are no less protective as the confidentiality obligations set out in this Master Agreement; and (4) the employee or Subcontractor agrees to promptly do any and all acts and cause to be executed and deliver to the Vendor any and all assignments, documents and instruments relating to the Deliverables, which the Vendor may request at any time or from time to time;

(g) the Vendor has not entered into any arrangement which would in any way restrict the Client's ability (and, in the case of a Client that is an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies, also Ontario's ability) to exercise the Intellectual Property Rights granted under the Statement of Work;

(h) there are no claims made or Proceedings pending or anticipated relating to the ownership of the Deliverables or any part of the Deliverables;

(i) the Vendor has, or shall obtain, all the rights for it to grant all of the rights and licences that it grants under the Statement of Work;

(j) neither the Deliverables nor the Services shall, to the best of Vendor's knowledge, in any way infringe or violate any Intellectual Property Rights or any other right of any third party including any patents or patent applications;

(k) the right, title or interest in or to any Deliverables or any Intellectual Property Rights that vests in the Client (but, in the case of a Client that is an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies, that vest in Ontario) in accordance with the terms of this Master Agreement and/or the Statement of Work will, upon such vesting, be transferred to the Client (but, in the case of a Client is an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies, be transferred to Ontario), free and clear of any Encumbrances;

(l) the Vendor has not entered into any agreement or arrangement that would restrict a Subcontractor from licensing or selling to the Client (and, in the case of a Client that is an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies, also licensing and selling to Ontario) goods or services relating to the Deliverables on the usual commercial basis and at market prices, for the purpose of installing, integrating, operating, using, maintaining, supporting, developing or modifying any of the Deliverables;

(m) the Vendor shall not provide or incorporate (or permit those for whom it is responsible, including its Subcontractors and Personnel to provide or incorporate) into any Deliverables, or request the Client to consent to the Vendor providing or incorporating into any Deliverables, and shall not use or permit the use in the provision of the Services, any Restrictive Material; and

(n) the media containing any Deliverables shall be new and free from defects in manufacture, materials, and design, and shall function properly under ordinary use for 90 days after receipt.

Throughout the Project Term of each Statement of Work, the Vendor covenants to take any actions required to ensure that the foregoing representations and warranties continue to be true and covenants not to take any actions that would cause any of the foregoing representations and warranties not to be true, and acknowledges that the Client is relying upon such covenants.

30.2 Representations and Warranties of the Client

It is a term of each Statement of Work that the Client makes the following representations and warranties to the Vendor as of the date of execution of each Statement of Work, and acknowledges that the Vendor is relying upon them:

(a) the execution and delivery of the Statement of Work has been duly authorized; and

(b) the Statement of Work constitutes a legal, valid and binding agreement of the Client enforceable in accordance with its terms.

30.3 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work

ARTICLE 31 INDEMNIFICATION

31.1 IP Indemnification

Despite the limitations of liability set out in Article 33 (Limitation of Liability), and except for any liability arising pursuant to the indemnity provided for in Section 31.3 (Confidentiality and Privacy Indemnification), the Vendor shall indemnify and hold harmless the Indemnified Parties from and against all Losses and Proceedings, by whomever made, sustained, incurred, brought or prosecuted, for any actual or possible infringement, inducement of infringement, misappropriation or violation of any Intellectual Property Rights or infringement of any Moral Rights arising out of or in connection with:

(a) the Deliverables (including the provision, use or disposal of the Deliverables) or the Services (including the provision or performance of the Services);

(b) the failure of the Vendor, its Subcontractors or the Vendor's Personnel to perform the Vendor's obligations pursuant to Section 18.4 (Waiver of Moral Rights); or

(c) the exercise of any rights, licences or permissions under a Statement of Work by any Indemnified Parties or by any persons authorized in or under the Statement of Work to exercise any such rights, licences or permissions.

If anything in subsection (a) or (c) above or resulting from the failure described in subsection (b) above is held, or is likely, in the reasonable opinion of the Client, to be held to constitute an infringement, inducement of infringement, misappropriation or violation of any Intellectual Property Rights or an infringement of any Moral Rights, or anything in subsection (a) or (c) above or resulting from the failure described in subsection (b) above is enjoined or threatened to be enjoined or held or threatened to be held improper by way of declaration, then without prejudice to any other rights and remedies as may be available to any of the Indemnified Parties under this Master Agreement or Statement of Work, or at law or in equity, the Vendor shall also, at its expense, either:

(1) obtain the rights, licences, permissions and waivers as are necessary so that such Deliverables, Services, or exercise of rights, licences or permissions, becomes non-infringing; or

(2) replace or modify the Deliverables or the Services so that the infringing portion no longer infringes (without any loss of quality or functionality) to the Client's satisfaction;

and shall make every reasonable effort to correct the situation with minimal effect upon the operations of the Client. If neither of the foregoing alternatives is reasonably available, the Minister (MGS) may terminate this Master Agreement and the Minister (Client) may terminate all or any part of the Statement of Work without further obligation or liability to the Vendor and, without prejudice to any other rights and remedies as may be available to any of the Indemnified Parties under this Master Agreement or the Statement of Work, or at law or in equity, the Vendor shall refund to the Client all amounts paid with respect to such Services or anything supplied that infringes.

31.2 Client Modification

With respect to a Statement of Work, the Vendor shall not have any liability to the Indemnified Parties under Section 31.1 (IP Indemnification) to the extent that any infringement or violation of any Intellectual Property Rights, other than Moral Rights, is caused by further development or modification made by the Client not

authorized by the Vendor to the Newly-Created Materials, Vendor Materials incorporated into any Deliverables, Vendor Work Inventions or Vendor Work Information.

31.3 Confidentiality and Privacy Indemnification

Despite the limitations of liability set out in Article 33 (Limitation of Liability), the Vendor shall indemnify and hold harmless the Indemnified Parties from and against all Losses and Proceedings, by whomever made, sustained, incurred, brought or prosecuted arising out of or in connection with a breach by the Vendor of: (a) its obligations under Article 26 (OPS Confidential Information); or (b) the Privacy Provisions.

31.4 Other Indemnification

Except for any liability arising pursuant to the indemnities provided for in Section 21.3 (Indemnity) (if Attachment E applies to the Statement of Work), 23.3 (Indemnity) (if Attachment D applies to the Statement of Work), 31.1 (IP Indemnification) or 31.3 (Confidentiality and Privacy Indemnification) and subject to the limitation of liability set out in Article 33 (Limitation of Liability), the Vendor shall indemnify and hold harmless the Indemnified Parties from and against all Losses and by whomever made, sustained, brought or prosecuted, arising out of or in connection with anything done or omitted to be done by the Vendor, its Subcontractors or the Vendor's Personnel in the course of the performance of the Vendor's obligations under this Master Agreement or the Statement of Work or otherwise in connection with this Master Agreement or the Statement of Work.

31.5 Notice

The Client shall notify the Vendor in writing of the commencement of any Proceeding referred to in Section 21.3 (Indemnity) (if Attachment E applies to the Statement of Work), 23.3 (Indemnity) (if Attachment D applies to the Statement of Work), 31.1 (IP Indemnification), 31.3 (Confidentiality and Privacy Indemnification), or 31.4 (Other Indemnification).

31.6 Defence

The Vendor shall, at its expense, to the extent requested by the Attorney General of Ontario, participate in or conduct the defence of any Proceedings against any Indemnified Parties referred to in Section 21.3 (Indemnity) (if Attachment E applies to the Statement of Work), 23.3 (Indemnity) (if Attachment D applies to the Statement of Work), 31.1 (IP Indemnification), 31.3 (Confidentiality and Privacy Indemnification), or 31.4 (Other Indemnification), and any negotiations for their settlement. Ontario may elect to participate in or conduct the defence of any such Proceedings by notifying the Vendor in writing of such election without prejudice to any other rights or remedies of Ontario under this Master Agreement or the Statement of Work, at law or in equity. Each party participating in the defence shall do so by actively participating with the other's counsel. No settlement shall be entered into by the Vendor unless it has obtained the prior written approval of the Attorney General of Ontario.

If the Vendor is requested by the Attorney General of Ontario to participate in or conduct the defence of any such Proceedings, Ontario agrees to co-operate with and assist the Vendor to the fullest extent possible in the Proceedings and any related settlement negotiations. If Ontario conducts the defence of any such Proceedings, the Vendor agrees to co-operate with and assist Ontario to the fullest extent possible in the Proceedings and any related settlement negotiations.

Subject to any rights and obligations of the Attorney General of Ontario, any Statement of Work that is entered into by a Client that is an OPS Entity may specify obligations that are the same as or similar to those set out above in this Section 31.6, in respect of the defence of any Proceedings against the Client and its officers, directors, advisors, agents, appointees and employees. If a Statement of Work of that kind is silent, the provisions of this Section shall apply to it, except that – and subject to any rights and obligations of the Attorney General of Ontario – "Attorney General of Ontario" shall be replaced by "Client", and "Ontario" shall be replaced by "the Client".

31.7 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 32 INSURANCE

32.1 General

Without limiting any other provision in this Article, the Vendor shall, at its own expense, put in effect with insurers having a secure A.M. Best rating of B+ or greater, or the equivalent, all the necessary and appropriate insurance that a prudent business person would acquire in like circumstances. The Vendor shall maintain such insurance throughout the Term of this Master Agreement and if the Project Term of a Statement of Work extends beyond this Master Agreement Expiry Date, until the Project End Date.

32.2 Commercial General Liability Insurance

The insurance required by Section 32.1 (General) shall include commercial general liability insurance on an occurrence basis to an inclusive limit not less than two million Canadian dollars (C$2,000,000.00) per occurrence of property damage, bodily injury (including death) or personal injury, and which provides the following minimum coverage:

(a) the Indemnified Parties as additional insureds with respect to any liability arising in the course of the performance of the Vendor's obligations under this Master Agreement and each Statement of Work or arising otherwise in connection with this Master Agreement or any Statement of Work;

(b) cross liability;

(c) a contractual liability coverage endorsement;

(d) a products and completed operations endorsement;

(e) a non-owned automobile coverage with blanket contractual endorsement;

(f) an employer's liability coverage endorsement, if the Vendor is not subject to the WSIA; and

(g) 30 days written notice to Ontario of cancellation, material change or termination.

Additional required coverage or endorsements may be set out in a Statement of Work for that Statement of Work.

32.3 Errors and Omissions Liability Insurance

The insurance required by Section 32.1 (General) shall include errors and omissions liability insurance, insuring liability for errors and omissions in the provision of the Deliverables and/or the performance of or failure to perform the Services, in the amount of not less than two million Canadian dollars (C$2,000,000.00) per claim and in the annual aggregate.

Additional required coverage may be set out in a Statement of Work for that Statement of Work.

32.4 Proof of Insurance

Before the Vendor signs the first Statement of Work under this Master Agreement, the Vendor shall provide to the MGS Representative proof of the insurance required by Sections 32.2 (Commercial General Liability Insurance) and 32.3 (Errors and Omissions Liability Insurance) in the form of valid certificates of insurance that reference this Master Agreement and confirm the coverage set out in this Article. The Vendor shall provide

renewal replacements to the MGS Representative on or before any subsequent policy renewals. Each certificate of insurance and renewal replacement must reference this Master Agreement by name, date and the full legal name of the Parties. Upon the request of the MGS Representative, a copy of each policy shall be made available to the MGS Representative.

32.5 Subcontractors

The Vendor shall ensure that each of its Subcontractors obtains all the necessary and appropriate insurance that a prudent person in the business of the Subcontractor would maintain and that the Indemnified Parties are named as additional insured with respect to any liability arising in the course of performance of the Subcontractor's obligations under the subcontract for the provision of the Deliverables.

32.6 Proof of WSIA Coverage

If the Vendor is subject to the WSIA, it shall submit a valid WSIB clearance certificate of WSIA coverage to the MGS Representative before the Vendor signs the first Statement of Work under this Master Agreement. In addition, the Vendor shall, from time to time at the request of the MGS Representative, provide additional WSIB clearance certificates. The Vendor covenants and agrees to pay when due, and to ensure that each of its Subcontractors pays when due, all amounts required to be paid by it and by its Subcontractors, from time to time during the Term of this Master Agreement and the Project Term of each Statement of Work, under the WSIA, failing which the Client shall have the right, in addition to and not in substitution for any other right it may have pursuant to the Statement of Work or otherwise at law or in equity, to pay to the WSIB any amount due pursuant to the WSIA and unpaid by the Vendor or its Subcontractors and to deduct such amount from any amount due and owing from time to time to the Vendor pursuant to the Statement of Work together with all costs incurred by the Client in connection therewith.

ARTICLE 33 LIMITATION OF LIABILITY

33.1 Categories of Damages

For the purposes of this Article, direct damages are those damages that fall within the scope of subsection (a) or (b) below, or both:

(a) damages that arise naturally from the breach of the Master Agreement or a Statement of Work or that are reasonably contemplated at the time the Parties enter into this Master Agreement or the Statement of Work as being the probable consequences of breach of this Master Agreement or the Statement of Work, but exclude those damages that, in order to be reasonably contemplated, require knowledge of special circumstances, which are not known to both Parties at the time the Parties enter into this Master Agreement or the Statement of Work;

(b) damages that are reasonably foreseeable as being the probable consequences of a tort that falls within the scope of this Master Agreement or a Statement of Work, subject to any express limitation or negation of the tort duty, or of the right to sue in tort, set out in this Master Agreement or the Statement of Work.

For the purposes of this Article, all damages of any type whatsoever that fall within the scope of this Master Agreement or the Statement of Work, which are not direct damages, are categorized as indirect damages.

33.2 Vendor's Liability for Damages

Subject to Section 33.3 (Vendor's Liability for Property Damage, Bodily Injury (Including Death) or Personal Injury) and Section 33.4 (Exception – Vendor Liability) for which there are no limits on the liability of the Vendor, if circumstances arise where Ontario or the OPS Entity is entitled to recover from the Vendor damages arising in the course of the performance of the Vendor's obligations under a Statement of Work or arising otherwise in connection with the Statement of Work, the Vendor's aggregate liability to Ontario and the OPS Entity for direct damages under the Statement of Work, shall not exceed:

(a) $250,000.00, if the Maximum Price in the Statement of Work is $250,000.00 or less (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $250,000.00 or less); or

(b) $750,000.00, if the Maximum Price in the Statement of Work is $750,000.00 or less but more than $250,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $750,000.00 or less but more than $250,000.00); or

(c) $2,000,000.00, if the Maximum Price in the Statement of Work is $2,000,000.00 or less but more than $750,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $2,000,000.00 or less but more than $750,000.00); or

(d) $5,000,000.00, if the Maximum Price in the Statement of Work is $5,000,000.00 or less but more than $2,000,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $5,000,000.00 or less, but more than $2,000,000.00); or

(e) the greater of the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work, if the Maximum Price in the Statement of Work exceeds $5,000,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work exceeds $5,000,000.00).

Subject to Section 33.3 (Vendor's Liability for Property Damage, Bodily Injury (Including Death) or Personal Injury) and Section 33.4 (Exception (Vendor Liability)), the Vendor shall have no liability for indirect damages in respect of the Statement of Work. The Statement of Work may expressly provide that this limitation shall not in any way restrict or limit any indemnities set out in the Statement of Work.

33.3 Vendor's Liability for Property Damage, Bodily Injury (including Death) or Personal Injury

The limitation of liability in Section 33.2 (Vendor's Liability for Damages) shall not apply in respect of damages for any property damage, bodily injury (including death) or personal injury.

33.4 Exception (Vendor Liability)

The limitation of liability in Section 33.2 (Vendor's Liability for Damages) shall not apply where Ontario or the OPS Entity would be entitled to recover from the Vendor under (a) Sections 21.3 (Indemnity) (if Attachment E applies to the Statement of Work), 23.3 (if Attachment D applies to the Statement of Work), 31.1 (IP Indemnification), and 31.3 (Confidentiality and Privacy Indemnification) or any express exceptions in this Master Agreement to Section 33.2 (Vendor's Liability for Damages); (b) any indemnity in the Statement of Work for breach or misappropriation of Intellectual Property Rights, breach of confidentiality or breach of privacy provisions; or (c) any indemnity in the Statement of Work where the Statement of Work expressly provides that the indemnity is not subject to, restricted by or limited by any limitation of liability.

33.5 Ontario and OPS Entities' Liability for Damages

Subject to Section 33.6 (Ontario and OPS Entities' Liability for Property Damage, Bodily Injury (including Death) or Personal Injury) and Section 33.7 (Exception (Ontario and OPS Entities' Liability)) for which there are no limits on the liability of Ontario and the OPS Entity, if circumstances arise where the Vendor is entitled to recover damages from Ontario or the OPS Entity in connection with a Statement of Work, the aggregate liability of Ontario and the OPS Entity to the Vendor for direct damages under the Statement of Work shall not exceed:

(a) $250,000.00, if the Maximum Price in the Statement of Work is $250,000.00 or less (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may

charge the Client or the Client must pay the Vendor under the Statement of Work is $250,000.00 or less); or

(b) $750,000.00, if the Maximum Price in the Statement of Work is $750,000.00 or less but more than $250,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $750,000.00 or less, but more than $250,000.00); or

(c) $2,000,000.00, if the Maximum Price in the Statement of Work is $2,000,000.00 or less but more than $750,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $2,000,000.00 or less, but more than $750,000.00); or

(d) $5,000,000.00, if the Maximum Price in the Statement of Work is $5,000,000.00 or less but more than $2,000,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work is $5,000,000.00 or less, but more than $2,000,000.00); or

(e) the greater of the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work, if the Maximum Price in the Statement of Work exceeds $5,000,000.00 (or if the Maximum Price is not specified in the Statement of Work but the amount the Vendor may charge the Client or the Client must pay the Vendor under the Statement of Work exceeds $5,000,000.00).

Subject to Section 33.6 (Ontario and OPS Entities' Liability for Property Damage, Bodily Injury (Including Death) or Personal Injury) and Section 33.7 (Exception (Ontario and OPS Entities' Liability)), Ontario and the OPS Entity shall have no liability for indirect damages in respect of the Statement of Work.

33.6 Ontario and OPS Entities' Liability for Property Damage, Bodily Injury (including Death) or Personal Injury

The limitation of liability in Section 33.5 (Ontario and OPS Entities' Liability for Damages) shall not apply in respect of damages for any property damage, bodily injury (including death) or personal injury.

33.7 Exception (Ontario and OPS Entities' Liability)

The limitation of liability in Section 33.5 (Ontario and OPS Entities' Liability for Damages) shall not apply where the Vendor is entitled to recover damages from Ontario or the OPS Entity (a) arising from use, infringement, inducement of infringement or violation of any Intellectual Property Rights or infringement of any Moral Rights in connection with the Statement of Work; or (b) based upon, occasioned by or attributable to breach of Article 28 (Confidential Vendor Information) in connection with the Statement of Work.

33.8 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 34 SUSPENSION

34.1 Suspension

The Minister (MGS), at its discretion, acting reasonably, may temporarily remove the Vendor immediately from the list of qualified vendors of record to which the Vendor was added pursuant to the RFP. For certainty and without limiting the generality of the foregoing, the Minister (MGS) may temporarily remove the Vendor from the list of qualified vendors of record immediately upon the occurrence of the following circumstances:

(a) the Vendor fails to comply with any of the terms of this Master Agreement or of any Statement of Work;

(b) the Vendor is in default under Article 10 (Security Clearance Checks);

(c) any Insolvency Event occurs with respect to the Vendor;

(d) the Vendor breaches any provision in Article 26 (OPS Confidential Information) or any Privacy Provisions;

(e) the Vendor breaches Section 5.6 (Conflict of Interest) or any other conflict of interest provisions applicable to this Master Agreement or any Statement of Work;

(f) the Vendor subcontracts for the provision of part or all of the Services or sells, assigns or transfers its interest in this Master Agreement, a Statement of Work, or any of its obligations under them to any third Person without the prior written approval of the Minister (MGS) or the Minister (Client), as appropriate, except as expressly contemplated and permitted by Section 5.3 (Subcontracting or Assignment);

(g) the Vendor, prior to or after executing this Master Agreement or any Statement of Work, makes a material misrepresentation or omission or provides materially inaccurate information to Ontario or the OPS Entity;

(h) the Vendor undergoes a change in control which, in the sole opinion of Ontario, adversely affects the Vendor's ability to satisfy some or all of its obligations under this Master Agreement or any Statement of Work;

(i) the Vendor undergoes a change in control which, in the sole opinion of the Client, adversely affects the Vendor's ability to satisfy some or all of its obligations under a Statement of Work;

(j) the Vendor is subject to suspension under the Performance Management Process; or

(k) the Vendor, on multiple occasions during the Term of the Master Agreement, replaces or substitutes Personnel prior to or shortly after the Project Start Date of Statements of Work.

34.2 Effect of Suspension

When removed from the list of qualified vendors of record, the Vendor:

(a) is not eligible to receive requests for services or other similar notices from Clients of work under the VOR arrangement nor to be awarded a Statement of Work;

(b) if requested by MGS, shall promptly return all OPS Confidential Information, Records, Personal Information, Ontario Data and Ontario Materials to the Client;

(c) if requested by MGS, shall provide MGS with a report detailing (i) the current state of the provision of the Services by the Vendor at the date of suspension for all current Statements of Work; and (ii) any other information requested by MGS pertaining to the provision of the Services and the performance of current Statements of Work;

(d) if requested by the MGS or the Client, shall comply with its obligations under Section 18.3 (Assignee and Form of Copyright Assignment) and 18.4 (Waiver of Moral Rights);

(e) if requested by MGS or the Client, shall execute such document required to give effect to the suspension; and

(f) shall comply with any other reasonable instructions provided by MGS.

The Minister (MGS) may, at its sole discretion, (i) set a fixed time-period during which the Vendor shall remain removed from the list of qualified vendors of record, (ii) impose conditions that the Vendor must meet in order to be reinstated onto the list of qualified vendors of record, or (iii) both. For certainty, temporary removal of the Vendor from the list of qualified vendors of record does not relieve the Vendor of any of its obligations under this Master Agreement or under each Statement of Work.

ARTICLE 35 TERMINATION OF MASTER AGREEMENT

35.1 Termination of Master Agreement by the Minister (MGS)

The Minister (MGS) may terminate this Master Agreement immediately upon written notice to the Vendor if any of the following events of default occurs:

(a) the Vendor fails to comply with any of the terms of this Master Agreement or of any Statement of Work if that failure continues unremedied for ten (10) Business Days or more after written notice of that failure is given by the Minister (MGS) to the Vendor;

(b) the Vendor is in default under Article 10 (Security Clearance Checks);

(c) any Insolvency Event occurs with respect to the Vendor;

(d) the Vendor breaches any provision in Article 26 (OPS Confidential Information) or any Privacy Provisions;

(e) the Vendor breaches Section 5.6 (Conflict of Interest) or any other conflict of interest provisions applicable to a Statement of Work;

(f) the Vendor subcontracts for the provision of part or all of the Services or sells, assigns or transfers its interest in this Master Agreement or any of its obligations under it to any third Person without the prior written approval of the Minister (MGS) except as expressly contemplated and permitted by Section 5.3 (Subcontracting or Assignment);

(g) the Vendor, prior to or after executing this Master Agreement, makes a material misrepresentation or omission or provides materially inaccurate information to Ontario;

(h) the Vendor undergoes a change in control which, in the sole opinion of Ontario, adversely affects the Vendor's ability to satisfy some or all of its obligations under this Master Agreement or any Statement of Work; or

(i) this Master Agreement is subject to termination under the Performance Management Process.

Any termination of this Master Agreement under this Section is without prejudice to Ontario's right to exercise or pursue any other remedies that may be available to Ontario under this Master Agreement, at law or in equity. All such other remedies shall survive any termination of this Master Agreement and remain in full force and effect thereafter.

35.2 Termination of Master Agreement for Convenience

The Minister (MGS) reserves the right to terminate this Master Agreement at any time, without cause and without penalty, upon sixty (60) calendar days prior written notice to the Vendor.

35.3 Termination of Master Agreement by Vendor on VOR Anniversary Date

The Vendor may, upon providing written notice to the MGS Representative no less than fifteen (15) Business Days prior to a VOR Anniversary Date, terminate this Master Agreement (but not any Statement of Work) effective as at that VOR Anniversary Date. For certainty, termination of this Master Agreement in accordance

with this Section 35.3 does not relieve the Vendor of any of its obligations under this Master Agreement or under each Statement of Work.

35.4 Effect of Expiry or Termination of Master Agreement

Upon termination of this Master Agreement, MGS will remove the Vendor from the list of qualified vendors of record to which the Vendor was added pursuant to the RFP. Despite the expiry or other termination of this Master Agreement for any reason, the terms and conditions of this Master Agreement shall continue to apply to, and shall remain in full force and effect in respect of, each Statement of Work then in effect.

35.5 Obligations on Termination of Master Agreement

Upon termination of this Master Agreement, the Vendor shall, in addition to its other obligations under this Master Agreement and at law:

(a) provide the MGS Representative with a report detailing (i) the current state of the provision of Services by the Vendor under all Statements of Work entered into at any time by the Vendor, up to and including at the date of termination, and (ii) any other information requested by MGS pertaining to the provision of the Services and performance of such Statements of Work;

(b) execute such documentation as may be required by MGS to give effect to the termination of this Master Agreement; and

(c) comply with any other reasonable instructions provided by MGS, including but not limited to instructions for facilitating the transfer of its obligations to another Person.

35.6 Debriefing

Upon the request of MGS following the expiry or earlier termination of this Master Agreement, the Vendor shall attend a debriefing session conducted by MGS where the Vendor will provide MGS with its conclusions and observations about the implementation of this Master Agreement in order to provide MGS with feedback for structuring contracts for similar services in the future.

35.7 Express Rights in Addition to Other Rights

The express rights of termination in this Master Agreement are in addition to and shall in no way limit any rights or remedies of Ontario under this Master Agreement, at law or in equity.

35.8 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 36 TERMINATION OF STATEMENTS OF WORK

36.1 Termination by Minister (Client)

The Minister (Client) may terminate a Statement of Work immediately upon written notice to the Vendor if any of the following events of default occurs:

(a) the Vendor fails to comply with any of the terms of the Statement of Work if that failure continues unremedied for ten (10) Business Days or more after written notice of that failure is given by the Minister (Client) to the Vendor;

(b) the Vendor is in default under Article 10 (Security Clearance Checks);

(c) any Insolvency Event occurs with respect to the Vendor;

(d) the Vendor breaches any provision in Article 26 (OPS Confidential Information) or any Privacy Provisions;

(e) the Vendor breaches Section 5.6 (Conflict of Interest) or any other conflict of interest provisions applicable to a Statement of Work;

(f) the Vendor subcontracts for the provision of part or all of the Services or sells, assigns or transfers its interest in the Statement of Work or any of its obligations under it to any third Person without the prior written approval of the Minister (Client) except as expressly contemplated and permitted by Section 5.3 (Subcontracting or Assignment);

(g) the Vendor, prior to or after executing the Statement of Work, makes a material misrepresentation or omission or provides materially inaccurate information to the Client;

(h) the Vendor undergoes a change in control which, in the sole opinion of the Client, adversely affects the Vendor's ability to satisfy some or all of its obligations under the Statement of Work;

(i) the Client exercises its termination right under Section 8.3 (Completion of Services); or

(j) the Client exercises its termination right under Section 9.4 (Substitution or Replacement Prior to or Shortly After Project Start Date)

Any termination of a Statement of Work under this Section is without prejudice to the Client's right to exercise or pursue any other remedies that may be available to the Client under the Statement of Work, at law or in equity. All such other remedies shall survive any termination of the Statement of Work and remain in full force and effect thereafter.

36.2 Termination for Non-Appropriation of Moneys

This Section only applies to Statements of Work to which Section 11.3 of the Financial Administration Act applies. If the Statement of Work extends into a Fiscal Year subsequent to its execution, continuation of the Statement of Work is conditional upon an appropriation of moneys by the Ontario Legislature sufficient to satisfy payments due under the Statement of Work. If such moneys are not available as a result of: (a) non-appropriation by the Ontario Legislature for the Fiscal Year in which payment becomes due; and (b) the payment being neither charged nor chargeable to an appropriation of the Ontario Legislature for a previous Fiscal Year, the Minister (Client) may terminate the Statement of Work upon giving notice to the Vendor. Termination shall become effective on the date of the beginning of the first Fiscal Year for which funds have not been appropriated.

36.3 Termination for Convenience

The Minister (Client) reserves the right to terminate any Statement of Work at any time, without cause and without penalty, upon 30 calendar days prior written notice to the Vendor, or such other number of days as may be expressly prescribed in the Statement of Work.

36.4 Payment of Vendor Upon Termination

If a Statement of Work is terminated pursuant to Section 36.2 (Termination for Non-Appropriation of Moneys) or 36.3 (Termination for Convenience), the Client shall be liable to the Vendor only for payment for Services properly performed and Deliverables delivered to and accepted by the Client up to and including the effective date of the termination, unless the Client and the Vendor agree otherwise in the Statement of Work. For certainty, if a Statement of Work provides that payment will be due and owing upon the meeting of a specified milestone (such as, for example, delivery and/or acceptance of a specified Deliverable) and the effective date of the termination of the Statement of Work passes prior to the specified milestone being met, the Client is not liable to the Vendor for payment for Services performed and/or Deliverables delivered and/or accepted in relation to that specified milestone, unless the Client and the Vendor agree otherwise in the Statement of Work. Termination shall not relieve the Vendor of its warranties and other responsibilities relating to the

accepted Deliverables, the Services performed or money paid. In addition to its other rights of hold back, the Client may hold back payment or set off against any payments owed if the Vendor fails to comply with its obligations on termination.

36.5 Obligations on Termination

Upon termination of a Statement of Work, the Vendor shall, in addition to its other obligations under the Statement of Work and at law:

(a) promptly return all OPS Confidential Information, Records, Personal Information, Ontario Data and Ontario Materials to the Client;

(b) provide the Client with a report detailing (i) the current state of the provision of the Services by the Vendor at the date of termination, and (ii) any other information requested by the Client pertaining to the provision of the Services and performance of the Statement of Work;

(c) comply with its obligations under Section 18.3 (Assignee and Form of Copyright Assignment) and 18.4 (Waiver of Moral Rights);

(d) execute such documentation as may be required by the Client to give effect to the termination of the Statement of Work; and

(e) comply with any other reasonable instructions provided by the Client, including but not limited to instructions for facilitating the transfer of its obligations to another Person.

36.6 Express Rights in Addition to Other Rights

The express rights of termination that apply to a Statement of Work are in addition to and shall in no way limit any rights or remedies of the Client under the Statement of Work, at law or in equity.

36.7 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 37 GENERAL

37.1 Promotion Restrictions - Master Agreement

Any publicity or publications related to this Master Agreement shall be at the sole discretion of MGS. Ontario may, in its sole discretion, acknowledge any Services provided by the Vendor in any such publicity or publication. The Vendor shall not make use of its association with Ontario in relation to this Master Agreement without the prior written consent of MGS. Without limiting the generality of this Section, the Vendor shall not at any time directly or indirectly communicate with the media in relation to this Master Agreement unless it has first obtained the express written authorization to do so by MGS.

37.2 Promotion Restrictions

Statements of Work - Any publicity or publications related to a Statement of Work shall be at the sole discretion of the Client. The Client may, in its sole discretion, acknowledge any Services provided by the Vendor in any such publicity or publication. The Vendor shall not make use of its association with the Client in relation to a Statement of Work without the prior written consent of the Client. Without limiting the generality of this Section, the Vendor shall not, among other things, at any time directly or indirectly communicate with the media in relation to a Statement of Work unless it has first obtained the express written authorization to do so by the Client.

37.3 Disclosure to the OPS

Despite anything to the contrary in this Master Agreement or any Statement of Work, the Vendor consents to the disclosure, and the provision of a copy, of this Master Agreement, each Statement of Work and Change Order (including any amendments to any of them and any related or resulting documents), and of data about the acquisition of Deliverables and Services pursuant to each Statement of Work, at any time and from time to time to the OPS and to the members of the Executive Council of Ontario and their advisors and staff.

37.4 Accessibility Requirements

The Vendor's delivery of the Deliverables shall comply with all applicable requirements, specifications and standards for accessibility established in accordance with the Ontario Human Rights Code (HRC) R.S.O. 1990, CHAPTER H.19, the Ontarians with Disabilities Act, S.O. 2001, CHAPTER 32, and the Accessibility for Ontarians with Disabilities Act, 2005, S.O. 2005 c. 11, any regulations made thereto and any direction from MGS or the Client.

[Signatures on next page]

IN WITNESS WHEREOF the parties hereto have executed this Master Agreement as of the date first written above.

HER MAJESTY THE QUEEN in right of Ontario as represented by the Minister of Government Services

Per:

Signature: _____

Name: **Wes Lapish**

Title: **Director, Enterprise Procurement Branch**

Pursuant to delegated authority

«Proponent_Name»

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor

ATTACHMENT A TO MASTER AGREEMENT – SERVICE CATEGORIES AND ROLES

«Proponent_Name» is qualified to provide Services in the following Roles in all Service Categories:

- Role 1: BCP/DRP Specialist
- Role 4: General Consultant
- Role 6: Financial Analyst
- Role 13: Project Manager/Lead .....

The description of all Roles and Service Categories under VOR OSS-00426611 are set out at http://www.doingbusiness.mgs.gov.on.ca/mbs/psb/psb.nsf/Attachments/OSS-00426611-Role-and-ServiceCat-Desc/$FILE/MngmntConsulting-VOR-OSS-00426611-Role-and-ServiceCat-Desc.pdf .

ATTACHMENT B TO MASTER AGREEMENT - FORM OF STATEMENT OF WORK- MINISTRIES

NOTE: THIS NOTE AND ALL INSTRUCTIONS CONTAINED IN THIS FORM ARE INTENDED ONLY AS AIDS AND SHOULD BE DELETED.

Statement of Work for Management Consulting Services

This Statement of Work no. **[Instructions: Insert reference number]** made in duplicate and effective **[Instructions: insert effective date and complete year]**, 20**[Instructions: complete year]**

[Instructions: Insert the legal name of the Vendor] (the "Vendor") and Her Majesty the Queen in Right of Ontario (the "Client") as represented by **[Instructions: Identify the minister that will sign the Statement of Work on behalf of Ontario. Insert "the Minister of" and name the applicable ministry, but in the case of the Ministry of the Attorney General, insert "the Attorney General".]** enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of **[Instructions: Insert date]** between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement"). This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client.

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$**[Instructions: Insert amount in Canadian dollars.]**

4. *Project Start Date:* **[Instructions: Insert date.]**

5. *Project End Date:* **[Instructions: Insert date.]**

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   [Instructions: describe the following here or set it out in a separate schedule:

   - **objectives**
   - **scope**
   - **detailed description of services and work to be provided or performed by the Vendor, including a list of tangible deliverables**
   - **results to be achieved**
   - **deliverables to be prepared and delivered by the Vendor**
   - **progress reports, and any other reporting requirements**
   - **project plan, if required**
   - **description of performance criteria and standards (objectives) to be achieved**
   - **measurement methods to be used by the Vendor to monitor and report on its performance**
   - **identify process for approving the replacement of the Vendor's Personnel**
   - **time frames that the Vendor must adhere to**

- **milestones and associated payment schedules**
- **associated documentation, if required**
- **contingency plan**
- **the Vendor's specific responsibilities.]**

7. *Ownership and Licences* - Attachment **[Instructions: Specify Attachment D (Vendor / Client Ownership Provisions) or Attachment E (Client Ownership Provisions).]** of the Master Agreement forms a part of this Statement of Work.

[Instructions: Number the following paragraphs.]

* *Quality Control* - **[Instructions: If the Vendor is required to use any quality control plan or process in the course of doing its work, identify it and set out the particulars here. Otherwise, delete this provision.]**

* *Methodologies* - **[Instructions: If the Vendor is required to use any specific methodology in the course of doing its work, identify it and set out the particulars here. Otherwise, delete this provision.]**

* *Beyond Scope of Services and Deliverables* - The following activities are not within the scope of this Statement of Work: **[Instructions: Identify activities that will not be addressed under this Statement of Work. Otherwise, delete this provision.]**

[Instructions: If the ministry consents to the use of any Subcontractor's Personnel, complete the following table. Otherwise, delete the following consent and table.]

*. *Names and Roles of Vendor's Subcontractors* - The Client hereby consents to the use by the Vendor of the Subcontractors, and of the Subcontractors' Personnel, listed below for the particular Roles (including experience levels) specified.

Legal Name of Corporation	**Individual's Legal Name**	**Individual's Role and Experience Level**	**Service Category**

[Instructions: Complete the following table in respect of the Vendor's own Personnel.]

* *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	Individual's Role and Experience Level	Service Category

* *Invoices* - Invoices for payment of any charges under this Statement of Work shall be sent to:

[Instructions: insert address]

or such other address as the Client may from time to time communicate to the Vendor in writing.

* *Billing and Payment Process* - **[Instructions: If the billing and payment process is to differ from that set out in Section 14.2 of the Master Agreement, set out the billing and payment process here. Otherwise, delete this provision.]**

* *Freedom of Information and Protection of Privacy Records* - The following chart lists recorded information that is not in the custody or control of the Client:

The following Records are not in the custody or control of the Client:

* *Communications and Reporting* - The Vendor shall meet with the Client Representative **[Instructions: specify frequency]** during the Project Term to provide status reports or to obtain approval for Deliverables.

* *Knowledge Transfer:*

From	To	Knowledge to be Transferred

[Instructions: Specify how knowledge is to be transferred by the Vendor.]

* *Destruction of Information* - The Vendor shall destroy all information contained on any media, if requested to do so by the Client. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

* *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**[insert complete mailing address]**
Client Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**
Backup Client Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**

[Instructions: This provision is optional:]

* *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**[insert complete mailing address]**
Vendor Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**
Backup Vendor Representative:	[insert name and title of individual]
Telephone number:	[insert area code and number]
E-mail:	[insert e-mail address]

*. *Insurance* – **[Instructions: If additional insurance coverage or amounts or endorsements are required for this specific Statement of Work, identify the additional requirements here.]**

* *Other Provisions* **– [Instructions: Insert other provisions as required.]**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN in right of Ontario as represented by **[Instructions: See the instructions on the first page]**

Per:

Signature: _____

Name: _____

Title: _____

Pursuant to delegated authority.

[INSTRUCTIONS: INSERT LEGAL NAME OF THE VENDOR]

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor.

ATTACHMENT C TO MASTER AGREEMENT - FORM OF STATEMENT OF WORK – OPS ENTITY

NOTE: THIS NOTE AND ALL INSTRUCTIONS CONTAINED IN THIS FORM ARE INTENDED ONLY AS AIDS AND SHOULD BE DELETED.

Statement of Work for Management Consulting Services

This Statement of Work no. **[Instructions: Insert reference number] made in duplicate and effective [Instructions: insert effective date and complete year]**, 20**[Instructions: complete year]**

[Instructions: Insert the legal name of the Vendor] (the "Vendor") and **[Instructions: Insert the legal name of the OPS Entity]** (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of **[Insert Date]** between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$ **[Instructions: Insert amount in Canadian dollars.]**

4. *Project Start Date:* **[Instructions: Insert date.]**

5. *Project End Date:* **[Instructions: Insert date.]**

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

[Instructions: describe the following here or set it out in a separate schedule:

- **objectives**
- **scope**
- **detailed description of services and work to be provided or performed by the Vendor, including a list of tangible deliverables**
- **results to be achieved**
- **deliverables to be prepared and delivered by the Vendor**
- **progress reports, and any other reporting requirements**
- **project plan, if required**
- **description of performance criteria and standards (objectives) to be achieved**
- **measurement methods to be used by the Vendor to monitor and report on its performance**
- **identify process for approving the replacement of the Vendor's Personnel**
- **time frames that the Vendor must adhere to**
- **milestones and associated payment schedules**
- **associated documentation, if required**
- **contingency plan**
- **the Vendor's specific responsibilities.]**

7. *Ownership and Licences* - Attachment **[Instructions: Specify Attachment D (Vendor / Client Ownership Provisions) or Attachment E (Client Ownership Provisions).]** of the Master Agreement forms a part of this Statement of Work.

[Instructions: Number the following paragraphs.]

* *Quality Control* - **[Instructions: If the Vendor is required to use any quality control plan or process in the course of doing its work, identify it and set out the particulars here. Otherwise, delete this provision.]**

* *Methodologies* - **[Instructions: If the Vendor is required to use any specific methodology in the course of doing its work, identify it and set out the particulars here. Otherwise, delete this provision.]**

* *Beyond Scope of Services and Deliverables* - The following activities are not within the scope of this Statement of Work: **[Instructions: Identify activities that will not be addressed under this Statement of Work. Otherwise, delete this provision.]**

[Instructions: If the Client consents to the use of any Subcontractor's Personnel, complete the following table. Otherwise, delete the following consent and table.]

* *Names and Roles of Vendor's Subcontractors* - The Client hereby consents to the use by the Vendor of the Subcontractors, and of the Subcontractors' Personnel, listed below for the particular Roles (including experience levels) specified.

Legal Name of Corporation	Individual's Legal Name	Individual's Role and Experience Level	Service Category

[Instructions: Complete the following table in respect of the Vendor's own Personnel.]

*. *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	Individual's Role and Experience Level	Service Category

*. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

[Instructions: insert address]

or such other address as the Client may from time to time communicate to the Vendor in writing.

*. *Billing and Payment Process* - **[Instructions: If the billing and payment process is to differ from that set out in Section 14.2 of the Master Agreement, set out the billing and payment process here. Otherwise, delete this provision.]**

* *Freedom of Information and Protection of Privacy Records* - The following chart lists recorded information that is not in the custody or control of the Client:

The following Records are not in the custody or control of the Client:

* *Communications and Reporting* - **The Vendor shall meet with the Client Representative [Instructions: specify frequency] during the Project Term to provide status reports or to obtain approval for Deliverables.**

* *Knowledge Transfer:*

From	To	Knowledge to be Transferred

[Instructions: Specify how knowledge is to be transferred by the Vendor.]

*. *Destruction of Information* - The Vendor shall destroy all information contained on any media, if requested to do so by the Client. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

[Instructions: Insert the relevant information below:]

* *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**[insert complete mailing address]**
Client Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**
Backup Client Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**

[Instructions: This provision is optional:]

* *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**[insert complete mailing address]**
Vendor Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**
Backup Vendor Representative:	**[insert name and title of individual]**
Telephone number:	**[insert area code and number]**
E-mail:	**[insert e-mail address]**

*. *Insurance* – **[Instructions: If additional insurance coverage or amounts or endorsements are required for this specific Statement of Work, identify the additional requirements here.]**

* *Other Provisions* – **[Instructions: Insert other provisions as required.]**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

[INSTRUCTIONS: INSERT LEGAL NAME OF THE OPS ENTITY.]

Per:

Signature: _____

Name: _____

Title: _____

Pursuant to delegated authority.

[INSTRUCTIONS: INSERT LEGAL NAME OF THE VENDOR]

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor.

ATTACHMENT D TO MASTER AGREEMENT – VENDOR / CLIENT OWNERSHIP PROVISIONS

1.2 In respect of each Statement of Work to which this Attachment D applies, these words and expressions have these meanings:

"**Competitive Commercialization**" means exploitation of Intellectual Property Rights in Vendor Work Inventions or Vendor Work Information for any commercial advantage in competition with the Vendor with the effect of making a net monetary gain, but does not include: (a) any exploitation by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work where the good or service developed or produced through such exploitation is for use by the Client, its sublicensees, Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, Provincially Funded Organizations, or the public, including any dissemination or distribution in connection with such exploitation, or (b) any dissemination or distribution by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work.

"**Confidential Work Information**" means all information that (a) is confidential by its nature or in the circumstances in which it is conceived, developed or produced, and (b) is conceived, developed or produced by one or more of the Personnel of the Vendor in the performance of Work whether with one or more of the Personnel of the Client or not. "Confidential Work Information" includes all Joint Work Inventions, Joint Work Material, Other Work Inventions and Non-Technical Work.

"**Non-Technical Work**" means all Deliverables other than the Vendor Work Inventions, the Vendor Work Information, the Confidential Work Information, the Joint Work Inventions, the Joint Work Material, and the Other Work Inventions. "Non-Technical Work" does not include the Vendor Materials.

"**Other Work Invention**" means any Invention conceived, or conceived and developed, solely or jointly by one or more of the Personnel of the Vendor in the performance of Work, but excludes any Joint Work Invention and any Vendor Work Invention.

"**Vendor Work Information**" means all Technical Information developed or produced by the Vendor or its Subcontractors in the performance of Work under a Statement of Work, but excludes any contribution made by one or more of the Personnel of the Vendor to any Joint Work Material; and also excludes all Client Work Information.

"**Vendor Work Invention**" means any Invention conceived, or conceived and developed, solely or jointly by one or more of the Personnel of the Vendor or its Subcontractor in the course of developing or producing Vendor Work Information, but excludes any Joint Work Invention.

"**Vendor Work Product**" means all Deliverables that are created, developed, generated, prepared or produced by one or more of the Personnel of the Vendor in the performance of Work, including all Joint Work Material and Non-Technical Work.

"**Work Patent Application**" means a patent application on a Vendor Work Invention filed by or on behalf of the Vendor or any of its assignees, related entities or Subcontractors or any of their advisors, agents or Personnel, in Canada or in any other country or international patent office.

ARTICLE 16. LICENCE TO RIGHTS IN VENDOR WORK INVENTIONS AND VENDOR WORK INFORMATION

16.1 Licence to Client

It is a provision of each Statement of Work that the Vendor hereby grants to the Client a non-exclusive, perpetual, irrevocable, world-wide, fully paid-up, royalty-free licence to exercise all Intellectual Property Rights and every other right, title and interest in the Vendor Work Inventions and Vendor Work Information, and under each patent issued as a result of a Work Patent Application, in any way and for any purpose whatsoever except Competitive Commercialization, and to have or permit others to do so. Solely by way of example, the licence granted to the Client above includes the right to use, reproduce, produce any translation, and improve, and

includes the right to sublicense to Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, Provincially Funded Organizations, other governments and their agencies, and other public bodies.

The licence rights to the Vendor Work Inventions and Vendor Work Information shall arise immediately, as and when they, or any part of them, are conceived, created, developed or modified, generated, prepared or produced. The licence set out in this Section is non-transferable by the Client except that: (1) if the Client is Ontario, the Client may transfer the licence to a Permitted OPS Assignee; and (2) if the Client is an OPS Entity, the Client may transfer the licence to Ontario or, where such transfer is necessitated by outsourcing, privatizing, partnering or similar activity, to a non-governmental entity.

16.2 Third-Party Contractors

The Vendor acknowledges that, at any time, the Client may wish to enter into contracts with one or more third parties, whether by a competitive process or not, to exercise the licence set out in Section 16.1. Solely by way of example, such contracts may be with non-governmental entities for the adaptation, audit, communication, correction, development, enhancement, improvement, inspection, modification, operation, overhaul, recording, reproduction, revision, storage, support, translation or use of any or all of the Vendor Work Inventions and Vendor Work Information. Without restricting Section 16.1, the Vendor agrees that the Client's licence in Section 16.1 includes the right to disclose the Vendor Work Inventions and Vendor Work Information to such third parties, including actual and potential proponents for such contracts, and to sublicense or otherwise authorize the use of the Vendor Work Inventions and Vendor Work Information by any third parties engaged by the Client solely to carry out any such contracts. The Client shall require actual and potential proponents and such third parties not to use or disclose any Vendor Work Inventions or Vendor Work Information except as may be necessary to bid for or to carry out any such contracts or except if required by order of a court or tribunal.

16.3 Title to Improvements and Modifications

All Intellectual Property Rights arising from any further development or modification of the Vendor Work Inventions and Vendor Work Information that is conceived, developed, effected or first reduced to practice by or for the Client in the exercise of the licence set out in Section 16.1 shall vest in the Client, or as the Client directs, and shall not vest in the Vendor, its Personnel or Subcontractors except pursuant to a subsequent written contract.

16.4 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work

ARTICLE 17. OWNERSHIP OF RIGHTS

17.1 Vendor's Ownership of Rights in Vendor Work Inventions and Vendor Work Information

Without affecting any Intellectual Property Rights or other interests in or to Ontario Data, and subject to Article 16, Section 17.2, Section 17.6, Article 18, Article 19, Article 24, all Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information shall immediately, as and when they come into existence, vest in and remain the property of the Vendor. The Client shall not have any right in or to the Vendor's Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information except any right that may be granted in writing by the Vendor.

17.2 Pre-Existing Intellectual Property Rights

All Intellectual Property Rights existing immediately prior to the Project Start Date, and all rights to Inventions first conceived, developed or reduced to practice prior to such date, shall be retained by each Party and each third party that owned such rights immediately prior to such date.

17.3 Disclosure to Client

The Vendor shall promptly report and fully disclose in writing to the Client all Confidential Work Information, Joint Work Inventions, Joint Work Material, Vendor Work Inventions, Vendor Work Information, Non-Technical Work, Other Work Inventions, and all contributions made by the Personnel of the Vendor to any Joint Work Inventions, including copies of all written disclosures submitted to the Vendor pertaining to them. The Vendor's disclosure shall include a description of the specific components in sufficient detail to permit the Client to clearly identify such components and to distinguish them from the Vendor Materials and the Ontario Materials. Disclosure of Vendor Work Inventions, Other Work Inventions and Joint Work Inventions shall be on the form set out in Attachment I. In any event, the Vendor shall make such disclosure not later than the time of completion of the Services or such earlier time as the Client or the Statement of Work may require.

17.4 Audit Rights

During the Project Term and for seven (7) years following the termination or expiry of each Statement of Work, the Client shall have the right to examine and make copies of all records and supporting data of the Vendor which the Client reasonably deems pertinent to the identification of Confidential Work Information, Joint Work Material, Vendor Work Inventions, Vendor Work Information, Non-Technical Work, Other Work Inventions, or any contribution made by one or more of the Personnel of the Vendor to any Joint Work Invention, upon reasonable notice and with no more than minimal disruption to the Vendor's ongoing operations, and the Vendor shall, at its own cost, retain and maintain in an organised, accessible mode, all such records and supporting data for such period.

17.5 Ownership of Tangible Materials

Regardless of the ownership of any Intellectual Property Rights in any Deliverables, the Client shall own, and have unrestricted ownership rights in, all tangible materials as and when delivered by the Vendor to the Client in connection with the Statement of Work. The Vendor hereby irrevocably assigns, sells and transfers, and it shall be a term of the Statement of Work that the Vendor irrevocably assigns, sells and transfers, all right, title and interest in and to such tangible materials to the Client at no additional cost as and when delivered. The Vendor shall, at its own expense, promptly do any and all acts and cause to be executed and deliver to the Client any and all assignments, documents and instruments that the Client may reasonably request at any time or from time to time to carry out the intent of this Section.

17.6 Vendor Trademarks and Designations

Despite any other provisions of this Master Agreement, nothing in this Master Agreement or in a Statement of Work or the performance of the Statement of Work shall grant to the Client any right, title, interest or licence in or to the names, trade names, logos, trade dress, or other trademarks or designations of the Vendor, its Subcontractors or third-party licensors, except as expressly stated in the Statement of Work.

17.7 IP Notices

Except to the extent the Vendor is required to convey to the Client all of the Intellectual Property Rights in the Vendor Work Inventions and the Vendor Work Information in accordance with Section 18.1, the Client shall not, without the prior written consent of the Vendor which shall not be unreasonably withheld, remove any intellectual property notices of the Vendor or of the Vendor's Subcontractors on any Vendor Work Information.

17.8 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 18. ASSIGNMENT TO ONTARIO AND OPS ENTITIES

18.1 Assignment on Default

If the Minister (Client) terminates a Statement of Work in whole or in part for default, or if

(a) the Vendor fails to complete the Services,

(b) the Vendor fails to deliver all of the Vendor Work Information to the Client,

(c) the Vendor Work Information do not meet the criteria as described in the Statement of Work, or

(d) the Vendor fails to disclose all of the Vendor Work Inventions, Vendor Work Information, Non-Technical Work, Other Work Inventions, and contributions made by any Personnel of the Vendor to any Joint Work Invention, in accordance with Section 17.3,

the Client may, by notice to the Vendor, require the Vendor to convey to the Client all of the Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information, including each patent issued as a result of a Work Patent Application or, in the case of a notice based on failure to disclose, all of the Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information not disclosed including each patent issued as a result of a Work Patent Application on a Vendor Work Invention not disclosed, if such failure to disclose is not cured by the Vendor within ninety (90) days after notice by the Client. In the case of any notice under this Section, the rights to be conveyed shall include the Intellectual Property Rights in any Vendor Work Inventions and Vendor Work Information that have vested or are to vest in a Subcontractor.

18.2 Assignment by Personnel, Subcontractors and Others

To give effect to Section 18.1, to the extent that any right, title or interest or any Intellectual Property Rights in or to any Vendor Work Inventions and Vendor Work Information vest, by operation of law or otherwise, in any of the Vendor's directors, officers, Personnel, advisors, agents, partners, affiliates, volunteers, Subcontractors, suppliers or others for whom the Vendor is responsible at law, the Vendor shall cause each of them to assign and transfer to the Client at no cost all of such right, title and interest and all of such Intellectual Property Rights other than any Intellectual Property Rights or interests in Intellectual Property Rights that came into existence prior to the Project Start Date.

18.3 Assignee and Form of Copyright Assignment

Written assignments of any Intellectual Property Rights pursuant to a Statement of Work: (a) to Ontario shall be to "Her Majesty the Queen in right of Ontario", but written assignments of any copyright shall be to the "Queen's Printer for Ontario" in the form set out in Attachment F, or in such form that is satisfactory to the Client where the assignor is not a corporation; and (b) to the OPS Entity shall be in the name of the OPS Entity and, where the Intellectual Property Right is copyright, the written assignment of copyright shall be in the form set out in Attachment F, or in such form that is satisfactory to the Client where the assignor is not a corporation. At the completion of the Services under each Statement of Work or upon the termination of the Statement of Work, the Vendor shall provide to the Client an original, executed assignment of copyright in the form set out in Attachment F, as modified as necessary as set out above.

18.4 Waiver of Moral Rights

The Vendor acknowledges and agrees that all Moral Rights with respect to the Deliverables under each applicable Statement of Work shall be waived irrevocably and without restriction by each of its Personnel in favour of Her Majesty the Queen in right of Ontario and all of its ministries, other administrative units over which ministers of Ontario preside, including its agencies, boards, commissions and Crown corporations, all offices of the officers of the Legislative Assembly or of the Ontario Legislature, OPS Entities, and all sublicenses and assignees, and all persons authorized at any time to use the Deliverables. At the completion of the Services under each Statement of Work or upon the termination of the Statement of Work, the Vendor shall obtain from

each of its Personnel an original, executed waiver of Moral Rights in the form attached as Attachment G (Waiver of Moral Rights Form) and shall deliver such waiver to the Client upon request of the Client.

18.5 Invention Disclosure

Prior to allowing any Person to perform Services under the Statement of Work, the Vendor shall, by written agreement, require such Person to agree,

(a) to promptly report and fully disclose in writing to the Vendor each Vendor Work Invention, Joint Work Invention and Other Work Invention, identifying those concepts or ideas thought to be new, useful and unobvious, and indicating whether they are thought to be an improvement on prior art or capable of commercial exploitation; and

(b) upon request, during and after employment, to execute all assignments, documents and instruments necessary or advantageous to file patent applications on Vendor Work Inventions, Joint Work Inventions and Other Work Inventions and to establish Vendor's rights in the Vendor Work Inventions and the Client's rights in the Joint Work Inventions and Other Work Inventions.

18.6 Intellectual Property Rights Applications

To give effect to Section 18.1, the Vendor shall, at the Client's expense, give the Client all reasonable assistance in the preparation and the prosecution of any applications or registrations in any jurisdiction for or of any Intellectual Property Rights on or arising out of the Vendor Work Inventions and Vendor Work Information, including the assistance of the inventors in the case of patent applications on any Vendor Work Inventions.

18.7 Further Assurances

The Vendor shall, at its own expense, promptly do any and all acts and cause to be executed and deliver to the Client any and all assignments, documents and instruments relating to the Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information, which the Client may reasonably request at any time or from time to time to carry out the intent of this Article.

18.8 Power of Attorney

If the Client is unable for any reason whatsoever to secure the Vendor's signature to any document assigning, perfecting, recording or acknowledging the ownership of any Vendor Work Inventions, Vendor Work Information or patent pursuant to Section 18.1, the Vendor hereby irrevocably designates and appoints the Client and its duly authorized officers as its attorneys-in-fact, with full power of substitution, to act for and on behalf of and instead of the Vendor to execute and file any such document and to do all lawfully permitted acts to further the purposes of this Section with the same legal force and effect as if executed by the Vendor.

18.9 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 19. TRANSFERS AND LICENCES BY VENDOR

19.1 Restrictions Before Completion and Disclosure

In respect of a Statement of Work, until the Vendor completes the Services and discloses all of the Vendor Work Inventions and Vendor Work Information in accordance with Section 17.3, the Vendor and its Personnel and Subcontractors shall not, without the prior written permission of the Client, assign, sell, or otherwise transfer title to the Intellectual Property Rights in any Vendor Work Inventions and Vendor Work Information.

19.2 Obligations and Restrictions

In any assignment, sale, transfer or licence of Intellectual Property Rights in Vendor Work Inventions and Vendor Work Information by the Vendor except a sale or licence for end use of a product based on Vendor Work Inventions and Vendor Work Information, the Vendor shall ensure that the other party is aware of and agrees to comply with all of the Vendor's obligations to the Client in relation to Intellectual Property Rights and any restrictions set out in this Master Agreement or any applicable Statement of Work on the use or disposition of Intellectual Property Rights, including the obligation to impose the same obligations and restrictions on any subsequent assignee, purchaser, transferee or licensee.

19.3 Notification

The Vendor shall promptly notify the Client of the name, address and other pertinent information in regard to any such assignee, purchaser, transferee or licensee, and shall ensure that such party is required to do the same with regard to any subsequent assignee, purchaser, transferee or licensee.

19.4 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 20. NOTIFICATION OF WORK PATENT APPLICATIONS AND ISSUED PATENTS

20.1 Notification of Work Patent Applications

The Vendor will notify the Client Representative in writing, in accordance with Section 2.9 (Notices by Prescribed Means), of each Work Patent Application within one month after the Work Patent Application is filed. The notification to the Client Representative shall:

(a) include the filing date, serial number and title of the Work Patent Application;

(b) include a copy of the Work Patent Application (including an English-language version if filed in a language other than English) and all official papers relating to the Work Patent Application;

(c) identify each inventor;

(d) provide particulars of the Statement of Work and specify that the Invention was made in the performance of work under the Statement of Work; and

(e) specify whether any manuscript describing the Invention has been submitted for publication and, if so, provide particulars of its publication or acceptance for publication as known when notified.

20.2 Notification of Resulting Patents

The Vendor will notify the Client Representative in writing, in accordance with Section 2.9 (Notices by Prescribed Means), of the patent number and issue date for each patent issued as a result of a Work Patent Application, within one month after the issuance of the patent.

20.3 Disclosure

The Vendor agrees that, eighteen (18) months after the filing date of a Work Patent Application, the Client may reproduce and disclose all documents furnished pursuant to this Article in connection with such Work Patent Application.

20.4 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 21. VENDOR MATERIALS

21.1 Request for Consent

The Parties acknowledge that from time to time, the Vendor may wish to incorporate Vendor Materials into the Deliverables. Prior to incorporating any Vendor Materials into any Deliverables, the Vendor shall:

(a) fully disclose to the Client in writing all Vendor Materials that the Vendor proposes to incorporate, which shall include a description of the specific components in sufficient detail to permit the Client to clearly identify and to distinguish them from the Vendor Work Product, Non-Technical Work and the Ontario Materials; and

(b) obtain the Client's prior written consent to such incorporation or use, which consent shall be in the sole discretion of the Client and subject to the terms and conditions as agreed to by the Client as set out in the Statement of Work or Change Order.

21.2 Subcontractors

If any applicable Intellectual Property Rights are owned by a Subcontractor or are licensed to the Subcontractor by a related person, the Vendor shall either obtain a licence from that Subcontractor that permits compliance with Sections 21.4, 22.1 and 22.2 or arrange for the Subcontractor to convey directly to the Client the same rights by execution of the form provided for that purpose by the Client, in which case the Vendor shall deliver that form to the Client, duly completed and executed by the Subcontractor, no later than the time of disclosure to the Client of those Vendor Materials.

21.3 Ownership of Vendor Materials

As between the Client and the Vendor, the Vendor shall have and continue to retain all right, title and interest, including all Intellectual Property Rights, in and to all Vendor Materials, except as otherwise set out in this Master Agreement or the Statement of Work. The Client shall not acquire by virtue of this Master Agreement or the Statement of Work any right, title or interest, including any Intellectual Property Rights, in or to any Vendor Materials, except as otherwise set out in this Master Agreement or the Statement of Work.

21.4 Licence to Vendor Materials Incorporated into Any Vendor Work Product

It is a provision of each Statement of Work that the Vendor hereby grants to the Client a non-exclusive, perpetual, irrevocable, world-wide, fully paid-up, royalty-free licence to exercise all Intellectual Property Rights in the Vendor Materials that are incorporated into any Vendor Work Product in any way and for any purpose whatsoever except Restricted Commercialization, and to have or permit others to do so. Solely by way of example, the licence granted to the Client above includes the right to use, reproduce, produce any translation, improve, and disclose, and includes the right to sublicense Ontario (including any and all of its ministries), OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, Provincially Funded Organizations, other governments and their agencies and other public bodies.

In this Section 21.4, "Restricted Commercialization" means exploitation of Intellectual Property Rights in Vendor Materials for any commercial advantage in competition with the Vendor with the effect of making a net monetary gain, but does not include: (a) any exploitation by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work where the good or service developed or produced through such exploitation is for use by the Client, its sublicensees, Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, the Provincially Funded Organizations, or the public, including any dissemination or distribution in connection with such exploitation, or (b) any dissemination

or distribution by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work.

The licence rights to the Vendor Materials that are incorporated into any Vendor Work Product shall arise immediately, as and when the Vendor Materials, or any part of them, are incorporated into the Vendor Work Product. The licence set out in this Section is non-transferable by the Client except that: (1) if the Client is Ontario, the Client may transfer the licence to a Permitted OPS Assignee; and (2) if the Client is an OPS Entity, the Client may transfer the licence to Ontario.

21.5 Vendor Materials and Third-Party Contractors

The Vendor acknowledges that the Client may wish to enter into contracts with one or more third parties in respect of the licence rights set out in Section 21.4, whether by a competitive process or not. Without restricting the generality of Section 21.4, the Vendor agrees that the licence granted in relation to the Intellectual Property Rights in the Vendor Materials includes the right to disclose the Vendor Materials to such third parties, including actual and potential proponents for such contracts, and to sublicense or otherwise authorize any such third parties engaged to do anything solely on behalf of the Client that the Client may do with the Vendor Materials and the Intellectual Property Rights in the Vendor Materials. Subject to Section 21.4, the Client shall require actual and potential proponents and such third parties not to use or disclose any confidential Vendor Materials except as may be necessary to bid for or to carry out any such contracts or except if required by order of a court or tribunal.

21.6 Title to Improvements and Modifications to Vendor Materials

All Intellectual Property Rights arising from any further development or modification of the Vendor Materials that is conceived, developed, effected or first reduced to practice by or for the Client in the exercise of any licence set out in Section 21.4 shall vest in the Client or as the Client directs, and shall not vest in the Vendor, its Personnel or Subcontractors except pursuant to a subsequent written contract executed by the Client and the Vendor, its Personnel or Subcontractors, as the case may be.

21.7 IP Notices on Vendor Materials

The Client shall not, without the prior written consent of the Vendor, which shall not be unreasonably withheld, remove any intellectual property notices of the Vendor or the Vendor's Subcontractors on any Vendor Materials.

21.8 Third-Party Vendor Materials Incorporated into the Deliverables

In the case of any Third-Party Vendor Materials that are incorporated into the Deliverables, the Client shall be entitled, at its option, to assume from the Vendor all of its rights to such Third-Party Vendor Materials under any licence and other agreements, and the Vendor shall ensure that any such agreements permitting their assignment and transfer to the Client or as the Client directs, and that such assignment and transfer shall be at no charge to the Client but the Client shall be responsible for any ongoing licence or other payments required to be made to any third parties under any such agreements. If such agreement is not acceptable to the Client, the Vendor will use commercially reasonable efforts to facilitate the Client's pursuit of an acceptable agreement with the relevant third party.

21.9 Third-Party Vendor Materials Used Non-Exclusively

In the case of any Third-Party Vendor Materials that are used in connection with the Services performed for the Client but are also used by the Vendor in connection with services provided by it to others or for the internal purposes of the Vendor not connected with this Master Agreement, upon request by the Client, the Vendor shall assist the Client to acquire a licence to such materials or to acquire from some other person a licence to materials that are functionally/substantively equivalent to such materials. Such licence shall contain terms and conditions as are reasonably acceptable to the Client to enable the Client to obtain or to use the Third-Party Vendor Materials or replacements therefor. The Client shall be responsible for any fees payable to the third-party licensor after such acquisition.

21.10 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 22. SPECIFIC THIRD-PARTY SUBLICENSEES AND LICENCE ISSUES

22.1 Provincially Funded Organizations

Without restricting Sections 16.1 or 21.4, the Vendor agrees that licence rights granted under a Statement of Work in relation to the Intellectual Property Rights in the Vendor Work Inventions, and Vendor Work Information, and in the Vendor Materials that are incorporated into any Vendor Work Product, include the right to disclose the Vendor Work Inventions, Vendor Work Information and such Vendor Materials to any Provincially Funded Organizations, and to sublicense or otherwise authorize the Provincially Funded Organization to exercise the licence rights granted under the Statement of Work. Such disclosure of Vendor Work Inventions and Vendor Work Information shall be limited and subject to obligations of confidentiality.

22.2 Third-Party Non-Governmental Entities

Without restricting Sections 16.1, 16.2, 21.4 or 21.5, the Vendor agrees that the licence rights under a Statement of Work in relation to the Intellectual Property Rights in the Vendor Work Inventions and Vendor Work Information, and in the Vendor Materials that are incorporated into any Vendor Work Product, include the right to disclose the Vendor Work Inventions, Vendor Work Information and such Vendor Materials to any third-party non-governmental entities that provide services to or on behalf of the Client as a result of alternative service delivery, backward or forward integration, outsourcing, privatization, partnering, procurement endeavours or similar activity, and to sublicense or otherwise authorize such third-party non-governmental entities to exercise the licence rights granted under the Statement of Work to the extent that they are exercised for or on behalf of the Client. The Client may disclose the Vendor Materials incorporated into any Joint Work Material or Non-Technical Work without restriction to any such third-party non-governmental entities. The Client shall require such third-party non-governmental entities not to use or disclose any Confidential Vendor Materials incorporated into the Vendor Work Inventions or Vendor Work Information, except as may be necessary to provide services as contemplated in this Section.

22.3 Scope of Rights to Inventions and Patents

To the extent necessary for the Client to exercise any licence granted under the Statement of Work, it is a provision of each Statement of Work that the Vendor hereby grants to the Client a licence under any patent now held or later obtained by the Vendor. Such patent licence shall be co-extensive and co-terminus with such licence. Nothing contained in this Master Agreement or any Statement of Work shall be deemed to grant to the Vendor any rights with respect to any Joint Work Invention, Client Work Invention or Other Work Invention. Subject to the foregoing, nothing contained in this Article shall be deemed to grant to the Client any rights with respect to any Invention other than Vendor Work Inventions or with respect to any patent other than a patent issued as a result of a Work Patent Application.

22.4 General

Without limiting any of Sections 16.1, 16.2, 21.4 or 21.5, Ontario's rights under Article 16, Article 21 and this Article:

(a) apply despite any terms to the contrary in any click-wrap licence, documentation, invoice, shrink-wrap licence, Technical Information, web site, or in any other terms or licence attached to or delivered by the Vendor with any Deliverables, except to the extent that the Client has agreed in writing pursuant to subsection (b) of Section 21.1;

(b) include the right to reproduce and use Vendor Work Inventions, Vendor Work Information, and Vendor Materials incorporated into any Vendor Work Product, and any developed or modified

form of them, on any and all computer systems owned, leased or operated by Ontario or the OPS (including OPS Entities) anywhere in the world at any time; and

(c) are in addition to and not in lieu of its rights under any other provisions of this Master Agreement or the Statement of Work.

22.5 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 23. PERSONAL KNOWLEDGE, SKILL AND EXPERTISE

23.1 Personal Knowledge, Skill and Expertise

Each Party understands and agrees that each of the Personnel of the other Party, in connection with the performance of this Master Agreement and a Statement of Work, may acquire Personal Knowledge. Subject to Article 26, Article 28, the Privacy Provisions and any other statute under which Ontario or the OPS Entity has the discretion or obligation not to disclose any records or other information, the use by such Personnel of the other Party of such Personal Knowledge in the ordinary course of their employment with the other Party (including its subsidiaries, its parent, or other subsidiaries of its parent, in the case of the Vendor; and including Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, or Provincially Funded Organizations, in the case of Ontario or the OPS Entity; and its Subcontractors) does not breach the Statement of Work provided, however, that nothing in this Section grants to any Personnel the right to obtain a patent in respect of any such Personal Knowledge.

23.2 Employee Mobility

Each Party agrees that the other Party's receipt of confidential information as contemplated by a Statement of Work will not create any obligation in any way limiting or restricting the transfer of Personnel within the other Party's organization.

23.3 Indemnity

Despite the limitations of liability set out in Article 33 (Limitation of Liability), the Vendor shall indemnify and hold harmless the Indemnified Parties from and against all Losses and Proceedings, by whomever made, sustained, incurred, brought or prosecuted, arising out of, or in connection with the use of any Personal Knowledge by the Vendor's Personnel.

23.4 Scope

Nothing in this Article grants or waives any Intellectual Property Rights of either Party or any other person.

23.5 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 24. PROPERTY OF ONTARIO AND THE OPS ENTITIES

24.1 Ownership of Ontario Materials and Ontario Data

The Vendor acknowledges that Ontario, OPS Entities and their respective Subcontractors and third-party licensors shall have and continue to retain all right, title and interest, including all Intellectual Property Rights, in and to all Ontario Materials and Ontario Data, all assets acquired or held by Ontario or the OPS Entity prior to the Project Start Date or during the Project Term of each Statement of Work, and all assets provided by Ontario or the OPS Entity to the Vendor in connection with each Statement of Work. The Vendor shall not acquire by

virtue of this Master Agreement, or any Statement of Work, any right, title or interest, including any Intellectual Property Rights, in or to any Ontario Materials and Ontario Data.

24.2 Ownership of Third-Party Ontario Materials

Nothing in this Master Agreement or any Statement of Work or the performance of any Statement of Work shall grant to the Vendor any right, title or interest in or to any Third-Party Ontario Materials. To the extent any right, title or interest in or to any Third-Party Ontario Materials vests, by operation of law or otherwise, in the Vendor (or its Personnel, Subcontractors or others for whom it is responsible at law), the Vendor shall, and hereby does, irrevocably assign, sell and transfer to the Client at no cost all of its right, title and interest in and to all such Third-Party Ontario Materials, and the same shall be deemed to form part of the Ontario Materials.

24.3 Works of Joint Authorship

Subject to Section 17.2 and Section 21.3, if any Vendor Work Product is a work of joint authorship, the copyright in the work of joint authorship shall immediately, as soon as it comes into existence, vest in the Client, and the Vendor and its Subcontractors shall have no right, title or interest in or to it.

24.4 Proscribed Intellectual Property Rights Registrations

The Vendor shall not file any application, and shall not contest any application filed by Ontario or any OPS Entity, in any jurisdiction for the registration of any Intellectual Property Rights arising out of any Ontario Materials, Client Work Information, Client Work Inventions, Joint Work Inventions, Joint Work Material, Non-Technical Work, or Other Work Inventions whether or not such Intellectual Property Rights depend or would depend upon any pre-existing Intellectual Property Rights.

24.5 Collective Works and Compilations

Despite any other provision in this Master Agreement or the Statement of Work, if any Vendor Work Product is a collective work or a compilation:

(a) the Client shall retain its right, title and interest in and to its contribution to such collective work or compilation;

(b) ownership of all right, title and interest in and to the Vendor's and its Subcontractors' contributions to such collective work or compilation shall be governed by Section 17.1; and

(c) the copyright in such collective work or compilation shall immediately, as soon as it comes into existence, vest in the Client, and the Vendor and its Subcontractors shall have no right, title or interest in or to it.

24.6 Client Work Inventions and Client Work Information

The Client retains all of its Intellectual Property Rights and all of its right, title, and interest throughout the world to each Client Work Invention and to all Client Work Information.

24.7 Intellectual Property Rights to Ontario Materials

To the extent any Intellectual Property Rights or any other right, title or interest in or to any Ontario Materials vests, by operation of law or otherwise, in the Vendor (or its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors or others for whom it is responsible at law), the Vendor shall, and hereby does, irrevocably assign, sell and transfer to the Client at no cost all of its Intellectual Property Rights and other right, title and interest in or to all such Ontario Materials.

24.8 Ontario Government Insignia

Nothing in this Master Agreement or any Statement of Work or the performance of any Statement of Work shall grant to the Vendor any right, title or interest in or to any Ontario Government Insignia. The Vendor shall not use any Ontario Government Insignia except where required to perform the Services, and only if it has received the express prior written authority of Ontario to do so.

24.9 Ownership of Rights in Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work and Other Work Inventions

Subject to Section 17.2 and Section 17.6, all Intellectual Property Rights in any Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work, and Other Work Inventions, shall immediately, as and when they come into existence, vest in and remain the property of the Client. The Vendor shall have no right in or to any such Intellectual Property Rights in the Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work and Other Work Inventions, except any right that may be granted in writing by the Client. The Vendor hereby irrevocably assigns, sells and transfers to the Client for no additional consideration: (a) all Intellectual Property Rights and all right, title and interest throughout the world in and to the Confidential Work Information, Joint Work Material, Non-Technical Work, Other Work Inventions, and contributions made by any Personnel of the Vendor to any Joint Work Inventions, other than (i) any Intellectual Property Rights or interests in Intellectual Property Rights that came into existence prior to the Project Start Date, and (ii) any Intellectual Property Rights or interests in Intellectual Property Rights in and to such Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work, and Other Work Inventions, assigned, sold and transferred to the Client by the Personnel of the Vendor; and (b) all of the Vendor's right, title and interest in and to each copyright referred to in Section 24.3 and subsection 24.5 (b).

24.10 Assignment by Personnel, Subcontractors and Others

To the extent that any right, title or interest or any Intellectual Property Rights in or to any Confidential Work Information, Joint Work Material, Non-Technical Work, Other Work Inventions or contributions made by any Personnel of the Vendor to any Joint Work Inventions, vest, by operation of law or otherwise, in any of the Vendor's advisors, agents, Personnel, Subcontractors, suppliers or others for whom the Vendor is responsible at law, the Vendor shall cause each of them to assign and transfer to the Client at no cost all of such right, title and interest and all of such Intellectual Property Rights other than any Intellectual Property Rights or interests in Intellectual Property Rights that came into existence prior to the Project Start Date.

24.11 Intellectual Property Rights Applications

The Vendor shall, at the Client's expense, give the Client all reasonable assistance in the preparation and the prosecution of any applications or registrations in any jurisdiction for or of any Intellectual Property Rights on or arising out of any Joint Work Inventions, Joint Work Material, Non-Technical Work, and Other Work Inventions, including the assistance of the inventors in the case of patent applications on any Joint Work Inventions and Other Work Inventions.

24.12 Further Assurances

The Vendor shall, at its own expense, promptly do any and all acts and cause to be executed and deliver to the Client any and all assignments, documents and instruments relating to the Intellectual Property Rights in the Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work, and Other Work Inventions, which Ontario or the OPS Entity may reasonably request at any time or from time to time to carry out the intent of this Article.

24.13 Power of Attorney

If the Client is unable for any reason whatsoever to secure the Vendor's signature to any document assigning, perfecting, recording or acknowledging the Client's ownership of any Confidential Work Information, Joint Work Inventions, Joint Work Material, Non-Technical Work, or Other Work Inventions, the Vendor hereby irrevocably designates and appoints the Client and its duly authorized officers as its attorneys-in-fact, with full power of

substitution, to act for and on behalf of and instead of the Vendor to execute and file any such document and to do all lawfully permitted acts to further the purposes of this Section with the same legal force and effect as if executed by the Vendor.

24.14 Intellectual Property Notice

The Vendor shall incorporate the following intellectual property notice on all Confidential Work Information, Joint Work Material, Non-Technical Work, Other Work Inventions and contributions made by any Personnel of the Vendor to any Joint Work Inventions, in all forms and however recorded:

(a) where the Client is Ontario, or where the Client is an OPS Entity to which Section 25.1 of this Attachment D applies:

Intellectual Property Notice

© Queen's Printer for Ontario, [Instructions: insert year of publication.].

Her Majesty the Queen in right of Ontario holds intellectual property rights, including rights of confidentiality, in this [Instructions: select one or more, as applicable: documentation / information / material / software].

(b) where the Client is an OPS Entity (except where Section 25.1 of this Attachment D applies):

Intellectual Property Notice

© [Instructions: Insert name of the OPS Entity], [Instructions: insert year of publication.].

[Instructions: Insert name of the OPS Entity] holds intellectual property rights, including rights of confidentiality, in this [Instructions: select one or more, as applicable: documentation / information / material / software].

24.15 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 25. OPS ENTITIES NOT CAPABLE OF HOLDING INTELLECTUAL PROPERTY RIGHTS

25.1 OPS Entities Not Capable of Holding Intellectual Property Rights

Despite any provision in the Master Agreement or any Statement of Work to the contrary, if an OPS Entity is not capable under its constituting instrument to hold Intellectual Property Rights, in respect to each Statement of Work entered into by a Client that is such an OPS Entity, Ontario and the Vendor agree that: (a) any Intellectual Property Rights assigned, sold or transferred to, owned or retained by, or otherwise conveyed to, such OPS Entity as the "Client" under the Statement of Work shall be deemed to be assigned, sold or transferred to, owned or retained by, or otherwise conveyed to, Ontario; (b) any licences granted to such OPS Entity as the "Client" under the Statement of Work shall, in addition to being granted to such OPS Entity, be granted separately to Ontario, subject to the same rights, benefits, obligations and restrictions, except that Ontario may also exercise the licence rights on behalf of such OPS Entity and to have and permit others to do so; and (c) the provisions of this Master Agreement shall apply with the necessary changes to reflect the intention of this Section.

ATTACHMENT E TO MASTER AGREEMENT – CLIENT OWNERSHIP PROVISIONS

1.2 In respect of each Statement of Work to which this Attachment E applies, these words and expressions have these meanings:

"**Confidential Work Information**" means all information that (a) is confidential by its nature or in the circumstances in which it is conceived, developed or produced, and (b) is conceived, developed or produced by one or more of the Personnel of the Vendor in the performance of Work, whether with one or more of the Personnel of the Client or not. "Confidential Work Information" includes all Joint Work Material, Joint Work Inventions and Vendor Work Inventions.

"**Newly-Created Materials**" means the Deliverables (including all components of the Deliverables), but excluding the Vendor Materials.

"**Restricted Commercialization**" means exploitation of Intellectual Property Rights in Vendor Materials, which are incorporated into the Deliverables, for any commercial advantage in competition with the Vendor with the effect of making a net monetary gain, but does not include: (a) any exploitation by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work where the good or service developed or produced through such exploitation is for use by the Client, its sublicensees, Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, Provincially Funded Organizations, or the public, including any dissemination or distribution in connection with such exploitation, or (b) any dissemination or distribution by or on behalf of the Client or its sublicensees for the purposes permitted under this Master Agreement or the Statement of Work.

"**Vendor Work Information**" means: (a) Technical Information, developed or produced by the Vendor or its Subcontractors in the performance of Work under a Statement of Work, developed or produced by the Vendor or its Subcontractors in the performance of Work under that Statement of Work; and (b) any contribution made by one or more of the Personnel of the Vendor to any Joint Work Material; but excludes all Client Work Information.

"**Vendor Work Invention**" means: (a) any Invention conceived, or conceived and developed, solely or jointly by one or more of the Personnel of the Vendor in the performance of Work; and (b) any contribution made by one or more of the Personnel of the Vendor to any Joint Work Invention.

ARTICLE 16. OWNERSHIP OF RIGHTS

16.1 Ownership of Rights in Newly-Created Materials and Inventions

Without affecting any Intellectual Property Rights or other interests in or to Ontario Data, and subject to Section 16.2 and Section 16.5, all Intellectual Property Rights in:

(a) the Newly-Created Materials; and

(b) Vendor Work Inventions and Joint Work Inventions;

shall immediately, as and when they come into existence, vest in and remain the property of the Client. The Vendor shall have no right in or to any such Intellectual Property Rights in the Newly-Created Materials, Vendor Work Inventions and Joint Work Inventions, except any right that may be granted in writing by the Client.

16.2 Pre-Existing Intellectual Property Rights

All Intellectual Property Rights existing immediately prior to the Project Start Date, and all rights to Inventions first conceived, developed or reduced to practice prior to such date, shall be retained by each Party and each third party that owned such rights immediately prior to such date.

16.3 Intellectual Property Notice

The Vendor shall incorporate the following intellectual property notice on all Newly-Created Materials, in all forms and however recorded:

(a) where the Client is Ontario, or where the Client is an OPS Entity to which Section 17.1 of this Attachment E applies:

> **Intellectual Property Notice**
>
> © Queen's Printer for Ontario, [Instructions: insert year of publication.].
>
> Her Majesty the Queen in right of Ontario holds intellectual property rights, including rights of confidentiality, in this [Instructions: select one or more, as applicable: documentation / information / material / software].

(b) where the Client is an OPS Entity (except where Section 17.1 of this Attachment E applies):

> **Intellectual Property Notice**
>
> © [Instructions: Insert name of the OPS Entity], [Instructions: insert year of publication.].
>
> [Instructions: Insert name of the OPS Entity] holds intellectual property rights, including rights of confidentiality, in this [Instructions: select one or more, as applicable: documentation / information / material / software].

16.4 Ownership of Tangible Materials

The Client shall own, and have unrestricted ownership rights in, all tangible materials as and when delivered by the Vendor to the Client in connection with the Statement of Work. The Vendor hereby irrevocably assigns, sells and transfers, and it shall be a term of the Statement of Work that the Vendor irrevocably assigns, sells and transfers, all right, title and interest in and to such tangible materials to the Client at no additional cost as and when delivered. The Vendor shall, at its own expense, promptly do any and all acts and cause to be executed and deliver to the Client any and all assignments, documents and instruments that the Client may reasonably request at any time or from time to time to carry out the intent of this Section.

16.5 Vendor Trademarks and Designations

Despite any other provisions of this Master Agreement, nothing in this Master Agreement or in a Statement of Work or the performance of the Statement of Work shall grant to the Client any right, title, interest or licence in or to the names, trade names, logos, trade dress, or other trademarks or designations of the Vendor, its Subcontractors or third-party licensors, except as expressly stated in the Statement of Work.

16.6 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 17. OPS ENTITIES NOT CAPABLE OF HOLDING INTELLECTUAL PROPERTY RIGHTS

17.1 OPS Entities Not Capable of Holding Intellectual Property Rights

Despite any provision in the Master Agreement or any Statement of Work to the contrary, if an OPS Entity is not capable under its constituting instrument to hold Intellectual Property Rights, in respect to each Statement of Work entered into by a Client that is such an OPS Entity, Ontario and the Vendor agree that: (a) any Intellectual Property Rights assigned, sold or transferred to, owned or retained by, or otherwise conveyed to, such OPS

Entity as the "Client" under the Statement of Work shall be deemed to be assigned, sold or transferred to, owned or retained by, or otherwise conveyed to, Ontario; (b) any licences granted to such OPS Entity as the "Client" under the Statement of Work shall, in addition to be granted to such OPS Entity, be granted separately to Ontario, subject to the same rights, benefits, obligations and restrictions, except that Ontario may also exercise the licence rights on behalf of such OPS Entity and to have or permit others to do so; and (c) the provisions of this Master Agreement shall apply with the necessary changes to reflect the intention of this Section.

ARTICLE 18. ASSIGNMENTS OF RIGHTS TO NEWLY-CREATED MATERIALS AND INVENTIONS

18.1 Assignment

The Vendor hereby irrevocably assigns, sells and transfers to the Client, and it shall be a term of each Statement of Work that the Vendor irrevocably assigns, sells and transfers to the Client, for no additional consideration:

(a) all Intellectual Property Rights and all right, title and interest throughout the world in and to:

(i) the Newly-Created Materials; and

(ii) Vendor Work Inventions and Joint Work Inventions; and

(b) all of the Vendor's right, title and interest in and to each copyright referred to in Section 22.3 and Section 22.5.

18.2 Assignment by Personnel, Subcontractors and Others

To the extent that any right, title or interest or any Intellectual Property Rights in or to any Newly-Created Materials, Vendor Work Inventions and Joint Work Inventions or in or to any copyright referred to in Section 22.3 or subsection 22.5, vest, by operation of law or otherwise, in any of the Vendor's directors, officers, Personnel, advisors, agents, partners, affiliates, volunteers, Subcontractors, suppliers, or others for whom the Vendor is responsible at law, the Vendor shall cause each of them to assign and transfer to the Client at no cost all of such right, title and interest and all of such Intellectual Property Rights.

18.3 Assignee and Form of Copyright Assignment

Written assignments of any Intellectual Property Rights: (a) to Ontario shall be to "Her Majesty the Queen in right of Ontario", but written assignments of any copyright shall be to the "Queen's Printer for Ontario" in the form set out in Attachment F, and in such form that is satisfactory to the Client where the assignor is not a corporation; or (b) to the OPS Entity shall be in the name of the OPS Entity and, where the Intellectual Property Right is copyright, the written assignment of copyright shall be in the form set out in Attachment F, or in such form that is satisfactory to the Client where the assignor is not a corporation. At the completion of the Services under each Statement of Work or upon the termination of the Statement of Work, the Vendor shall provide to the Client an original, executed assignment of copyright in the form set out in Attachment F, as modified if necessary as set out above.

18.4 Waiver of Moral Rights

The Vendor acknowledges and agrees that all Moral Rights with respect to the Deliverables under each applicable Statement of Work shall be waived irrevocably and without restriction by each of its Personnel in favour of Her Majesty the Queen in right of Ontario and all of its ministries and other administrative units over which ministers of Ontario preside, including its agencies, boards, commissions, and Crown corporations, all offices of the officers of the Legislative Assembly or of the Ontario Legislature, OPS Entities, and all sublicensees and assignees, and all persons authorized at any time to use the Deliverables. At the completion of the Services under each Statement of Work or upon the termination of the Statement of Work, the Vendor shall obtain from each of its Personnel an original, executed waiver of Moral Rights in the form attached as

Attachment G (Waiver of Moral Rights Form) and shall deliver such waiver to the Client upon the request of the Client.

18.5 Invention Disclosure

Prior to allowing any Person to perform Services under the Statement of Work, the Vendor shall, by written agreement, require such Person to agree,

(a) to promptly report and fully disclose in writing to the Vendor each Vendor Work Invention and Joint Work Invention, identifying those concepts or ideas thought to be new, useful and unobvious, and indicating whether they are thought to be an improvement on prior art or capable of commercial exploitation; and

(b) upon request, during and after employment, to execute all assignments, documents and instruments necessary or advantageous to file patent applications on Vendor Work Inventions and Joint Work Inventions and to establish the Client's rights in the Vendor Work Inventions and Joint Work Inventions.

18.6 Disclosure to Client

The Vendor shall promptly report and fully disclose in writing to the Client all Deliverables, as well as all Vendor Work Inventions and Joint Work Inventions. The Vendor's disclosure shall include a description of the specific components of the Deliverables (including all Newly Created Materials (including all Confidential Work Information, Joint Work Materials, Vendor Work Information), Vendor Materials and Ontario Materials) and all contributions made by the Personnel of the Vendor to any Vendor Work Inventions and Joint Work Inventions, including copies of all written disclosures submitted to the Vendor pertaining to them, in sufficient detail to permit the Client to clearly identify each such component and to distinguish them from the other components. Disclosure of Joint Work Inventions and Vendor Work Inventions shall be on the form set out in Attachment I. In any event, the Vendor shall make such disclosure not later than the time of completion of the Services or such earlier time as the Client or the Statement of Work may require.

18.7 Audit Rights

During the Project Term and for seven (7) years following the termination or expiry of each Statement of Work, the Client shall have the right to examine and make copies of all records and supporting data of the Vendor which the Client reasonably deems pertinent to the identification of each component of the Deliverables (including all Newly Created Materials (including all Confidential Work Information, Joint Work Materials, Vendor Work Information), Vendor Materials and Ontario Materials) and all contributions made by the Personnel of the Vendor to any Vendor Work Inventions and Joint Work Inventions, upon reasonable notice and with no more than minimal disruption to the Vendor's ongoing operations, and the Vendor shall, at its own cost, retain and maintain in an organised, accessible mode, all such records and supporting data for such period.

18.8 Intellectual Property Rights Applications

The Vendor shall, at the Client's expense, give the Client all reasonable assistance in the preparation and the prosecution of any applications or registrations in any jurisdiction for or of any Intellectual Property Rights on or arising out of the Newly Created Materials, including Joint Work Inventions and Vendor Work Inventions, including the assistance of the inventors in the case of patent applications on any Vendor Work Inventions and Joint Work Inventions.

18.9 Further Assurances

The Vendor shall, at its own expense, promptly do any and all acts and cause to be executed and deliver to the Client any and all assignments, documents and instruments relating to the Intellectual Property Rights in the Newly-Created Materials, Joint Work Inventions and Vendor Work Inventions, which the Client may reasonably request at any time or from time to time to carry out the intent of this Article and Article 16.

18.10 Power of Attorney

If the Client is unable for any reason whatsoever to secure the Vendor's signature to any document assigning, perfecting, recording or acknowledging the Client's ownership of any Newly-Created Materials (including copyright in Joint Work Materials and collective works), Joint Work Inventions, or Vendor Work Inventions, the Vendor hereby irrevocably designates and appoints the Client and its duly authorized officers as its attorneys-in-fact, with full power of substitution, to act for and on behalf of and instead of the Vendor to execute and file any such document and to do all lawfully permitted acts to further the purposes of this Section with the same legal force and effect as if executed by the Vendor.

18.11 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 19. VENDOR MATERIALS

19.1 Request for Consent

The Parties acknowledge that from time to time, the Vendor may wish to incorporate Vendor Materials into the Deliverables .Prior to incorporating any Vendor Materials into any Deliverables, the Vendor shall:

(a) fully disclose to the Client in writing all Vendor Materials that the Vendor proposes to incorporate, which shall include a description of the specific components in sufficient detail to permit the Client to clearly identify and to distinguish them from the Newly-Created Materials and the Ontario Materials; and

(b) obtain the Client's prior written consent to such incorporation or use, which consent shall be in the sole discretion of the Client and subject to the terms and conditions as agreed to by the Client as set out in the Statement of Work or Change Order.

19.2 Subcontractors

If any applicable Intellectual Property Rights are owned by a Subcontractor or are licensed to the Subcontractor by a related person, the Vendor shall either obtain a licence from that Subcontractor that permits compliance with Sections 19.4, 20.1 and 20.2 or arrange for the Subcontractor to convey directly to the Client the same rights by execution of the form provided for that purpose by the Client, in which case the Vendor shall deliver that form to the Client, duly completed and executed by the Subcontractor, no later than the time of disclosure to the Client of those Vendor Materials.

19.3 Ownership of Vendor Materials

As between the Client and the Vendor, the Vendor shall have and continue to retain all right, title and interest, including all Intellectual Property Rights, in and to all Vendor Materials, except as otherwise set out in this Master Agreement or the Statement of Work. The Client shall not acquire by virtue of this Master Agreement or the Statement of Work any right, title or interest, including any Intellectual Property Rights, in or to any Vendor Materials, except as otherwise set out in the Statement of Work or this Master Agreement.

19.4 Licence to Vendor Materials Incorporated into Deliverables

It is a provision of each Statement of Work that the Vendor hereby grants to the Client a non-exclusive, perpetual, irrevocable, world-wide, fully paid-up, royalty-free licence to exercise all Intellectual Property Rights in the Vendor Materials that are incorporated into any Deliverables, in any way and for any purpose whatsoever except Restricted Commercialization, and to have or permit others to do so. Solely by way of example, the licence granted to the Client above includes the right to use, reproduce, produce any translation, improve, and disclose, and includes the right to sublicense Ontario, OPS Entities, any office of an officer of the Legislative

Assembly or of the Ontario Legislature, Provincially Funded Organizations, other governments and their agencies and other public bodies.

The licence set out in this Section is non-transferable by the Client except that: (1) if the Client is Ontario, the Client may transfer the licence to a Permitted OPS Assignee; and (2) if the Client is an OPS Entity, the Client may transfer the licence to Ontario or where such transfer is necessitated by outsourcing, privatizing, partnering or similar activity, to a non-governmental entity.

19.5 Vendor Materials and Third-Party Contractors

The Vendor acknowledges that the Client may wish to enter into contracts with one or more third parties in respect of the licence rights set out in Section 19.4, whether by a competitive process or not. Without restricting the generality of Section 19.4, the Vendor agrees that the licence granted in relation to the Intellectual Property Rights in the Vendor Materials includes the right to disclose the Vendor Materials to such third parties and to any actual and potential proponents for such contracts, and to sublicense or otherwise authorize any such third parties engaged to do anything solely on behalf of the Client that the Client may do with the Vendor Materials and the Intellectual Property Rights in the Vendor Materials. The Client shall require actual and potential proponents and such third parties not to use or disclose any confidential Vendor Materials incorporated into the Deliverables except as may be necessary to bid for or to carry out any such contracts or except if required by order of a court or tribunal.

19.6 Title to Improvements and Modifications to Vendor Materials

All Intellectual Property Rights arising from any further development or modification of the Vendor Materials that is conceived, developed, effected or first reduced to practice by or for the Client in the exercise of any licence set out in Section 19.4 shall vest in the Client, or as the Client directs, and shall not vest in the Vendor, its Personnel or Subcontractors except pursuant to a subsequent written contract executed by the Client and the Vendor, its Personnel or Subcontractors, as the case may be.

19.7 Vendor Material IP Notice

The Client shall not, without the prior written consent of the Vendor which shall not be unreasonably withheld, remove any intellectual property notices of the Vendor or of the Vendor's Subcontractors on any Vendor Materials.

19.8 Third-Party Vendor Materials Incorporated into the Deliverables

In the case of any Third-Party Vendor Materials that are incorporated into the Deliverables, the Client shall be entitled, at its option, to assume from the Vendor all of its rights to such Third-Party Vendor Materials under any licence and other agreements, and the Vendor shall ensure that any such agreements permitting their assignment and transfer to the Client or as the Client directs, and that such assignment and transfer shall be at no charge to the Client but the Client shall be responsible for any ongoing licence or other payments required to be made to any third parties under any such agreements. If such agreement is not acceptable to the Client, the Vendor will use commercially reasonable efforts to facilitate the Client's pursuit of an acceptable agreement with the relevant third party.

19.9 Third-Party Vendor Materials Used Non-Exclusively

In the case of any Third-Party Vendor Materials that are used in connection with the Services performed for the Client but are also used by the Vendor in connection with services provided by it to others or for the internal purposes of the Vendor not connected with this Master Agreement, upon request by the Client, the Vendor shall assist the Client to acquire a licence to such materials or to acquire from some other person a licence to materials that are functionally/substantively equivalent to such materials. Such licence shall contain terms and conditions as are reasonably acceptable to the Client to enable the Client to obtain or to use the Third-Party Vendor Materials or replacements therefor. The Client shall be responsible for any fees payable to the third-party licensor after such acquisition.

19.10 General

Without limiting any of Sections 19.4 or 19.5, Ontario's rights under this Article:

(a) apply despite any terms to the contrary in any click-wrap licence, documentation (including technical manuals or technical specifications), invoice, shrink-wrap licence, Technical Information, web site, or in any other terms or licence attached to or delivered by the Vendor with any Deliverables, except to the extent that the Client has agreed in writing pursuant to subsection (b) of Section 19.1;

(b) include the right to reproduce and use Vendor Materials incorporated into any Deliverables, and any developed or modified form of them, on any and all computer systems owned, leased or operated by Ontario or the OPS (including OPS Entities) anywhere in the world at any time; and

(c) are in addition to and not in lieu of its rights under any other provisions of this Master Agreement or the Statement of Work.

19.11 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 20. SPECIFIC THIRD-PARTY SUBLICENSEES

20.1 Provincially Funded Organizations

Without restricting Section 19.4, the Vendor agrees that the Client's licence rights under a Statement of Work in relation to the Intellectual Property Rights in the Vendor Materials incorporated into any Deliverables include the right to disclose such Vendor Materials to any Provincially Funded Organizations, and to sublicense or otherwise authorize the Provincially Funded Organization to exercise the licence rights granted under the Statement of Work. Such disclosure of Vendor Materials incorporated into any Deliverables shall be limited and subject to obligations of confidentiality.

20.2 Third-Party Non-Governmental Entities

Without restricting Sections 19.4 and 19.5, the Vendor agrees that the Client's licence rights under a Statement of Work in relation to the Intellectual Property Rights in the Vendor Materials incorporated into any Deliverables include the right to disclose such Vendor Materials to any third-party non-governmental entities that provide services to or on behalf of the Client as a result of alternative service delivery, backward or forward integration, outsourcing, privatization, partnering, procurement endeavours or similar activity, and to sublicense or otherwise authorize such third-party non-governmental entities to exercise the licence rights granted to the Client under the Statement of Work to the extent that they are exercised for or on behalf of the Client. The Client shall require such third-party non-governmental entities not to use or disclose any confidential Vendor Materials incorporated into the Deliverables except as may be necessary to provide services to or on behalf of the Client as contemplated in this Section.

20.3 Patent Licences

To the extent necessary for the Client to exercise any licence granted under a Statement of Work, it is a provision of each Statement of Work that the Vendor hereby grants to the Client a licence under any patent now held or later obtained by the Vendor (or a sub-licence under any patent now held or later obtained by its Subcontractors). Such patent licence shall be co-extensive and co-terminus with such licence. Nothing contained in this Article or in Article 16 shall be deemed to grant to the Vendor any rights with respect to any Inventions, including any Vendor Work Inventions, Joint Work Inventions, and Client Work Inventions.

20.4 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 21. PERSONAL KNOWLEDGE, SKILL AND EXPERTISE, AND GENERIC CONCEPTS, IDEAS AND KNOW-HOW

21.1 Personal Knowledge, Skill and Expertise

Each Party understands and agrees that each of the Personnel of the other Party, in connection with the performance of this Master Agreement or a Statement of Work, may acquire Personal Knowledge. Subject to Article 26, Article 28, the Privacy Provisions and any other statute under which Ontario or the OPS Entity has the discretion or obligation not to disclose any records or other information, the use by such Personnel of the other Party of such Personal Knowledge in the ordinary course of their employment with the other Party (including its subsidiaries, its parent, or other subsidiaries of its parent, in the case of the Vendor; and including Ontario, OPS Entities, offices of an officer of the Legislative Assembly or of the Ontario Legislature, or Provincially Funded Organizations, in the case of Ontario or the OPS Entity; and its Subcontractors) does not breach the Statement of Work provided, however, that nothing in this Section grants to any Personnel the right to obtain a patent in respect of any such Personal Knowledge.

21.2 Employee Mobility

Each Party agrees that the other Party's receipt of confidential information as contemplated by a Statement of Work will not create any obligation in any way limiting or restricting the transfer of Personnel within the other Party's organization.

21.3 Indemnity

Despite the limitations of liability set out in Article 33 (Limitation of Liability), the Vendor shall indemnify and hold harmless the Indemnified Parties from and against all Losses and Proceedings, by whomever made, sustained, incurred, brought or prosecuted, arising out of, or in connection with the use by the Vendor's Personnel of any Personal Knowledge referred to in Section 21.1 (Personal Knowledge, Skill and Expertise) or any concepts, ideas or know-how referred to in Section 21.4 (Use of Generic Concepts, Ideas, or Know-How by Vendor).

21.4 Use of Generic Concepts, Ideas, or Know-How by Vendor

Subject to Article 26 and the Privacy Provisions and any other statute under which Ontario or the OPS Entity has the discretion or obligation not to disclose any records or other information, Ontario and the OPS Entity each acknowledges that the Vendor shall be entitled on a non-exclusive, non-transferable, perpetual, world-wide, irrevocable, fully-paid up, royalty-free basis to use in its business, and for purposes of developing and incorporating into other works and licensing such works to others, any concepts, ideas or know-how, whether patented (or patentable) or not, that are developed or created by the Vendor in the course of providing the Services, and that are not retained by the Vendor in any electronic, optical, printed, written or other recorded form, but only to the extent they are of a generic technical nature and are not specific to the operation and activities of Ontario or the OPS Entity, and only to the extent that they are not protected by the Intellectual Property Rights of any third party, and provided, however, that the rights of the Vendor under this Section do not include the right to obtain a patent in respect of any such concepts, ideas or know-how. The rights of the Vendor under this Section do not include the right to disclose personnel information, financial information, statistical information, business plans or processes, pre-existing code, documentation or any other such information or intellectual property of the OPS.

21.5 Scope

Nothing in this Article grants or waives any Intellectual Property Rights of either Party or any other person.

21.6 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 22. PROPERTY OF ONTARIO AND THE OPS ENTITIES

22.1 Ownership of Ontario Materials and Ontario Data

The Vendor acknowledges that Ontario, the OPS Entity and their respective Subcontractors and third-party licensors shall have and continue to retain all right, title and interest, including all Intellectual Property Rights, in and to all Ontario Materials and Ontario Data, all assets acquired or held by Ontario or the OPS Entity prior to the Project Start Date or during the Project Term of each Statement of Work, and all assets provided by Ontario or the OPS Entity to the Vendor in connection with each Statement of Work. The Vendor shall not acquire by virtue of this Master Agreement, or any Statement of Work, any right, title or interest, including any Intellectual Property Rights, in or to any Ontario Materials and Ontario Data.

22.2 Ownership of Third-Party Ontario Materials

Nothing in this Master Agreement or any Statement of Work or the performance of any Statement of Work shall grant to the Vendor any right, title or interest in or to any Third-Party Ontario Materials. To the extent any right, title or interest in or to any Third-Party Ontario Materials vests, by operation of law or otherwise, in the Vendor (or its Personnel, Subcontractors or others for whom it is responsible at law), the Vendor shall, and hereby does, irrevocably assign and transfer to the Client at no cost all of its right, title and interest in and to all such Third-Party Ontario Materials, and the same shall be deemed to form part of the Ontario Materials.

22.3 Works of Joint Authorship

Subject to Section 16.2 and Section 19.3, if any Newly-Created Materials or any portion thereof (such as the Joint Work Material) is a work of joint authorship, the copyright in the work of joint authorship shall immediately, as soon as it comes into existence, vest in the Client, and the Vendor and its Subcontractors shall have no right, title or interest in or to it.

22.4 Proscribed Intellectual Property Rights Registrations

The Vendor shall not file any application, and shall not contest any application filed by Ontario or any OPS Entity, in any jurisdiction for the registration of any Intellectual Property Rights arising out of any Newly-Created Materials (including any Client Work Information, Vendor Work Information and Joint Work Materials), Ontario Materials, Client Work Inventions, Vendor Work Inventions or Joint Work Inventions, whether or not such Intellectual Property Rights depend or would depend upon any pre-existing Intellectual Property Rights.

22.5 Collective Works and Compilations

Despite any other provision in this Master Agreement or the Statement of Work, if any Newly-Created Materials or any portion thereof is a collective work or a compilation:

(a) the Client shall retain its right, title and interest in and to its contribution to such collective work or compilation;

(b) ownership of all right, title and interest in and to the Vendor's and its Subcontractors' contributions to such collective work or compilation shall be governed by Section 16.1; and

(c) the copyright in such collective work or compilation shall immediately, as soon as it comes into existence, vest in the Client, and the Vendor and its Subcontractors shall have no right, title or interest in or to it.

22.6 Client Work Inventions and Client Work Information

The Client retains all of its Intellectual Property Rights and all of its right, title, and interest throughout the world to each Client Work Invention and to all Client Work Information.

22.7 Intellectual Property Rights to Ontario Materials

To the extent any Intellectual Property Rights or any other right, title or interest in or to any Ontario Materials vests, by operation of law or otherwise, in the Vendor (or its directors, officers, Personnel, agents, partners, affiliates, volunteers or Subcontractors or others for whom it is responsible at law), the Vendor shall, and hereby does, irrevocably assign, sell and transfer to the Client at no cost all of its Intellectual Property Rights and other right, title and interest in or to all such Ontario Materials.

22.8 Ontario Government Insignia

Nothing in this Master Agreement or any Statement of Work or the performance of any Statement of Work shall grant to the Vendor any right, title or interest in or to any Ontario Government Insignia. The Vendor shall not use any Ontario Government Insignia except where required to perform the Services, and only if it has received the express prior written authority of Ontario to do so.

22.9 Survival

The provisions of this Article shall survive the termination or expiry of this Master Agreement and of every Statement of Work.

ARTICLE 23. [INTENTIONALLY LEFT BLANK]

ARTICLE 24. [INTENTIONALLY LEFT BLANK]

ARTICLE 25. [INTENTIONALLY LEFT BLANK]

ATTACHMENT F TO MASTER AGREEMENT - ASSIGNMENT OF COPYRIGHT

NOTE: THIS NOTE AND ALL INSTRUCTIONS CONTAINED IN THIS DOCUMENT ARE INTENDED ONLY AS GUIDES AND SHOULD BE DELETED.

A. Form of Assignment of Copyright – Ministries and Certain OPS Entities

[Instructions: The template below is to be used by: (1) a ministry; or (2) any OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies. At least one fully completed and signed assignment of copyright under each Statement of Work must be signed by the Vendor upon the completion of the performance of all Services and delivery of all Deliverables under the Statement of Work. The Vendor must submit it promptly to the Client Representative.]

ASSIGNMENT OF COPYRIGHT

THIS ASSIGNMENT is made in duplicate as of **[Instructions: insert date]**.

Ontario and **[Instructions: Insert legal name of the Vendor]** (the "Vendor") entered into a Master Agreement for Management Consulting Services, dated **[Insert Date]**, reference number OSS-0042661 (the "Master Agreement"), pursuant to a Request for Proposals for Management Consulting Services issued by the Minister of Government Services. All terms with initial capital letters used in this Assignment of Copyright without definition shall have the meaning ascribed to them in the Master Agreement.

In consideration of **[Instructions: If a ministry entered into the Statement of Work on behalf of Ontario, insert "Her Majesty the Queen in right of Ontario as represented by", and identify the minister that signed the Statement of Work on behalf of Ontario; insert "the Minister of" and name the applicable ministry, and in the case of the Ministry of the Attorney General, insert "the Attorney General". If an OPS Entity to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies entered into the Statement of Work, set out the appropriate name of the OPS Entity here.]** entering, pursuant to the Master Agreement, into an agreement with the undersigned, entitled **[Instructions: insert title of the Statement of Work]**, dated **[Instructions: insert date]**, 20**[Instructions: complete year]**, reference number **[Instructions: insert reference number]** (the "Statement of Work"), the undersigned agreed to assign and now does assign and transfer unto the Queen's Printer for Ontario: (a) each and every copyright and interest in copyright in Canada and throughout the known universe in and to: (i) if Attachment D (Vendor/Client Ownership Provisions) applies to the Statement of Work, Confidential Work Information, Joint Work Materials, Joint Work Inventions, Non-Technical Work and Other Work Inventions and, where the Statement of Work is terminated in accordance with Section 18.1 (Assignment on Default), Vendor Work Inventions and Vendor Work Information; or (ii) if Attachment E (Client Ownership Provisions) applies to the Statement of Work, Newly Created Materials, Joint Work Inventions and Vendor Work Inventions; and (b) all of the Vendor's right, title and interest in and to each copyright referred to in: (i) if Attachment D applies to the Statement of Work, Section 24.3 (Works of Joint Authorship) and subsection 24.5(c) (Collective Works and Compilations) of the Master Agreement; or (ii) if Attachment E (Client Ownership) applies to the Statement of Work, Section 22.3 (Works of Joint Authorship) and subsection 22.5(c) (Collective Works and Compilations) of the Master Agreement.

Without limiting the generality of the foregoing and for certainty, the foregoing and the documents that record the Inventions, include, but are not limited to: **[Instructions: Identify each applicable component of the Deliverable listed in above (a) or (b) above based on whether Attachment D or Attachment E applies and document that records the applicable Joint Work Inventions, Other Work Inventions and Vendor Work Inventions.]**

IN WITNESS WHEREOF the undersigned has executed this Assignment.

[Instructions: Insert legal name of the Vendor]

Per:

Signature: _____

Name: _____

Title: _____

I have authority to bind the Vendor.

B. Form of Assignment of Copyright – OPS Entities (other than OPS Entities to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies)

[Instructions: The template below is to be used by an OPS Entity (other than OPS Entities to which Section 25.1 of Attachment D or Section 17.1 of Attachment E applies). At least one fully completed and signed assignment of copyright under each Statement of Work must be signed by the Vendor upon the completion of the performance of all Services and delivery of all Deliverables under the Statement of Work. The Vendor must submit it promptly to the Client Representative.]

ASSIGNMENT OF COPYRIGHT

THIS ASSIGNMENT is made in duplicate as of **[Instructions: insert date]**.

Ontario and **[Instructions: Insert legal name of the Vendor]** (the "Vendor") entered into a Master Agreement for Management Consulting Services, dated **[Insert Date]**, reference number OSS-00426611 (the "Master Agreement"), pursuant to a Request for Proposals for Management Consulting Services issued by the Minister of Government Services. All terms with initial capital letters used in this Assignment of Copyright without definition shall have the meaning ascribed to them in the Master Agreement.

In consideration of **[Instructions: Set out the appropriate name of the OPS Entity here.]** entering, pursuant to the Master Agreement, into an agreement with the undersigned, entitled **[Instructions: insert title of the Statement of Work]**, dated **[Instructions: insert date]**, 20**[Instructions: complete year]**, reference number [Instructions: insert reference number] (the "Statement of Work"), the undersigned agreed to assign and now does assign and transfer unto the **[Instructions: Set out the appropriate name of the OPS Entity here.]**: (a) each and every copyright and interest in copyright in Canada and throughout the known universe in and to: (i) if Attachment D (Vendor/Client Ownership Provisions) applies to the Statement of Work, Confidential Work Information, Joint Work Materials, Joint Work Inventions, Non-Technical Work and Other Work Inventions, and, where the Statement of Work is terminated in accordance with Section 18.1 (Assignment on Default), Vendor Work Inventions and Vendor Work Information; or (ii) if Attachment E (Client Ownership Provisions) applies to the Statement of Work, Newly Created Materials, Joint Work Inventions and Vendor Work Inventions; and (b) all of the Vendor's right, title and interest in and to each copyright referred to in: (i) if Attachment D applies to the Statement of Work, Section 24.3 (Works of Joint Authorship) and subsection 24.5(c) (Collective Works and Compilations) of the Master Agreement; or (ii) if Attachment E (Client Ownership) applies to the Statement of Work, Section 22.3 (Works of Joint Authorship) and subsection 22.5(c) (Collective Works and Compilations) of the Master Agreement.

Without limiting the generality of the foregoing and for certainty, the foregoing and the documents that record the Inventions, include, but are not limited to: **[Instructions: Identify each applicable component of the Deliverable listed in above (a) or (b) above based on whether Attachment D or Attachment E applies and document that records the applicable Joint Work Inventions, Other Work Inventions and Vendor Work Inventions.]**

IN WITNESS WHEREOF the undersigned has executed this Assignment.

[Instructions: Insert legal name of the Vendor]

Per:

Signature: _____

Name: _____

Title: _____

I have authority to bind the Vendor.

ATTACHMENT G TO MASTER AGREEMENT – WAIVER OF MORAL RIGHTS

NOTE: THIS NOTE AND ALL INSTRUCTIONS CONTAINED IN THIS DOCUMENT ARE INTENDED ONLY AS GUIDES AND SHOULD BE DELETED.

WAIVER OF MORAL RIGHTS

THIS WAIVER OF MORAL RIGHTS is made in duplicate.

Her Majesty the Queen in right of Ontario as represented by the Minister of Government Services and **[Instructions: Insert legal name of the Vendor.]** (the "Vendor") entered into a Master Agreement for Management Consulting Services, dated **[insert date]**, reference number OSS-00426611 (the "Master Agreement").

Pursuant to the Master Agreement, **[Instructions: If a ministry entered into the Statement of Work on behalf of Ontario, insert "Her Majesty the Queen in right of Ontario as represented by", and identify the minister that signed the Statement of Work on behalf of Ontario; insert "the Minister of" and name the applicable ministry, and in the case of the Ministry of the Attorney General, insert "the Attorney General". If an OPS Entity entered into the Statement of Work, set out the appropriate name of the OPS Entity here.]** (the "Client") and the Vendor entered into a statement of work dated **[Instructions: insert date]**, reference number **[Instructions: insert reference number]** (the "Statement of Work").

The Vendor agreed to cause each and every individual who is assigned by the Vendor to perform services for the Client, pursuant to the Statement of Work, to execute this Waiver of Moral Rights.

I, **[Instructions: insert the full legal name of the individual.]**, an author of any or all of the Deliverables, as this term is defined in the Master Agreement, hereby expressly, irrevocably and without restriction, waive all my Moral Rights with respect to all Deliverables in favour of Her Majesty the Queen in right of Ontario and all of its ministries and other administrative units over which ministers of Ontario preside, including without limitation Ontario and Ontario's agencies, boards, commissions, and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature, the OPS Entities, and all sublicensees and assignees, and all persons authorized at any time to use the Deliverables.

In this Waiver of Moral Rights, "Moral Rights" has the same meaning as in the Copyright Act, R.S.C. 1985, c. C-42, as amended or replaced from time to time, and includes comparable rights in applicable jurisdictions, and includes without limitation the right of attribution of authorship, the right to restrain any distortion, mutilation or other modification of any work and the right to prohibit any use of any work in association with a product, service, cause or institution that may be prejudicial to my honour or reputation.

IN WITNESS WHEREOF I have executed this Waiver of Moral Rights.

[INSTRUCTIONS: INSERT THE FULL LEGAL NAME OF THE INDIVIDUAL.]

Signature: _____

Date: _____

Address: _____

_____

ATTACHMENT H TO MASTER AGREEMENT - CONFIDENTIALITY AGREEMENT

NOTE: THIS NOTE AND ALL INSTRUCTIONS CONTAINED IN THIS DOCUMENT ARE INTENDED ONLY AS GUIDES AND SHOULD BE DELETED.

Confidentiality Agreement

During and following the term of the Master Agreement for Management Consulting Services effective **[insert effective date]** between **[Instructions: insert name of Vendor.]** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the Minister of Government Services, (the "Master Agreement") and during and following the term of each Statement of Work entered into by the Vendor and **[Instructions: If a ministry entered into the Statement of Work on behalf of Ontario, insert "Her Majesty the Queen in right of Ontario as represented by", and identify the minister that signed the Statement of Work on behalf of Ontario; insert "the Minister of" and name the applicable ministry, and in the case of the Ministry of the Attorney General, insert "the Attorney General". If an OPS Entity entered into the Statement of Work, set out the appropriate name of the OPS Entity here.]** (the "Client") pursuant to the Master Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and OPS Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the Freedom of Information and Protection of Privacy Act ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: _____ Signature: _____
Date: _____

Witness: _____ Signature: _____
Date: _____

ATTACHMENT I TO MASTER AGREEMENT - INVENTION DISCLOSURE FORM

INVENTION DISCLOSURE FORM

Confidential - This form contains scientific, technical and commercial information and trade secrets that are provided in confidence to Her Majesty the Queen in right of Ontario or the OPS Entity.

Statement by the Vendor		
Name of Vendor	**Business Mailing Address**	**Business Telephone Number**

Identify the applicable contract/statement of work with Ontario or OPS Entity under which the invention was conceived, developed or first reduced to practice		
Title of Contract/Statement of Work	**Ministry signing on behalf of Ontario; or OPS Entity**	**Date of Contract/Statement of Work**

Is the invention or any part of it being further developed under the contract/statement of work?	**Will the invention or any part of it be further developed under the contract/statement of work?**
Yes q No q	Yes q No q

If the answer to either of the questions above is "Yes", and the development is being made or will be made by a subcontractor, complete the following.

Name of Subcontractor No. 1	**Business Mailing Address**	**Business Telephone Number**	**Contact Name**
Name of Subcontractor No. 2	**Business Mailing Address**	**Business Telephone Number**	**Contact Name**
Name of Subcontractor No. 3	**Business Mailing Address**	**Business Telephone Number**	**Contact Name**

Signature of the Vendor		
Signature:		**Date:**
Name:	**Title:**	**Place:**

Statement from Inventors			
Title of Invention			
Number of Inventors			
Instructions: Use additional Invention Disclosure Forms if there are more than three inventors			
Name of Inventor No. 1	**Residence Address**	**Residence Telephone Number**	**Citizenship**
Name of Employer When Invention Made	**Business Mailing Address**	**Business Telephone Number**	
Name of Supervisor When Invention Made	**Title of Inventor When Invention Made**	**Nature of Inventor's Work When Invention Made**	
Name of Key Ministry/ OPS Entity Contact	**Telephone Number of Key Ministry /OPS Entity Contact**		
Name of Inventor No. 2	**Residence Address**	**Residence Telephone Number**	**Citizenship**
Name of Employer When Invention Made	**Business Mailing Address**	**Business Telephone Number**	
Name of Supervisor When Invention Made	***Title of Inventor When Invention Made***	***Nature of Inventor's Work When Invention Made***	
Name of Key Ministry/ OPS Entity Contact	**Telephone Number of Key Ministry/ OPS Entity Contact**		
Name of Inventor No. 3	**Residence Address**	**Residence Telephone Number**	**Citizenship**
Name of Employer When Invention Made	**Business Mailing Address**	**Business Telephone Number**	
Name of Supervisor When Invention Made	**Title of Inventor When Invention Made**	**Nature of Inventor's Work When Invention Made**	
Name of Key Ministry/ OPS Entity Contact	**Telephone Number of Key Ministry/ OPS Entity Contact**		

Description of the Invention
Instructions: Avoid jargon. Attach additional pages as appendices as necessary, including drawings, sequences of steps in a process, references to published literature or known patents relating to the problem or the invention, additional information, etc.
Provide a clear and concise summary of the invention, and indicate the technical field to which it pertains
What is the problem that the invention deals with?
What is the concept for solving the problem through the invention?
What are the principal uses of the invention?
Which concepts or ideas are thought to be new, useful and unobvious?
Which concepts or ideas are thought to be an improvement on prior art?
Which concepts or ideas are thought to be capable of commercial exploitation now or in the future?
What are potential commercial applications of the invention?

History of Invention		
A. Events other than disclosures	**Date**	**Names and Addresses of People Having First-Hand Knowledge, and Places Where Events Occurred**
Conception of invention		
First written description		
First test of invention		
B. Disclosures	**Date**	**Names, Places, Form (written / oral) and Exact Information Disclosed (or "None")**
Disclosure in any publication		
Disclosure at any conference		
Disclosure at any presentation or demonstration		
Other disclosure		
Planned disclosures to non-government personnel		
Have the inventors assigned the invention?	If "yes", name of assignee	If "yes", address of assignee
Are any inventors obligated to assign, license or convey the invention to any other entity?	If "yes", name of other entity	If "yes", address of other entity

Signatures of Inventors	
Inventor No. 1:	Date:
	Place:
Inventor No. 2:	Date:
	Place:
Inventor No. 3:	Date:
	Place:

ATTACHMENT J TO MASTER AGREEMENT-PROVINCIALLY FUNDED ORGANIZATION NOTICE

[INSTRUCTION TO VENDOR: PRIOR TO responding to requests from a Provincially Funded Organization, forward a copy of this document to the Provincially Funded Organization. Aside from inserting the information in the applicable fields below, this Provincially Funded Organization Notice may not be amended.]

BACKGROUND INFORMATION:

- Ontario has established various vendor of record arrangements (each a "**VOR Arrangement**") for selected qualified vendors (each a "**Vendor**") to supply certain products or services, or both, (the **"Deliverable"**) to Ontario.

- Vendors under most VOR Arrangements are required, subject to the terms of their agreement with Ontario under the applicable VOR Arrangement (each an "**Ontario Agreement**"), to consider requests from you (if you are a "Provincially Funded Organization", as defined in the applicable Ontario Agreement) to make Deliverables available to you for purchase.

- In order for a Vendor to consider requests from you, the Vendor must first provide you with this Provincially Funded Organization Notice ("**Notice**").

- If you continue with your request after being provided with this Notice, you will be deemed to have acknowledged and agreed to the terms set out in this Notice.

TERMS

1. Your Status in Relation to Ontario Agreements. You are not a party to any Ontario Agreement and you cannot acquire any Deliverables as a "Client" under any Ontario Agreement. If you wish to acquire products and services from a Vendor, you must enter into a separate agreement with the Vendor ("**Provincially Funded Organization Agreement**").

2. Provincially Funded Organization Agreement. Although Ontario is providing you with access to Vendors listed on VOR Arrangements, you remain solely responsible for negotiating the terms and conditions of your Provincially Funded Organization Agreement with each Vendor, including the responsibility for ensuring that each of your Provincially Funded Organization Agreements contains business, legal or other terms and conditions as may be necessary or desirable for you.

3. Procurement Processes. You are solely responsible for ensuring that the selection of any Vendor and the procurements made under any of your Provincially Funded Organization Agreements comply with any and all procurement rules, regulations, obligations and processes to which you are subject. Any differences between the terms and conditions of an Ontario Agreement and the terms and conditions of your Provincially Funded Organization Agreement may affect whether the selection of the Vendor and the procurements made under your Provincially Funded Organization Agreement meet the procurement rules, regulations, obligations or processes to which you are subject.

4. Ontario Not Liable for Your Relationship with Vendors.

   - Ontario does not endorse, recommend or approve the suitability of: (i) any Vendor as a supplier to you; (ii) the procurement process used to establish any VOR Arrangement as meeting the procurement rules, regulations, obligations and processes to which you are subject; (iii) the ordering process established for any VOR Arrangement as meeting the procurement rules, regulations, obligations and processes to which you are subject; and (iv) the terms and conditions of any Ontario Agreement as a basis for, in whole or in part, any Provincially Funded Organization Agreement or any other resulting or related relationships or agreements between you and any Vendor. You are solely responsible for conducting your own independent assessment (including obtaining your own professional advice (which may include legal and business advice) as may be necessary and appropriate in your specific circumstances) to determine the suitability of the above.

Please note that legal and other professional advice provided to Ontario with respect to the establishment of its VOR Arrangements and its Ontario Agreements was solely for the benefit of Ontario to take into account Ontario's specific legal and other concerns, and may not be applicable to or appropriate for, and may not address any of your concerns or the concerns of any other third party. Legal counsel for Ontario recommends that you obtain independent legal representation and receive independent legal advice, as well as other required independent professional advice, prior to executing any document or entering into any contract or agreement with, or acquiring any products or services from, a Vendor.

- Ontario makes no representation, assurance, warranty, or guarantee: (i) that a Vendor will enter into a Provincially Funded Organization Agreement with you; or (ii) of the quality, value or volume of products or services that may or will be sold, if any, to you.

- Ontario will not: (i) be or be deemed to be a party to, or a guarantor of any obligations or liability of any party under, any Provincially Funded Organization Agreement or any resulting or related relationship or agreement between you and any Vendor; or (ii) be responsible or liable to you for, and nothing in any agreement between you and any Vendor will have the effect of imposing or resulting in the imposition of, any costs, obligation, liability or covenant on Ontario for any matter arising under or in connection with: the VOR Arrangement; any Deliverable; the Ontario Agreement or any related documentation; any access to the VOR Arrangement or the Ontario Agreement or related documentation; any Provincially Funded Organization Agreement; any act, error or omission of the Vendor (including the provision or non-provision of any Deliverables or other products or services by the Vendor); or this Notice.

- You will not, in relation to or under any Provincially Funded Organization Agreement or under any resulting or related relationship or agreement between you and any Vendor, bring any cause of action, action, claim, demand or lawsuit against Ontario or any of its personnel as a result of: (i) any act, error or omission of the parties to any Provincially Funded Organization Agreement; or (ii) any act, error or omission of Ontario or any of its personnel.

- Any obligations, costs or liability arising under or in connection with any Provincially Funded Organization Agreement or any resulting or related relationships or agreements between you and the Vendor will remain with you and the Vendor.

- You are solely responsible for your own contract administration with the Vendor and will not direct any issues that may arise with the Vendor to Ontario.

- For the purposes of any Provincially Funded Organization Agreement, you have no power or authority to bind Ontario or to assume or create any obligation or responsibility, express or implied, on behalf of Ontario.

5. Data and Documentation. You will provide to Ontario, at Ontario's request, any data and documentation about your acquisition of products and services from the Vendor.

6. Access to VOR Arrangements, Vendor/Ontario Agreements and Deliverables. It is Ontario's intention that, if you choose to access any VOR Arrangement, you will do so only to acquire products or services for your operational needs. Ontario, in its sole discretion, may delay, restrict or choose to not renew access by you to information regarding any VOR Arrangement, any Ontario Agreement and any products and services provided by the suppliers to Ontario on any VOR Arrangement.

7. Restrictions to Becoming a Supplier to Ontario. If you choose to access the Ministry of Government Services' enterprise-wide VOR Arrangements, you are advised that, in some circumstances, you may be restricted or ineligible to submit a bid to become a supplier to Ontario under future procurement opportunities.

8. Confidentiality. You acknowledge that information of a confidential nature to Ontario or the Vendor, regardless of whether it is identified as confidential or not ("**Confidential Information**") may come into your

knowledge, possession or control. You will: (a) keep all Confidential Information confidential and secure; (b) limit the disclosure of Confidential Information to only those of your directors, officers, employees, agents, partners, affiliates, volunteers or subcontractors who have a need to know it for the purpose of acquiring or considering the acquisition of products and services from a Vendor (the "**Purpose**") and who have been specifically authorized to have such disclosure; (c) not directly or indirectly disclose, destroy, exploit or use any Confidential Information (except for the Purpose, or except if required by order of a court or tribunal), without first obtaining: (i) the written consent of the Ministry of Government Services ("**MGS**"); and (ii) in respect of any Confidential Information about the Vendor or any other third-party, the written consent of the Vendor and any such other third-party; and (d) return all Confidential Information to MGS on demand, with no copy or portion kept by you. You will not copy any Confidential Information, in whole or in part, unless copying is essential for the Purpose. On each copy made by you, you will reproduce all notices which appear on the original.

Materials for Tuesday.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]
CC: michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; david.c.greenall@ca.pwc.com [david.c.greenall@ca.pwc.com]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Materials for Tuesday
Date: Thursday, November 10, 2016 16:59:25
Attachment 1: Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT CLEAN.docx
Attachment 2: Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT.docx

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Please see attached a revised version of the Cap and Trade memo taking into account the points that came up in the last MOECC meeting and our discussions on our last update call. There is a clean version and also one in tracked changes to the last version that I circulated.

As mentioned on the update call there is one significant area to do with the Escrow accounts that is pending more information that I am hoping will be in the legal analysis to be provided by the MOECC. I would lean towards the second option drafted in terms of what makes intuitive sense, but legal rights and control seem very relevant to consider in coming to a final conclusion.

We have our meeting scheduled for 10-11am. I plan to be there in person.
For my part I am planning that the meeting would be to discuss comments on the memo - any additional considerations or where you might challenge or have concerns with the preliminary conclusions, and also to confirm our next steps. Please let me know if there are other items you would like to add to the agenda so we can prepare accordingly.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT CLEAN.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations

Commented [LD1]: O/S – MOECC was to provide comments on accuracy of background terminology .

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction (after the distribution of free EAs). The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances.

5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

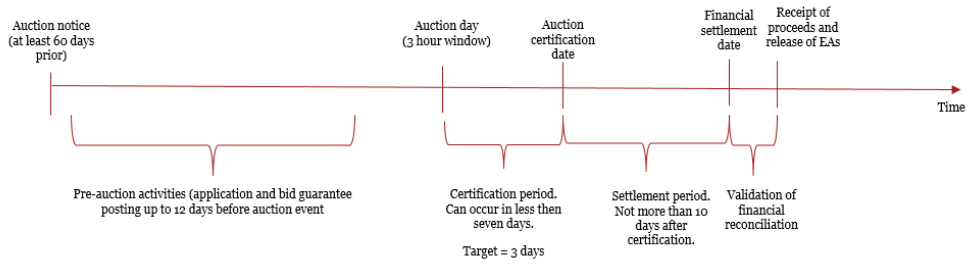
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall. There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that provinces that do not have either a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. Therefore actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix A

PS 1000, Financial statement concepts

PS 1200, Financial statement presentation

PS 3210, Assets

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation and sales of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see Part 5). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation are not recognized as assets, whether sold at auction or issued as free allowances.

d) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify

the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On settlement date:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

Dr Cost of sales (expected to be nil cost)

Cr Inventory held-for-sale (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation and sales of free and auctioned EAs</u>:

EAs are created to be sold to participants. These sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. Therefore despite being intangible in nature, the EAs also meet the definition of inventories held-for-sale and could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities). PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view was ultimately rejected because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

Commented [LD2]: O/S Subject to Summary of legal opinion obtained by MOECC. Not yet seen.

[EITHER]

An asset is recognized by the province as cash is received into a participant's escrow "sub-account".

Any Escrowed cash amounts held in participants sub-accounts are still held for the benefit of the Minister as they are sub-accounts of the Province's escrow account and are only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead. Therefore any escrowed cash amounts are similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. It is noted that based on amounts of bid guarantees posted in cash in other WCI jurisdictions it is not expected that these amounts would be material. Any cash posted as bid guarantees would be considered to be restricted cash as it is held in a separate account and is not available for general use by the government.

Any LOC or LOG amounts received into a participant's sub-account are not assets as they are in the form of a commitment but do not represent either cash or the contractual right to receive cash.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement

date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred into a participant's sub-account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date as this is a matter of time and the settlement process. Therefore during the settlement process, as cash payments are received from participants and deposited into the participant's escrow settlement account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. After the certification date any cash recognized for successful bid participants would not be considered to be restricted cash as it is no longer required to be returned to the bidder and is no longer externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province from the certification date neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash". The revenue implications of settlement date and delivery of EAs are discussed in Section 5.

[OR]

An asset is recognized by the province as cash is transferred to the jurisdiction's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids, or if their bids are successful and therefore whether the Province has any rights to the escrow proceeds prior to the auction being held. Rather the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. [NTD – to confirm]

Commented [LD3]: To confirm nature of the Escrow sub-accounts
Based on legal analysis?

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is

considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred from participant's sub-account to the jurisdiction's escrow account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date which is a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 5 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

[Update with rejected view from above – e.g. participant sub-account recognition vs not on bid guarantee date]

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 5 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement create a derivative that needs to be recognized as a contract exists from the certification date to the settlement date for the Province to sell the specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy

objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs. This alternative view would be consistent with a view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 4 below.

It was considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. Therefore the right to receive an EA is also not an asset. The Province does not control how many EAs may be received back that can be re-sold (i.e. those remitted for increased compliance obligations) and so any recognition of an asset for the right to receive back was recognized for all EAs, would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not appropriate accounting.

e) Failure of participant to pay increased compliance obligation:

The Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations. As participants can settle their obligations with EAs (including those from a future compliance period) and EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (c) above there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognized the receivable would be recognized at the amount expected to be received at the time of initial recognition. This would take into account the expected settlement of the receivable. For example, some or part of the amount might be settled by the a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not

settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation.

4. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance

PS 1000, Financial statement concepts

PS 3200, Liabilities

PS 3300, Contingent liabilities

PS 3310, Loan guarantees

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liability for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There may be an implicit loan guarantee by the Province to the extent that there are funds held in escrow for the participants that are not recognized as assets of the Province, but for which the Province may have a duty to repay to the participants in the case of insolvency issues at the escrow agent. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent such implicit guarantees exist over the balance sheet date disclosures of the implicit loan guarantee should be made, if material.

[NTD – position to be confirmed based on discussion of insolvency risk with DB accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]

Analysis

a) Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.

Once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed for cash or any other financial asset, or exchanged for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.

Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 5 below.

c) Loan guarantees and contingent liabilities: To the extent that escrow amounts are recognized on the Province's balance sheet there would be a corresponding liability already recognized in respect of the requirement to return the participants deposit or in respect of deferred revenue. However to the extent that participants have submitted cash bid guarantees in Escrow that are not recognized in the Public Accounts of the Province there may an implied guarantee to the participants that their financial assurance will be returned to them if the auction does not run or they are not successful. [TBD – To be supported by facts, if any, which indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts.

5. Revenue recognition under the cap and trade program as sponsoring government

This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Relevant guidance - See Appendix A for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position –The sale of EAs are exchange transactions.

Analysis:

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not

solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

Alternative positions considered and rejected: An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.

Revenue recognition for sale of EAs (Exchange transactions)

Relevant guidance - See Appendix A for details.

PS 1000, Financial statement concepts

PS 1150, Generally accepted accounting principles

Other GAAP accounting frameworks

Preliminary position: Revenue is recognized for the sale of EAs on the auction date as there are no further substantive performance obligations by the Province.

Analysis:

a) What is the performance obligation? A performance obligation is defined in IFRS 15/ASC 606 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the PSAS Revenue Statement of Principles which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". This analysis has applied the IFRS concept, as permitted under PS 1150. In both IFRS 15/ASC 606 and the PSAS Revenue Statement of Principles, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the enforceable rights and obligations that are entered into when an auction occurs.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix A for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction, the Province has only one distinct performance obligation to each successful bidder under this contract, which is the delivery of the EAs.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 4 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the sale of EAs. Finally, it is noted that there is no legislative provisions for the termination of the program, and there are no contractual provisions embedded in the EAs

that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written of implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15/ASC 606 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400 or IAS 18 there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the PSAS Revenue Statement of Principles proposes a "control" model similar to IFRS 15/ASC 606, so this approach has been applied in the analysis. Under IFRS 15/ASC 606 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

   IFRS 15/ASC 606 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the PSAS Revenue Statement of Principles and have been considered in this analysis. See IFRS 15.38 in Appendix A. The indicators have been assessed as follows:

   Present right to payment – As noted in Section 3 above, there is considered to be a contract from the auction certification date, and payment must be received by the Province prior to the financial settlement date.

   Legal title to the asset – Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs. Participants can only trade or use the EAs when they are credited to the participants account. This occurs after the settlement process is completed.

   The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.

   The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the date of transfer to their CITSS account, which is the settlement date of the contract. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the transfer into the participant's account. Therefore the participant has access to the rights inherent in the EA only after it has been transferred to their account.

   The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.

   Based on the balance of the indicators above it can be concluded that there is support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant.

   Alternatives considered and rejected:

   Certification date: It was considered whether revenue should be recognized at a point in time when the contract to purchase/sell the EAs is agreed upon i.e. the auction certification date (if substantive) or the auction date if certification is not substantive. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset", and it could be argued that the delayed delivery of the EAs is only because of the financial settlement process to ensure payment is received and does not indicate that control has not passed earlier. This view was ultimately rejected because of the lack of legal title to the EAs (as they are not "property")

and the intangible nature of the EAs means that control cannot be evidenced as passing earlier until the EAs are credited to the participants account.

Trade date accounting: It was considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix A for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets"

in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

6. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

7. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

8. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

9. Implementation risks and audit considerations

Appendix A – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35-.37. PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not defined under PSAS. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and OS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). After the adoption of PS 3450, which is currently effective for the Province for fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - “Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations.”

PS 3100.04 (a) - “External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used.”

PS 3100.11 - “Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified.”

PS 3100.27-.28 - Designated assets – “...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises....”

Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations

Commented [LD1]: O/S – MOECC was to provide comments on accuracy of background terminology .

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~ capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations ~~T~~there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many ~~MOECC determines how many~~ EAs of each vintage will be available at each auction (after the distribution of free EAs).~~, and how many of each "the vintage" of the EAs is available.~~ The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". ~~, but m~~More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are

held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's~~ regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). ~~regulations.~~ When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and ~~, in which case~~ the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and ~~payment has been received~~ the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]

Auction timeline illustration

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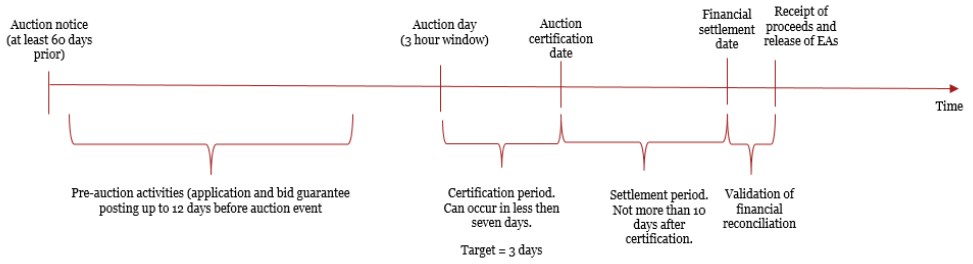

Free allowances

C~~Mandatory and c~~apped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

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The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~ issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "~~credits for early action~~early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall. There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any p~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund

costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that provinces that do not have either a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. Therefore actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

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3. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix A

PS 1000, Financial statement concepts

PS 1200, Financial statement presentation

PS 3210, Assets

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation and sales of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~ retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction.~~transfer of funds into the Province's escrow settlement account.

   ~~On the auction date, a receivable is recognized by the Province for the sale of EAs.~~ After auction certification cash from successful bidders is transferred to the Province's escrow settlement account,

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resulting in recognition of an asset (cash). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants ~~A corresponding amount is recognized in Revenue~~ (see Part 5). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation are not recognized as assets, whether sold at auction or issued as free allowances.

d) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date*~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr ~~Receivable~~ Cash (~~from successful participants/~~in Escrow~~ed amounts~~)

Cr Deferred Revenue

~~Dr Cost of sales (expected to be nil cost)~~

~~Cr Inventory held-for-sale (expected to be nil cost)~~

On settlement date:

Dr ~~Cash~~Deferred revenue

Cr ~~Receivable~~ Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)~~(from successful participants/Escrowed amounts)~~

Dr Cost of sales (expected to be nil cost)

Cr Inventory held-for-sale (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) On creation and sales of free and auctioned EAs:

EAs are created to be sold to participants. These sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. Therefore despite being intangible in nature, the EAs also meet the definition of inventories held-for-sale and could be given accounting

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recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

EAs that are returned to the government and not ~~cancelled~~ retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities). PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view was ultimately rejected because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead~~ provide an opportunity ~~to~~for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

[EITHER]

An asset is recognized by the province as cash is received into a participant's escrow "sub-account".

Any Escrowed cash amounts held in participants sub-accounts are still held for the benefit of the Minister as they are sub-accounts of the Province's escrow account and are only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid

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guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead. Therefore any escrowed cash amounts are similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. It is noted that based on amounts of bid guarantees posted in cash in other WCI jurisdictions it is not expected that these amounts would be material. Any cash posted as bid guarantees would be considered to be restricted cash as it is held in a separate account and is not available for general use by the government.

Any LOC or LOG amounts received into a participant's sub-account are not assets as they are in the form of a commitment but do not represent either cash or the contractual right to receive cash.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred into a participant's sub-account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date as this is a matter of time and the settlement process. Therefore during the settlement process, as cash payments are received from participants and deposited into the participant's escrow settlement account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. After the certification date any cash recognized for successful bid participants would not be considered to be restricted cash as it is no longer required to be returned to the bidder and is no longer externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province from the certification date neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank

account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash". The revenue implications of settlement date and delivery of EAs are discussed in Section 5.

[OR]

~~b)~~ An asset is recognized by the province as cash is transferred to the jurisdiction's escrow settlement account.

Prior to the auction process, the Province does not control the cash ~~proceeds~~or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids, or if their bids are successful and therefore whether the Province has any rights to the escrow proceeds prior to the auction being held. Rather the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. [NTD – to confirm]

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred from participant's sub-account to the jurisdiction's escrow account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date which is a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province neither

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party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 5 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

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~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

Alternative positions considered and rejected:

[Update with rejected view from above – e.g. participant sub-account recognition vs not on bid guarantee date]

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~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow~~

~~accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 5 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement create a derivative that needs to be recognized as a contract exists from the certification date to the settlement date for the Province to sell the specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting~~

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~~subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

~~c)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~ retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs. This alternative view would be consistent with a view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 4 below.

It was considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. Therefore the right to receive an EA is also not an asset. The Province does not control how many EAs may be received back that can be re-sold (i.e. those remitted for increased compliance obligations) and so any recognition of an asset for the right to receive back was recognized for all EAs, would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not appropriate accounting.

~~d)~~e) Failure of participant to pay increased compliance obligation:

The Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations. As participants can settle their obligations with EAs (including those from a future compliance period) ~~that~~ and EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (c) above there is no asset of the Province until ~~. It is only when~~ a participant has not settled with EAs ~~that~~ and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognized the receivable would be recognized at the amount expected to be received at the time of initial recognition. This would take into account the expected settlement of the receivable. For example, some or part of the amount might be settled by the a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation.

4. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance

PS 1000, Financial statement concepts

PS 3200, Liabilities

PS 3300, Contingent liabilities

PS 3310, Loan guarantees

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liability for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: ~~**EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement.~~ There may be an implicit loan guarantee by the Province to the extent that there are funds held in escrow for the participants that are not recognized as assets of the Province, but for which the Province may have a duty to repay to the participants in the case of insolvency issues at the escrow agent. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent ~~that there are escrowed proceeds held over a balance sheet date~~such implicit guarantees exist over the balance sheet date disclosures of the implicit loan guarantee should be made, if material.

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~

[NTD – position to be confirmed based on discussion of insolvency risk with DB accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]

Analysis

a) Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.

Once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed for cash or any other financial asset, or exchanged for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~ retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.

Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to ~~deliver~~ transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is ~~Ultimately however, the delivery of free EAs is~~ a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that

liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

~~and is at the discretion of the Province, rather than a contractual or constructive obligation to the participants, as the Province retains discretion over the issuance of free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC not comfortable with the idea there is no obligation to issue free EAs.]~~

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected: ~~It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 5 below.

c) Loan guarantees and contingent liabilities: To the extent that escrow amounts are recognized on the Province's balance sheet there would be a corresponding liability already recognized in respect of the requirement to return the participants deposit or in respect of deferred revenue. However to the extent that participants have submitted cash bid guarantees in Escrow that are not recognized in the Public Accounts of the Province there may an implied guarantee to the participants that their financial assurance will be returned to them if the auction does not run or they are not successful. [TBD – To be supported by facts, if ~~any, that~~any, which indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts.

5. *Revenue recognition under the cap and trade program as sponsoring government*

This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Relevant guidance - See Appendix A for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position –The sale of EAs are exchange transactions.

Analysis:

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

Alternative positions considered and rejected: An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in order to meet their compliance obligations which are created by legislation, and initially EAs are only available

from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.

Revenue recognition for sale of EAs (Exchange transactions)

Relevant guidance - See Appendix A for details.

PS 1000, Financial statement concepts

PS 1150, Generally accepted accounting principles

Other GAAP accounting frameworks

Preliminary position: Revenue is recognized for the sale of EAs on the auction date as there are no further substantive performance obligations by the Province.

Analysis:

a) What is the performance obligation? A performance obligation is defined in IFRS 15/ASC 606 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the PSAS Revenue Statement of Principles which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". This analysis has applied the IFRS concept, as permitted under PS 1150. In both IFRS 15/ASC 606 and the PSAS Revenue Statement of Principles, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the enforceable rights and obligations that are entered into when an auction occurs.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix A for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction, the Province has only one distinct performance obligation to each successful bidder under this contract, which is the delivery of the EAs.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 4 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore ~~this obligation to redeem~~Ontario has no obligation to redeem an EA that ~~cannot arise~~arises from the original exchange transaction and ~~is therefore~~therefore there is ~~not~~no ~~a~~ performance obligation ~~of that transaction~~that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the sale of EAs. Finally, it is noted that there is no legislative provisions for the termination of the program, and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written of implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15/ASC 606 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400 or IAS 18 there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the PSAS Revenue Statement of Principles proposes a "control" model similar to IFRS 15/ASC 606, so this approach has been applied in the analysis. Under IFRS 15/ASC 606 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15/ASC 606 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the PSAS Revenue Statement of Principles and have been considered in this analysis. See IFRS 15.38 in Appendix A. The indicators have been assessed as follows:

Present right to payment – As noted in Section 3 above, there is considered to be a contract from the auction certification date, and payment must be received by the Province prior to the financial settlement date. ~~present right to payment at the auction date.~~

Legal title to the asset – Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs. ~~Legal title is transferred when~~ Participants can only trade or use the ~~the~~ EAs when they are credited to the participants account. This occurs after the ~~auction certification and~~ settlement process is completed. ~~[MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.

The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the ~~auction~~ date of transfer to their CITSS account, which is the settlement date of the contract. ~~If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value.~~ The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the ~~auction~~transfer into the participant's account. Therefore the participant has access to the rights inherent in the EA only after it has been transferred to their account. ~~While EAs are credited to a participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.

Based on the balance of the indicators above it can be concluded that there is support for recognizing revenue on a "point in time" basis on the ~~auction date~~date when the EAs are transferred to the participant.

Alternatives considered and rejected:

Certification date: It was considered whether revenue should be recognized at a point in time when the contract to purchase/sell the EAs ~~are~~ is agreed upon i.e. the auction certification date (if substantive) or the

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auction date if certification is not substantive. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset", and it could be argued that the delayed delivery of the EAs is only because of the financial settlement process to ensure payment is received and does not indicate that control has not passed earlier. This view was ultimately rejected because of the lack of legal title to the EAs (as they are not "property") and the intangible nature of the EAs means that control cannot be evidenced as passing earlier until the EAs are credited to the participants account.

Trade date accounting: It was considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

~~credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix A for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

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Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. [~~NTD – to confirm that all interested parties agree with this statement~~]

6. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

7. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

8. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

9. Implementation risks and audit considerations

Appendix A – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35-.37. PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not defined under PSAS. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and OS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). After the adoption of PS 3450, which is currently effective for the Province for fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - “Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations.”

PS 3100.04 (a) - “External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used.”

PS 3100.11 - “Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified.”

PS 3100.27-.28 - Designated assets – “...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises....”

Materials for Tuesday.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]
CC: michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; david.c.greenall@ca.pwc.com [david.c.greenall@ca.pwc.com]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Materials for Tuesday
Date: Thursday, November 10, 2016 16:59:25
Attachment 1: Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT CLEAN.docx
Attachment 2: Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT.docx

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Please see attached a revised version of the Cap and Trade memo taking into account the points that came up in the last MOECC meeting and our discussions on our last update call. There is a clean version and also one in tracked changes to the last version that I circulated.

As mentioned on the update call there is one significant area to do with the Escrow accounts that is pending more information that I am hoping will be in the legal analysis to be provided by the MOECC. I would lean towards the second option drafted in terms of what makes intuitive sense, but legal rights and control seem very relevant to consider in coming to a final conclusion.

We have our meeting scheduled for 10-11am. I plan to be there in person.
For my part I am planning that the meeting would be to discuss comments on the memo - any additional considerations or where you might challenge or have concerns with the preliminary conclusions, and also to confirm our next steps. Please let me know if there are other items you would like to add to the agenda so we can prepare accordingly.

Regards,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

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Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT CLEAN.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations

Commented [LD1]: O/S – MOECC was to provide comments on accuracy of background terminology .

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction (after the distribution of free EAs). The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances.

5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

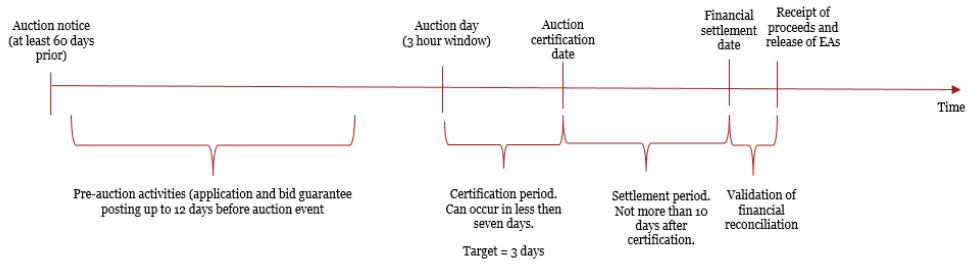
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall. There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that provinces that do not have either a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. Therefore actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix A

PS 1000, Financial statement concepts

PS 1200, Financial statement presentation

PS 3210, Assets

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation and sales of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see Part 5). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation are not recognized as assets, whether sold at auction or issued as free allowances.

d) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify

the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On settlement date:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

Dr Cost of sales (expected to be nil cost)

Cr Inventory held-for-sale (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation and sales of free and auctioned EAs</u>:

EAs are created to be sold to participants. These sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. Therefore despite being intangible in nature, the EAs also meet the definition of inventories held-for-sale and could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities). PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view was ultimately rejected because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

Commented [LD2]: O/S Subject to Summary of legal opinion obtained by MOECC. Not yet seen.

[EITHER]

An asset is recognized by the province as cash is received into a participant's escrow "sub-account".

Any Escrowed cash amounts held in participants sub-accounts are still held for the benefit of the Minister as they are sub-accounts of the Province's escrow account and are only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead. Therefore any escrowed cash amounts are similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. It is noted that based on amounts of bid guarantees posted in cash in other WCI jurisdictions it is not expected that these amounts would be material. Any cash posted as bid guarantees would be considered to be restricted cash as it is held in a separate account and is not available for general use by the government.

Any LOC or LOG amounts received into a participant's sub-account are not assets as they are in the form of a commitment but do not represent either cash or the contractual right to receive cash.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement

date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred into a participant's sub-account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date as this is a matter of time and the settlement process. Therefore during the settlement process, as cash payments are received from participants and deposited into the participant's escrow settlement account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. After the certification date any cash recognized for successful bid participants would not be considered to be restricted cash as it is no longer required to be returned to the bidder and is no longer externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province from the certification date neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash". The revenue implications of settlement date and delivery of EAs are discussed in Section 5.

[OR]

An asset is recognized by the province as cash is transferred to the jurisdiction's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids, or if their bids are successful and therefore whether the Province has any rights to the escrow proceeds prior to the auction being held. Rather the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. [NTD – to confirm]

Commented [LD3]: To confirm nature of the Escrow sub-accounts
Based on legal analysis?

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is

considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred from participant's sub-account to the jurisdiction's escrow account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date which is a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 5 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

[Update with rejected view from above – e.g. participant sub-account recognition vs not on bid guarantee date]

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 5 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement create a derivative that needs to be recognized as a contract exists from the certification date to the settlement date for the Province to sell the specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy

objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs. This alternative view would be consistent with a view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 4 below.

It was considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. Therefore the right to receive an EA is also not an asset. The Province does not control how many EAs may be received back that can be re-sold (i.e. those remitted for increased compliance obligations) and so any recognition of an asset for the right to receive back was recognized for all EAs, would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not appropriate accounting.

e) Failure of participant to pay increased compliance obligation:

The Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations. As participants can settle their obligations with EAs (including those from a future compliance period) and EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (c) above there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognized the receivable would be recognized at the amount expected to be received at the time of initial recognition. This would take into account the expected settlement of the receivable. For example, some or part of the amount might be settled by the a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not

settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation.

4. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance

PS 1000, Financial statement concepts

PS 3200, Liabilities

PS 3300, Contingent liabilities

PS 3310, Loan guarantees

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liability for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There may be an implicit loan guarantee by the Province to the extent that there are funds held in escrow for the participants that are not recognized as assets of the Province, but for which the Province may have a duty to repay to the participants in the case of insolvency issues at the escrow agent. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent such implicit guarantees exist over the balance sheet date disclosures of the implicit loan guarantee should be made, if material.

[NTD – position to be confirmed based on discussion of insolvency risk with DB accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]

Analysis

a) Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.

Once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed for cash or any other financial asset, or exchanged for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.

Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 5 below.

c) Loan guarantees and contingent liabilities: To the extent that escrow amounts are recognized on the Province's balance sheet there would be a corresponding liability already recognized in respect of the requirement to return the participants deposit or in respect of deferred revenue. However to the extent that participants have submitted cash bid guarantees in Escrow that are not recognized in the Public Accounts of the Province there may an implied guarantee to the participants that their financial assurance will be returned to them if the auction does not run or they are not successful. [TBD – To be supported by facts, if any, which indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts.

5. Revenue recognition under the cap and trade program as sponsoring government

This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Relevant guidance - See Appendix A for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position –The sale of EAs are exchange transactions.

Analysis:

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not

solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

Alternative positions considered and rejected: An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.

Revenue recognition for sale of EAs (Exchange transactions)

Relevant guidance - See Appendix A for details.

PS 1000, Financial statement concepts

PS 1150, Generally accepted accounting principles

Other GAAP accounting frameworks

Preliminary position: Revenue is recognized for the sale of EAs on the auction date as there are no further substantive performance obligations by the Province.

Analysis:

a) What is the performance obligation? A performance obligation is defined in IFRS 15/ASC 606 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the PSAS Revenue Statement of Principles which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". This analysis has applied the IFRS concept, as permitted under PS 1150. In both IFRS 15/ASC 606 and the PSAS Revenue Statement of Principles, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the enforceable rights and obligations that are entered into when an auction occurs.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix A for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction, the Province has only one distinct performance obligation to each successful bidder under this contract, which is the delivery of the EAs.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 4 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the sale of EAs. Finally, it is noted that there is no legislative provisions for the termination of the program, and there are no contractual provisions embedded in the EAs

that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written of implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15/ASC 606 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400 or IAS 18 there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the PSAS Revenue Statement of Principles proposes a "control" model similar to IFRS 15/ASC 606, so this approach has been applied in the analysis. Under IFRS 15/ASC 606 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

   IFRS 15/ASC 606 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the PSAS Revenue Statement of Principles and have been considered in this analysis. See IFRS 15.38 in Appendix A. The indicators have been assessed as follows:

   Present right to payment – As noted in Section 3 above, there is considered to be a contract from the auction certification date, and payment must be received by the Province prior to the financial settlement date.

   Legal title to the asset – Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs. Participants can only trade or use the EAs when they are credited to the participants account. This occurs after the settlement process is completed.

   The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.

   The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the date of transfer to their CITSS account, which is the settlement date of the contract. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the transfer into the participant's account. Therefore the participant has access to the rights inherent in the EA only after it has been transferred to their account.

   The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.

   Based on the balance of the indicators above it can be concluded that there is support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant.

   Alternatives considered and rejected:

   Certification date: It was considered whether revenue should be recognized at a point in time when the contract to purchase/sell the EAs is agreed upon i.e. the auction certification date (if substantive) or the auction date if certification is not substantive. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset", and it could be argued that the delayed delivery of the EAs is only because of the financial settlement process to ensure payment is received and does not indicate that control has not passed earlier. This view was ultimately rejected because of the lack of legal title to the EAs (as they are not "property")

and the intangible nature of the EAs means that control cannot be evidenced as passing earlier until the EAs are credited to the participants account.

Trade date accounting: It was considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix A for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets"

in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

6. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

7. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

8. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

9. Implementation risks and audit considerations

Appendix A – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35-.37. PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not defined under PSAS. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and OS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). After the adoption of PS 3450, which is currently effective for the Province for fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - “Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations.”

PS 3100.04 (a) - “External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used.”

PS 3100.11 - “Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified.”

PS 3100.27-.28 - Designated assets – “...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises....”

Cap and Trade accounting implications - memorandum to file v4 November 3 DRAFT.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations

Commented [LD1]: O/S – MOECC was to provide comments on accuracy of background terminology .

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~ capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations ~~T~~there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many ~~MOECC determines how many~~ EAs of each vintage will be available at each auction (after the distribution of free EAs).~~, and how many of each "the vintage" of the EAs is available.~~ The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". ~~, but m~~More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are

held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's~~ regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). ~~regulations.~~ When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and ~~, in which case~~ the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and ~~payment has been received~~ the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]

Auction timeline illustration

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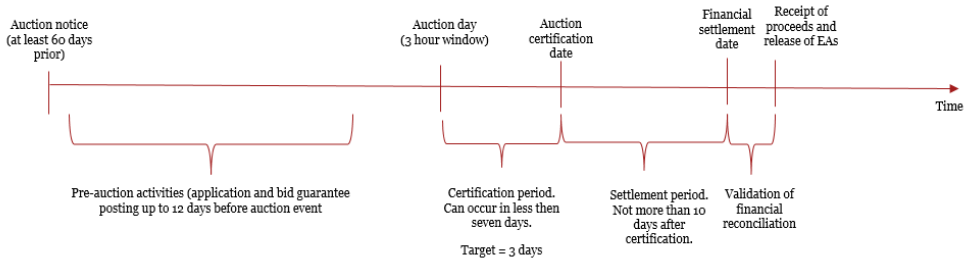

Free allowances

C~~Mandatory and c~~apped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

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The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~ issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "~~credits for early action~~early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall. There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any p~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund

costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that provinces that do not have either a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. Therefore actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

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3. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix A

PS 1000, Financial statement concepts

PS 1200, Financial statement presentation

PS 3210, Assets

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation and sales of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~ retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction.~~transfer of funds into the Province's escrow settlement account.

   ~~On the auction date, a receivable is recognized by the Province for the sale of EAs.~~ After auction certification cash from successful bidders is transferred to the Province's escrow settlement account,

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resulting in recognition of an asset (cash). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants ~~A corresponding amount is recognized in Revenue~~ (see Part 5). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation are not recognized as assets, whether sold at auction or issued as free allowances.

d) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date*~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr ~~Receivable~~ Cash (~~from successful participants/~~in Escrow~~ed amounts~~)

Cr Deferred Revenue

~~Dr Cost of sales (expected to be nil cost)~~

~~Cr Inventory held-for-sale (expected to be nil cost)~~

On settlement date:

Dr ~~Cash~~Deferred revenue

Cr ~~Receivable~~ Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)~~(from successful participants/Escrowed amounts)~~

Dr Cost of sales (expected to be nil cost)

Cr Inventory held-for-sale (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) On creation and sales of free and auctioned EAs:

EAs are created to be sold to participants. These sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. Therefore despite being intangible in nature, the EAs also meet the definition of inventories held-for-sale and could be given accounting

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recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

EAs that are returned to the government and not ~~cancelled~~ retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities). PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view was ultimately rejected because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead~~ provide an opportunity ~~to~~for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

[EITHER]

An asset is recognized by the province as cash is received into a participant's escrow "sub-account".

Any Escrowed cash amounts held in participants sub-accounts are still held for the benefit of the Minister as they are sub-accounts of the Province's escrow account and are only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid

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guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead. Therefore any escrowed cash amounts are similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. It is noted that based on amounts of bid guarantees posted in cash in other WCI jurisdictions it is not expected that these amounts would be material. Any cash posted as bid guarantees would be considered to be restricted cash as it is held in a separate account and is not available for general use by the government.

Any LOC or LOG amounts received into a participant's sub-account are not assets as they are in the form of a commitment but do not represent either cash or the contractual right to receive cash.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred into a participant's sub-account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date as this is a matter of time and the settlement process. Therefore during the settlement process, as cash payments are received from participants and deposited into the participant's escrow settlement account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. After the certification date any cash recognized for successful bid participants would not be considered to be restricted cash as it is no longer required to be returned to the bidder and is no longer externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province from the certification date neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank

account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash". The revenue implications of settlement date and delivery of EAs are discussed in Section 5.

[OR]

~~b)~~ An asset is recognized by the province as cash is transferred to the jurisdiction's escrow settlement account.

Prior to the auction process, the Province does not control the cash ~~proceeds~~or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids, or if their bids are successful and therefore whether the Province has any rights to the escrow proceeds prior to the auction being held. Rather the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. [NTD – to confirm]

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date. This view is supported because the certification process by the Province is considered substantive - the jurisdiction reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Therefore there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. The sale of the EAs is accounted for using "settlement date" accounting in respect of revenue recognition (See discussion on revenue recognition in Section 5 for further analysis).

Once cash has been transferred from participant's sub-account to the jurisdiction's escrow account it is an asset of the Province as it is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the settlement completion date which is a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue. Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) prior to either cash deposit or settlement of the LOC/LOG would not be recognized as an asset of the Province under settlement date accounting. While there is a contract between the participant and the province neither

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party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract. Amounts receivable would only be recognized if the EAs had been delivered prior to receipt of payment. However the settlement process arrangements mean that this does not occur. As there is no amount receivable there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 5 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

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~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

Alternative positions considered and rejected:

[Update with rejected view from above – e.g. participant sub-account recognition vs not on bid guarantee date]

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~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow~~

~~accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 5 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement create a derivative that needs to be recognized as a contract exists from the certification date to the settlement date for the Province to sell the specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting~~

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~~subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

~~c)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~ retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs. This alternative view would be consistent with a view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 4 below.

It was considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. Therefore the right to receive an EA is also not an asset. The Province does not control how many EAs may be received back that can be re-sold (i.e. those remitted for increased compliance obligations) and so any recognition of an asset for the right to receive back was recognized for all EAs, would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not appropriate accounting.

~~d)~~e) Failure of participant to pay increased compliance obligation:

The Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations. As participants can settle their obligations with EAs (including those from a future compliance period) ~~that~~ and EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (c) above there is no asset of the Province until ~~. It is only when~~ a participant has not settled with EAs ~~that~~ and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognized the receivable would be recognized at the amount expected to be received at the time of initial recognition. This would take into account the expected settlement of the receivable. For example, some or part of the amount might be settled by the a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation.

4. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance

PS 1000, Financial statement concepts

PS 3200, Liabilities

PS 3300, Contingent liabilities

PS 3310, Loan guarantees

PS 3450, Financial instruments

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liability for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: ~~**EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement.~~ There may be an implicit loan guarantee by the Province to the extent that there are funds held in escrow for the participants that are not recognized as assets of the Province, but for which the Province may have a duty to repay to the participants in the case of insolvency issues at the escrow agent. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent ~~that there are escrowed proceeds held over a balance sheet date~~such implicit guarantees exist over the balance sheet date disclosures of the implicit loan guarantee should be made, if material.

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~

[NTD – position to be confirmed based on discussion of insolvency risk with DB accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]

Analysis

a) Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.

Once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed for cash or any other financial asset, or exchanged for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~ retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.

Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to ~~deliver~~ transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is ~~Ultimately however, the delivery of free EAs is~~ a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that

liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

~~and is at the discretion of the Province, rather than a contractual or constructive obligation to the participants, as the Province retains discretion over the issuance of free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC not comfortable with the idea there is no obligation to issue free EAs.]~~

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected: ~~It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 5 below.

c) Loan guarantees and contingent liabilities: To the extent that escrow amounts are recognized on the Province's balance sheet there would be a corresponding liability already recognized in respect of the requirement to return the participants deposit or in respect of deferred revenue. However to the extent that participants have submitted cash bid guarantees in Escrow that are not recognized in the Public Accounts of the Province there may an implied guarantee to the participants that their financial assurance will be returned to them if the auction does not run or they are not successful. [TBD – To be supported by facts, if ~~any, that~~any, which indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts.

5. *Revenue recognition under the cap and trade program as sponsoring government*

This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Relevant guidance - See Appendix A for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position –The sale of EAs are exchange transactions.

Analysis:

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

Alternative positions considered and rejected: An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in order to meet their compliance obligations which are created by legislation, and initially EAs are only available

from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.

Revenue recognition for sale of EAs (Exchange transactions)

Relevant guidance - See Appendix A for details.

PS 1000, Financial statement concepts

PS 1150, Generally accepted accounting principles

Other GAAP accounting frameworks

Preliminary position: Revenue is recognized for the sale of EAs on the auction date as there are no further substantive performance obligations by the Province.

Analysis:

a) What is the performance obligation? A performance obligation is defined in IFRS 15/ASC 606 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the PSAS Revenue Statement of Principles which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". This analysis has applied the IFRS concept, as permitted under PS 1150. In both IFRS 15/ASC 606 and the PSAS Revenue Statement of Principles, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the enforceable rights and obligations that are entered into when an auction occurs.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix A for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction, the Province has only one distinct performance obligation to each successful bidder under this contract, which is the delivery of the EAs.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 4 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore ~~this obligation to redeem~~Ontario has no obligation to redeem an EA that ~~cannot arise~~arises from the original exchange transaction and ~~is therefore~~therefore there is ~~not~~no ~~a~~ performance obligation ~~of that transaction~~that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the sale of EAs. Finally, it is noted that there is no legislative provisions for the termination of the program, and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written of implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15/ASC 606 the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400 or IAS 18 there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the PSAS Revenue Statement of Principles proposes a "control" model similar to IFRS 15/ASC 606, so this approach has been applied in the analysis. Under IFRS 15/ASC 606 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15/ASC 606 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the PSAS Revenue Statement of Principles and have been considered in this analysis. See IFRS 15.38 in Appendix A. The indicators have been assessed as follows:

Present right to payment – As noted in Section 3 above, there is considered to be a contract from the auction certification date, and payment must be received by the Province prior to the financial settlement date. ~~present right to payment at the auction date.~~

Legal title to the asset – Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs. ~~Legal title is transferred when~~ Participants can only trade or use the ~~the~~ EAs when they are credited to the participants account. This occurs after the ~~auction certification and~~ settlement process is completed. ~~[MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.

The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the ~~auction~~ date of transfer to their CITSS account, which is the settlement date of the contract. ~~If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value.~~ The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the ~~auction~~transfer into the participant's account. Therefore the participant has access to the rights inherent in the EA only after it has been transferred to their account. ~~While EAs are credited to a participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.

Based on the balance of the indicators above it can be concluded that there is support for recognizing revenue on a "point in time" basis on the ~~auction date~~date when the EAs are transferred to the participant.

Alternatives considered and rejected:

Certification date: It was considered whether revenue should be recognized at a point in time when the contract to purchase/sell the EAs ~~are~~ is agreed upon i.e. the auction certification date (if substantive) or the

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auction date if certification is not substantive. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset", and it could be argued that the delayed delivery of the EAs is only because of the financial settlement process to ensure payment is received and does not indicate that control has not passed earlier. This view was ultimately rejected because of the lack of legal title to the EAs (as they are not "property") and the intangible nature of the EAs means that control cannot be evidenced as passing earlier until the EAs are credited to the participants account.

Trade date accounting: It was considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

~~credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix A for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

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Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. [~~NTD – to confirm that all interested parties agree with this statement~~]

6. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

7. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

8. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

9. Implementation risks and audit considerations

Appendix A – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35-.37. PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not defined under PSAS. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and OS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). After the adoption of PS 3450, which is currently effective for the Province for fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - “Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations.”

PS 3100.04 (a) - “External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used.”

PS 3100.11 - “Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified.”

PS 3100.27-.28 - Designated assets – “...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises....”

Meeting Forward Notification_ OTPP (Legal Opinion) - call with Deloitte (Martin Raymond).rtf

From: Microsoft Outlook []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Meeting Forward Notification: OTPP (Legal Opinion) - call with Deloitte (Martin Raymond)
Date: Saturday, September 10, 2016 14:11:11

Your meeting was forwarded

Hatzis, Len (TBS) has forwarded your meeting request to additional recipients.

Meeting
OTPP (Legal Opinion) - call with Deloitte (Martin Raymond)

Meeting Time
September 10, 2016 2:00 PM-3:00 PM.

Recipients
Killoch, Alex (MOF)

All times listed are in the following time zone: (UTC-05:00) Eastern Time (US & Canada)

Sent by Microsoft Exchange Server 2010

Meeting on Monday at 9_00 a.m..rtf

From: Virani, Shyrose (TBS) []
To: frostcomplex.opps.visitors (MOF) [frostcomplex.opps.visitors@ontario.ca]
CC: christina.chan@ca.ey.com [christina.chan@ca.ey.com]; Stretovitch, Ana (TBS) [Ana.Stretovitch@ontario.ca]
Subject: Meeting on Monday at 9:00 a.m.
Date: Tuesday, February 21, 2017 09:50:25

If you could please her as visitor.

Christina Chan

She is from Ernst and Young

Contact Ana Stretovitch at 416 327 4685 or Shyrose Virani at 416 325 1448

Thanks

Shyrose Virani

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Wednesday, November 23, 2016 11:33:42
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx
Attachment 2: Cap and Trade accounting implications - memorandum to file v5 November 2....docx

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Attachments are “privileged and confidential”

updated memo attached for tomorrow’s discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario’s Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General’s office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

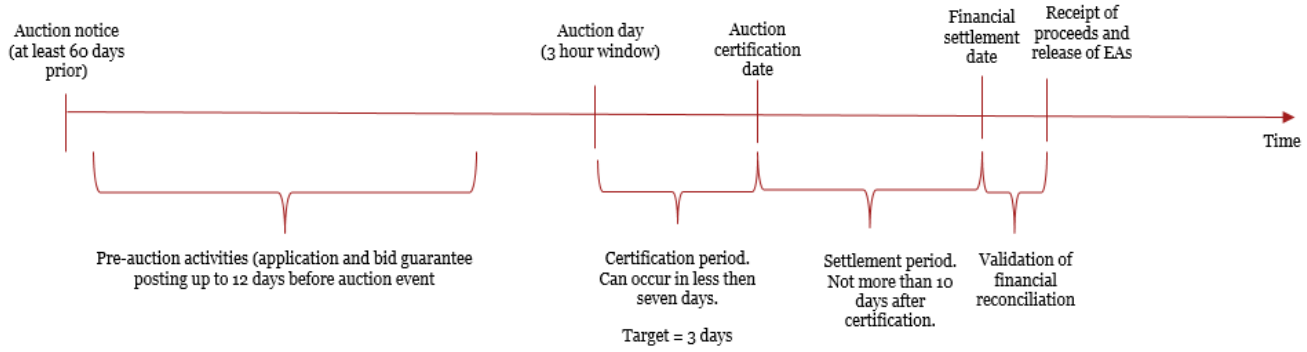
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Cap and Trade accounting implications - memorandum to file v5 November 2....pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [INTD – MOECC to provide comments on accuracy of background terminology]

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The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: ~~There~~In accordance with the Regulations there are four auctions a year. ~~MOECC determines~~ EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, ~~and how many of each "the vintage"~~after the distribution of ~~the EAs is available.~~free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage~~", but more~~". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which

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case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value~~.~~, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

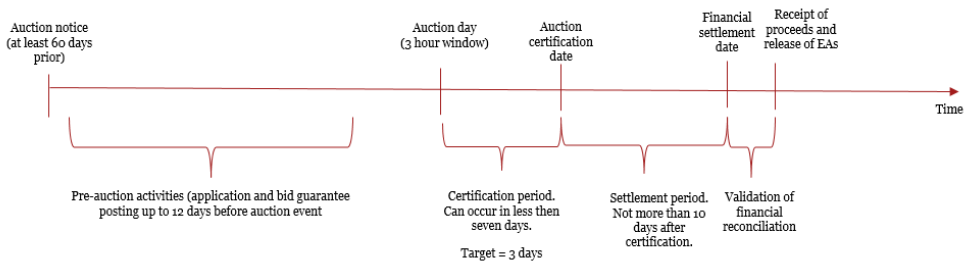
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB~~).~~.) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's regulations.~~regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices~~.~~ by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days~~, in~~ into their sub-account, which ~~case~~ is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once ~~payment has~~all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

~~[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]~~

Auction timeline illustration



Free allowances

~~Mandatory and capped~~Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant~~.~~ and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period~~.~~ (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations~~.~~ and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If

they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits ~~for early action~~" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall~~.~~, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities

of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

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- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

~~3.~~4. *Identification of assets relating to the cap and trade program as sponsoring government*

Summary of relevant guidance – See Appendix ~~A~~C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation ~~and sales~~ of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction~~transfer of funds into the Province's escrow settlement account.

   ~~On the~~After auction ~~date, a receivable~~certification cash from successful bidders is ~~recognized by the Province for the sale of EAs.~~transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized ~~in Revenue~~as deferred revenue until the contract is settled by the transfer of EAs to the participants (see ~~Part 5).~~section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

~~c)~~d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

~~d)~~e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

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Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date:*~~

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr ~~Receivable (from successful participants/Escrowed amounts)~~

~~Cr Revenue~~

~~Dr Cost of sales~~Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

~~*On settlement date:*~~

~~Dr Cash~~

~~Cr Receivable (~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants~~/Escrowed amounts~~

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

~~*Analysis*~~

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a) On creation ~~and sales~~ of free and auctioned EAs:

EAs are "goods" created to be sold or distributed to participants~~. These~~ (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. ~~Therefore despite being intangible in nature,~~ PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs ~~also~~therefore meet the definition of inventories held-for-sale ~~and~~as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

~~EAs that are returned to the government and not cancelled due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).~~ PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory. ~~[ASK MOECC CREATION PROCESS – EXPECTATION IS THAT NO FIXED PRODUCTION OVERHEADS EITHER – ALL WOULD BE GENERAL MANAGEMENT I.E. IF NO PRODUCTION OCCURRED WOULD ANY OVERHEAD COSTS BE ELIMINATED.]~~

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~ EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for

production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead to~~provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the ~~proceeds~~ cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids~~, or~~ and therefore if their bids are successful ~~and therefore whether~~. Only successful bids give the Province ~~has~~ any rights to the escrow proceeds ~~prior to the auction being held. Rather~~. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed ~~amounts. [NTD – to confirm]~~cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a~~

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

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~~market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

~~*Measurement of receivable:* The receivable would be measured at the auction price, being the amount of consideration expected to be received from the sale. Due to the bid guarantees it would be expected that the full auction price would be received. [IF EXPOSED TO DB CREDIT RISK MAY NEED TO ADD SOMETHING REGARDING BAD DEBT EXPENSE]~~

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the

restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected: ~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province~~It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders~~, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued

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that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected: ~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

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~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

~~e)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can

deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs~~. This alternative view would be consistent with a~~ as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section ~~4~~5 below~~.~~ and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. ~~Therefore~~ The only exception is when EAs for a future compliance period are received as part of the ~~right to receive an EA is also not an asset. The~~3 for 1 increased compliance obligation as these may be

re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold ~~(i.e. those remitted~~ or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations~~) and so any~~. Any recognition of an asset for the right to receive back ~~was recognized for~~ applied to all EAs~~,~~ would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not ~~appropriate accounting~~a fair presentation.

~~d)~~e) Failure of participant to pay increased compliance obligation:

~~The~~An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations~~. As participants~~ as they can ~~settle their obligations with~~purchase additional EAs ~~that~~on the market at the market price. EAs do not enhance or create expected economic future benefits for the government~~. It~~ for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is ~~only when~~linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs ~~that~~and under legislation the Province has a right to demand cash as settlement of the compliance obligation~~.~~ (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: ~~The~~ There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues*. However, it would be consistent with PS 3510 and other standard to recognize the receivable ~~would be recognized~~ at the amount expected to ~~-~~be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

~~4.~~5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial ~~liability~~liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub-accounts.

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~~*Analysis*Loan guarantees and contingent liabilities: **EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent that there are escrowed proceeds held over a balance sheet date disclosures of the implicit loan guarantee should be made, if material.~~

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~
~~[NTD – position to be confirmed based on discussion of insolvency risk with DB~~

~~c)~~ Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once~~accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]~~

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~~*Analysis*~~

a) ~~Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.~~

a) ~~Once~~ the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them ~~in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed~~ for cash or any other financial asset, or ~~exchanged~~exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

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After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach ~~and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.~~. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

~~Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as~~

there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to deliver transfer "goods" (being the free EAs) in total or to specific participants. Ultimately however, the The delivery of free EAs is a transition mechanism and is at the discretion of the Province, rather than a contractual or constructive obligation non-reciprocal (as opposed to the participants, as the Province retains discretion over the issuances sale of EAs which is a reciprocal transaction). The transfer of free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC EAs is not comfortable with the idea technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is no an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs]. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

~~*Alternative positions considered and rejected:* It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the

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Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section ~~5~~6 below.

~~c) Loan guarantees and contingent liabilities: [TBD – To be supported by facts, if any, that indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]~~

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~5.~~6. Revenue recognition under the cap and trade program as sponsoring government

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This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix AC for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position – The sale of EAs are exchange transactions.

***Analysis*:**

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

***Alternative positions considered and rejected*:** An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in

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~~order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.~~

~~Revenue recognition for sale of EAs (Exchange transactions)~~

~~*Relevant guidance* - See Appendix A for details.~~

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

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Preliminary position: Revenue is recognized for the sale of EAs on the ~~auction~~ date of delivery of the EAs as ~~there are no further substantive~~this is when the performance ~~obligations~~obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation~~?~~ for the sale of EAs? A performance obligation is defined in IFRS 15~~/ASC 606~~ a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". ~~This~~The following analysis has applied the IFRS concept, as permitted under PS 1150.

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~~a)~~ In both IFRS 15~~/ASC 606~~ and the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the ~~standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the~~

~~enforceable rights and obligations that are entered into when an auction occurs.~~auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix ~~A~~C for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction~~,~~ as confirmed in the auction certification process. The Province has ~~only one~~ distinct performance ~~obligation~~obligations to deliver each EA to each successful bidder under ~~this contract, which is the delivery of the EAs~~these contracts.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in ~~4~~5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions~~.~~ as settlement of their compliance obligations. Therefore ~~this~~Ontario has no obligation to redeem ~~cannot arise~~an EA that arises from the original exchange transaction and ~~is~~ therefore ~~not a~~there is no performance obligation ~~of~~ that ~~transaction~~exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at

auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program~~,~~ and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written ~~of~~or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15~~/ASC 606~~ the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP proposes a "control" model similar to IFRS 15~~/ASC 606~~, so this approach has been applied in the analysis. Under IFRS 15~~/ASC 606~~ an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15~~/ASC 606~~ provides indicators of when a point-in-time obligation has been satisfied. These are also included in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP and have been considered in this analysis. See IFRS 15.38 in Appendix ~~A~~C. The indicators have been assessed as follows:

~~Present right to payment – As noted in Section 3 above, there is a present right to payment at the auction date.~~

~~Legal title to the asset – Legal title is transferred when the EAs are credited to the participants account. This occurs after the auction certification and settlement process is completed. [MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

~~The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.~~

~~The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the auction date. If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the auction. While EAs are credited to a~~

~~participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

~~The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.~~

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset. Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or	Possibly – the price	Yes – From this date	N/A already met	N/A already met

suffering from the fluctuations in the market price of EAs	that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.		

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the ~~auction date.~~date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected: ~~It was considered whether revenue should be recognized at a point in time when the EAs are credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

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Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for

participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.

- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix ~~A~~C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. ~~[NTD – to confirm that all interested parties agree with this statement]~~

~~6.~~7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

~~7.~~8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

~~8.~~9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

~~9.~~10. Implementation risks and audit considerations

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Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

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Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35~~-.37.~~.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not ~~defined under PSAS.~~specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and ~~OS~~PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). ~~After the adoption of PS 3450, which is currently effective for the Province for~~

~~fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.~~

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

~~PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).~~

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

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Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Hewitt, Myra (MOECC) [Myra.Hewitt@ontario.ca]; Beaton, Sheri (MOECC) [Sheri.Beaton@ontario.ca]; Pearson, Heather (MOECC) [Heather.E.Pearson@ontario.ca]
CC: Sawosch, Mercedes (TBS) [Mercedes.Sawosch@ontario.ca]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]; Lau, Lucia (MOECC) [Lucia.Lau@ontario.ca]; Lugo, Grace (MOECC) [Grace.Lugo@ontario.ca]; Chiu, Jenny (MOECC) [Jenny.Chiu@ontario.ca]; Kamaratakis, Toula (MOECC) [Toula.Kamaratakis@ontario.ca]; Hurdman, Jeff (MOECC) [Jeff.Hurdman@ontario.ca]; Tiffin, Dave (MOECC) [Dave.Tiffin@ontario.ca]; Molnar, Adrienne (MOECC) [Adrienne.Molnar@Ontario.ca]; Lo, Rudy (MOECC) [Rudy.Lo@ontario.ca]; david.c.greenall@pwc.com [david.c.greenall@pwc.com]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Wednesday, November 23, 2016 11:33:42
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx
Attachment 2: Cap and Trade accounting implications - memorandum to file v5 November 2....docx

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Attachments are “privileged and confidential”

updated memo attached for tomorrow’s discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario’s Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General’s office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

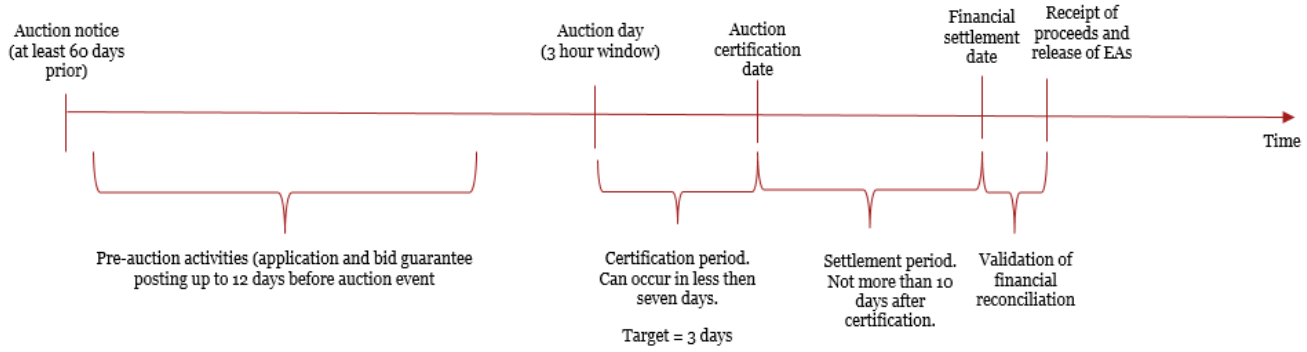
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Cap and Trade accounting implications - memorandum to file v5 November 2....pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [INTD – MOECC to provide comments on accuracy of background terminology]

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The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: ~~There~~In accordance with the Regulations there are four auctions a year. ~~MOECC determines~~ EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, ~~and how many of each "the vintage"~~after the distribution of ~~the EAs is available.~~free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage~~", but more~~". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which

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case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value~~.~~, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

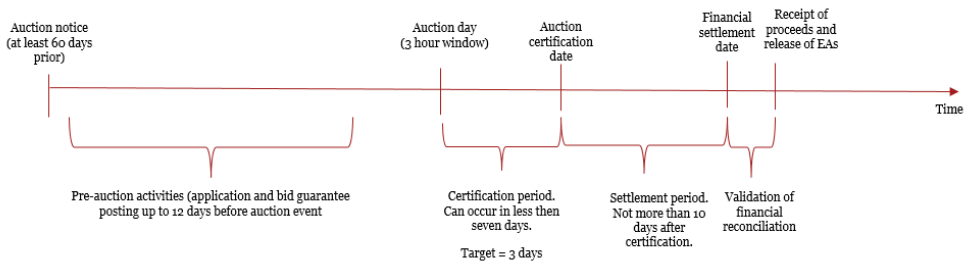
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB~~).~~.) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's regulations.~~regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices~~.~~ by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days~~, in~~ into their sub-account, which ~~case~~ is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once ~~payment has~~all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

~~[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]~~

Auction timeline illustration



Free allowances

~~Mandatory and capped~~Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant~~.~~ and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period~~.~~ (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations~~.~~ and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If

they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits ~~for early action~~" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall~~.~~, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities

of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

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- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

~~3.~~4. *Identification of assets relating to the cap and trade program as sponsoring government*

Summary of relevant guidance – See Appendix ~~A~~C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation ~~and sales~~ of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction~~transfer of funds into the Province's escrow settlement account.

   ~~On the~~After auction ~~date, a receivable~~certification cash from successful bidders is ~~recognized by the Province for the sale of EAs.~~transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized ~~in Revenue~~as deferred revenue until the contract is settled by the transfer of EAs to the participants (see ~~Part 5).~~section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

~~c)~~d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

~~d)~~e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

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Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date:*~~

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr ~~Receivable (from successful participants/Escrowed amounts)~~

~~Cr Revenue~~

~~Dr Cost of sales~~Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

~~*On settlement date:*~~

~~Dr Cash~~

~~Cr Receivable (~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants~~/Escrowed amounts~~

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

~~*Analysis*~~

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a) On creation ~~and sales~~ of free and auctioned EAs:

EAs are "goods" created to be sold or distributed to participants~~. These~~ (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. ~~Therefore despite being intangible in nature,~~ PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs ~~also~~therefore meet the definition of inventories held-for-sale ~~and~~as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

~~EAs that are returned to the government and not cancelled due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).~~ PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory. ~~[ASK MOECC CREATION PROCESS – EXPECTATION IS THAT NO FIXED PRODUCTION OVERHEADS EITHER – ALL WOULD BE GENERAL MANAGEMENT I.E. IF NO PRODUCTION OCCURRED WOULD ANY OVERHEAD COSTS BE ELIMINATED.]~~

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~ EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for

production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead to~~provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the ~~proceeds~~ cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids~~, or~~ and therefore if their bids are successful ~~and therefore whether~~. Only successful bids give the Province ~~has~~ any rights to the escrow proceeds ~~prior to the auction being held. Rather~~. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed ~~amounts. [NTD – to confirm]~~cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a~~

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

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~~market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

~~*Measurement of receivable:* The receivable would be measured at the auction price, being the amount of consideration expected to be received from the sale. Due to the bid guarantees it would be expected that the full auction price would be received. [IF EXPOSED TO DB CREDIT RISK MAY NEED TO ADD SOMETHING REGARDING BAD DEBT EXPENSE]~~

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the

restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected: ~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province~~It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders~~, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued

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that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected: ~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

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~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

~~e)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can

deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs~~. This alternative view would be consistent with a~~ as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section ~~4~~5 below~~.~~ and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. ~~Therefore~~ The only exception is when EAs for a future compliance period are received as part of the ~~right to receive an EA is also not an asset. The~~3 for 1 increased compliance obligation as these may be

re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold ~~(i.e. those remitted~~ or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations~~) and so any~~. Any recognition of an asset for the right to receive back ~~was recognized for~~ applied to all EAs~~,~~ would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not ~~appropriate accounting~~a fair presentation.

~~d)~~e) Failure of participant to pay increased compliance obligation:

~~The~~An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations~~. As participants~~ as they can ~~settle their obligations with~~purchase additional EAs ~~that~~on the market at the market price. EAs do not enhance or create expected economic future benefits for the government~~. It~~ for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is ~~only when~~linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs ~~that~~and under legislation the Province has a right to demand cash as settlement of the compliance obligation~~.~~ (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: ~~The~~ There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues*. However, it would be consistent with PS 3510 and other standard to recognize the receivable ~~would be recognized~~ at the amount expected to ~~-~~be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

~~4.~~5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial ~~liability~~liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub-accounts.

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~~*Analysis*Loan guarantees and contingent liabilities: **EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent that there are escrowed proceeds held over a balance sheet date disclosures of the implicit loan guarantee should be made, if material.~~

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~
~~[NTD – position to be confirmed based on discussion of insolvency risk with DB~~

~~c)~~ Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once~~accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]~~

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~~*Analysis*~~

a) ~~Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.~~

a) ~~Once~~ the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them ~~in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed~~ for cash or any other financial asset, or ~~exchanged~~exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

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After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach ~~and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.~~. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

~~Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as~~

there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to deliver transfer "goods" (being the free EAs) in total or to specific participants. Ultimately however, the The delivery of free EAs is a transition mechanism and is at the discretion of the Province, rather than a contractual or constructive obligation non-reciprocal (as opposed to the participants, as the Province retains discretion over the issuances sale of EAs which is a reciprocal transaction). The transfer of free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC EAs is not comfortable with the idea technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is no an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs]. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

~~*Alternative positions considered and rejected:* It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the

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Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section ~~5~~6 below.

~~c) Loan guarantees and contingent liabilities: [TBD – To be supported by facts, if any, that indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]~~

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~5.~~6. Revenue recognition under the cap and trade program as sponsoring government

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This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix AC for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position – The sale of EAs are exchange transactions.

***Analysis*:**

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

***Alternative positions considered and rejected*:** An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in

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~~order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.~~

~~Revenue recognition for sale of EAs (Exchange transactions)~~

~~*Relevant guidance* - See Appendix A for details.~~

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

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Preliminary position: Revenue is recognized for the sale of EAs on the ~~auction~~ date of delivery of the EAs as ~~there are no further substantive~~this is when the performance ~~obligations~~obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation~~?~~ for the sale of EAs? A performance obligation is defined in IFRS 15~~/ASC 606~~ a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". ~~This~~The following analysis has applied the IFRS concept, as permitted under PS 1150.

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~~a)~~ In both IFRS 15~~/ASC 606~~ and the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the ~~standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the~~

~~enforceable rights and obligations that are entered into when an auction occurs.~~auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix ~~A~~C for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction~~,~~ as confirmed in the auction certification process. The Province has ~~only one~~ distinct performance ~~obligation~~obligations to deliver each EA to each successful bidder under ~~this contract, which is the delivery of the EAs~~these contracts.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in ~~4~~5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions~~.~~ as settlement of their compliance obligations. Therefore ~~this~~Ontario has no obligation to redeem ~~cannot arise~~an EA that arises from the original exchange transaction and ~~is~~ therefore ~~not a~~there is no performance obligation ~~of~~ that ~~transaction~~exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at

auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program~~,~~ and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written ~~of~~or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15~~/ASC 606~~ the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP proposes a "control" model similar to IFRS 15~~/ASC 606~~, so this approach has been applied in the analysis. Under IFRS 15~~/ASC 606~~ an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15~~/ASC 606~~ provides indicators of when a point-in-time obligation has been satisfied. These are also included in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP and have been considered in this analysis. See IFRS 15.38 in Appendix ~~A~~C. The indicators have been assessed as follows:

~~Present right to payment – As noted in Section 3 above, there is a present right to payment at the auction date.~~

~~Legal title to the asset – Legal title is transferred when the EAs are credited to the participants account. This occurs after the auction certification and settlement process is completed. [MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

~~The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.~~

~~The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the auction date. If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the auction. While EAs are credited to a~~

~~participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

~~The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.~~

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset. Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or	Possibly – the price	Yes – From this date	N/A already met	N/A already met

suffering from the fluctuations in the market price of EAs	that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.		

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the ~~auction date.~~date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected: ~~It was considered whether revenue should be recognized at a point in time when the EAs are credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

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Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for

participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.

- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix ~~A~~C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. ~~[NTD – to confirm that all interested parties agree with this statement]~~

~~6.~~7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

~~7.~~8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

~~8.~~9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

~~9.~~10. Implementation risks and audit considerations

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Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

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Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35~~-.37.~~.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not ~~defined under PSAS.~~specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and ~~OS~~PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). ~~After the adoption of PS 3450, which is currently effective for the Province for~~

~~fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.~~

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

~~PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).~~

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

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Meeting to review proposed Cap and Trade accounting.rtf

From: Hewitt, Myra (MOECC) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Tiffin, Dave (MOECC) [Dave.Tiffin@ontario.ca]; david.c.greenall@ca.pwc.com [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Lugo, Grace (MOECC) [Grace.Lugo@ontario.ca]; Pearson, Heather (MOECC) [Heather.E.Pearson@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Hurdman, Jeff (MOECC) [Jeff.Hurdman@ontario.ca]; Chiu, Jenny (MOECC) [Jenny.Chiu@ontario.ca]; Lau, Lucia (MOECC) [Lucia.Lau@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; lucy.durocher@pwc.com [lucy.durocher@pwc.com]; Sawosch, Mercedes (TBS) [Mercedes.Sawosch@ontario.ca]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; michael.hawtin@pwc.com [michael.hawtin@pwc.com]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Beaton, Sheri (MOECC) [Sheri.Beaton@ontario.ca]; Kamaratakis, Toula (MOECC) [Toula.Kamaratakis@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Wednesday, November 23, 2016 11:11:51

Heather is tied up for a few more minutes. We will be joining very shortly.

Organizer: Virani, Shyrose (TBS)
When: 10:00 AM - 12:00 PM November 23, 2016
Subject: Meeting to review proposed Cap and Trade accounting
Location: APFR boardroom, 7 Queen's Park Crescent, 2nd floor, teleconference 416 212 8014 passcode 1474532#

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]; Lloyd, Patti (TBS) [Patti.Lloyd@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Tuesday, November 22, 2016 16:28:29
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx

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updated memo attached for tomorrow's discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

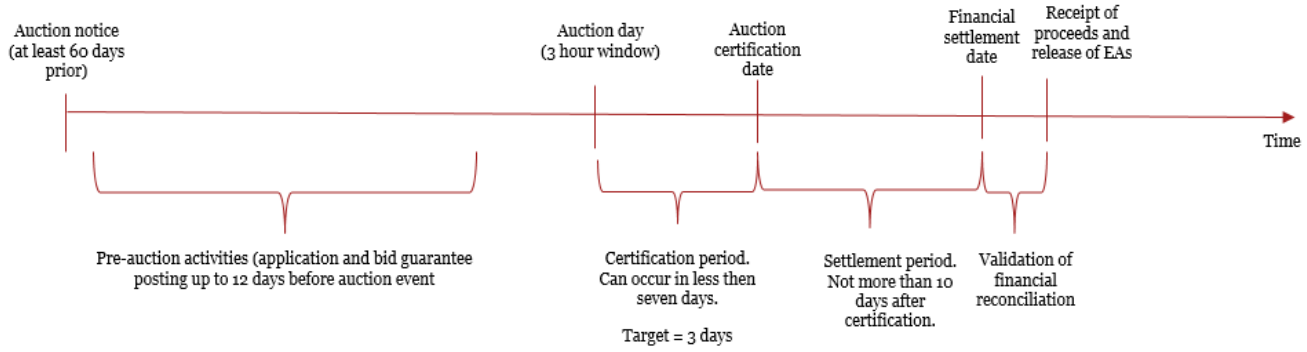
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Hewitt, Myra (MOECC) [Myra.Hewitt@ontario.ca]; Beaton, Sheri (MOECC) [Sheri.Beaton@ontario.ca]; Pearson, Heather (MOECC) [Heather.E.Pearson@ontario.ca]
CC: Sawosch, Mercedes (TBS) [Mercedes.Sawosch@ontario.ca]; 'lucy.durocher@pwc.com' [lucy.durocher@pwc.com]; 'michael.hawtin@pwc.com' [michael.hawtin@pwc.com]; Lau, Lucia (MOECC) [Lucia.Lau@ontario.ca]; Lugo, Grace (MOECC) [Grace.Lugo@ontario.ca]; Chiu, Jenny (MOECC) [Jenny.Chiu@ontario.ca]; Kamaratakis, Toula (MOECC) [Toula.Kamaratakis@ontario.ca]; Hurdman, Jeff (MOECC) [Jeff.Hurdman@ontario.ca]; Tiffin, Dave (MOECC) [Dave.Tiffin@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Tuesday, November 22, 2016 16:28:29
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx

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updated memo attached for tomorrow's discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

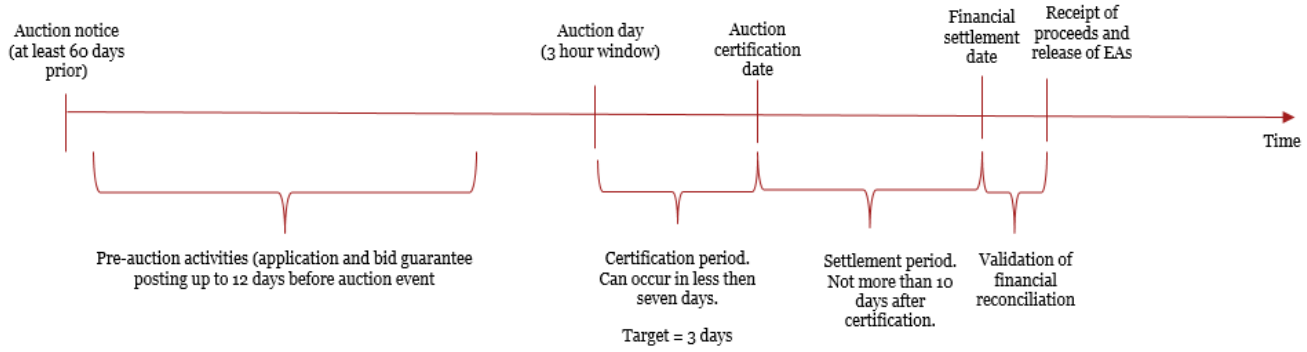
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Hewitt, Myra (MOECC) [Myra.Hewitt@ontario.ca]; Beaton, Sheri (MOECC) [Sheri.Beaton@ontario.ca]; Pearson, Heather (MOECC) [Heather.E.Pearson@ontario.ca]
CC: Sawosch, Mercedes (TBS) [Mercedes.Sawosch@ontario.ca]; lucy.durocher@pwc.com [lucy.durocher@pwc.com]; michael.hawtin@pwc.com [michael.hawtin@pwc.com]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Tuesday, November 22, 2016 12:13:05
Attachment 1: Cap and Trade accounting implications - memo for Nov 23 meeting.docx

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updated memo attached for tomorrow's discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo for Nov 23 meeting.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

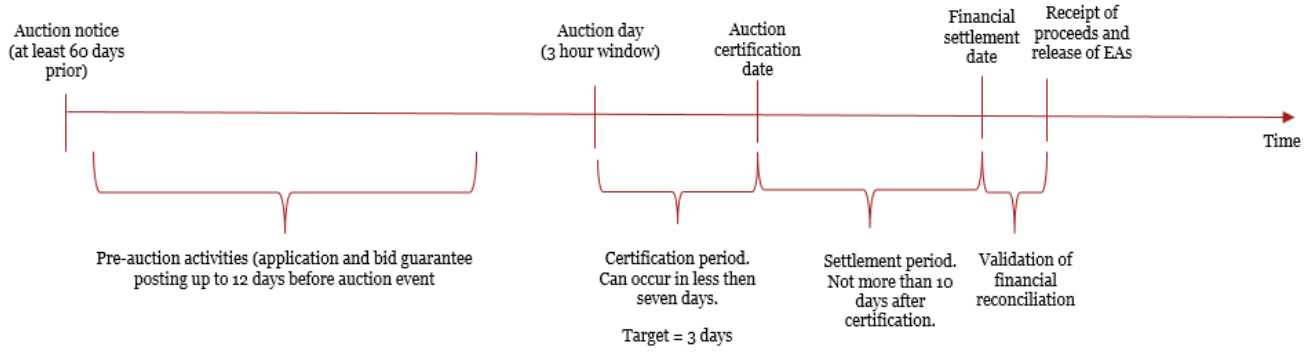
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Hewitt, Myra (MOECC) [Myra.Hewitt@ontario.ca]
CC: Sawosch, Mercedes (TBS) [Mercedes.Sawosch@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Tuesday, November 15, 2016 13:38:38

Myra/Doris

Pls extend the invite to appropriate staff.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
Shyrose

As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario's Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General's office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Meeting to review proposed Cap and Trade accounting.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Graham, Helen (TBS) [Helen.Graham@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; Chen, Doris (MOECC) [Doris.Chen@ontario.ca]; Hewitt, Myra (MOECC) [Myra.Hewitt@ontario.ca]
Subject: Meeting to review proposed Cap and Trade accounting
Date: Tuesday, November 15, 2016 13:32:50

Myra/Doris

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Meeting to review proposed Cap and Trade accounting.pdf

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Graham, Helen (TBS); Keates, James (TBS); Li, Wendy (TBS); Provis, Ian (TBS); Saboor, Ibrahim (TBS); lucy.durocher@ca.pwc.com; michael.hawtin@ca.pwc.com; "david.c.greenall@ca.pwc.com"; Chen, Doris (MECP); Hewitt, Myra (MECP); Beaton, Sheri (MECP); Pearson, Heather (MECP)
Cc:	Sawosch, Mercedes (TBS); "lucy.durocher@pwc.com"; "michael.hawtin@pwc.com"; Lau, Lucia (MECP); Lugo, Grace (MECP); Chiu, Jenny (MECP); Kamaratakis, Toula (MECP); Hurdman, Jeff (MECP); Tiffin, Dave (MECP); Molnar, Adrienne (MECP); Lo, Rudy (MECP); "david.c.greenall@pwc.com"; Taylor, Heather (MECP)
Subject:	Meeting to review proposed Cap and Trade accounting
Start:	November 23, 2016 10:00:00 AM
End:	November 23, 2016 12:00:00 PM
Location:	APFR boardroom, 7 Queen"s Park Crescent, 2nd floor, teleconference 416 212 8014 passcode 1474532#
Attachments:	Cap and Trade accounting implications - memo for Nov 23 meeting.docx Cap and Trade accounting implications - memorandum to file v5 November 2....docx

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Attachments are “privileged and confidential”

updated memo attached for tomorrow’s discussion.

Upon arrival, please call Shyrose Virani at 416 325 1448 to gain entry into our building.

Thanks
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As per recent discussion, this meeting will be to review the proposed accounting treatment for Ontario’s Cap and Trade program. Subject to any changes in the proposed approach, OPCD will initiate a discussion with the Auditor General’s office to review the planned accounting treatment.

Pre-reading materials will be provided in advance of the meeting.

Cap and Trade accounting implications - memo .pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [NTD – *MOECC to provide comments on accuracy of background terminology*]

The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: In accordance with the Regulations there are four auctions a year. EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, after the distribution of free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular

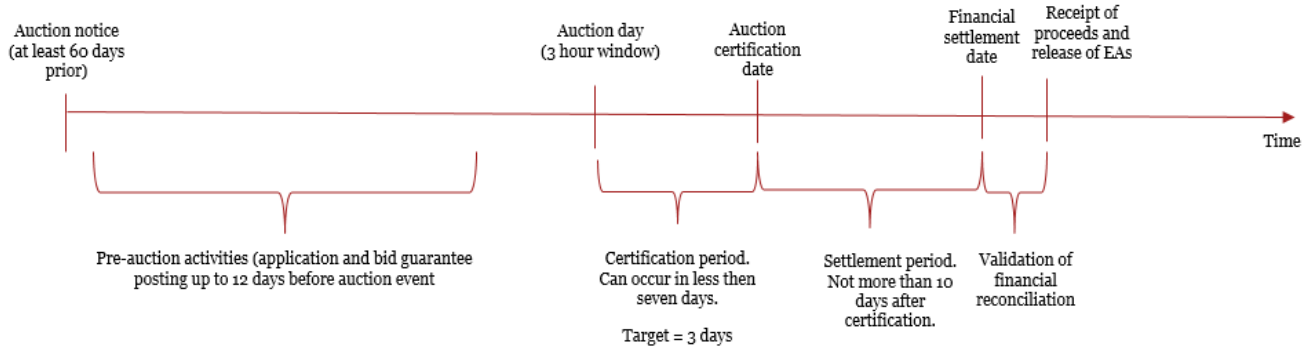
auction may be sold, in which case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province reviews the results for compliance with the regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days into their sub-account, which is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts.

Auction timeline illustration



Free allowances

Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the

participant and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director

under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program

means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction

and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the

payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

4. Identification of assets relating to the cap and trade program as sponsoring government

Summary of relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the transfer of funds into the Province's escrow settlement account.

   After auction certification cash from successful bidders is transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized as deferred revenue until the contract is settled by the transfer of EAs to the participants (see section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

As payment from successful bidders is received and placed into Ontario Settlement account:

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

a) <u>On creation of free and auctioned EAs</u>:

EAs are "goods" created to be sold or distributed to participants (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs therefore meet the definition of inventories held-for-sale as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount. PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory.

EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no

cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids and therefore if their bids are successful. Only successful bids give the Province any rights to the escrow proceeds. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. If no auction occurs for any reason then the Province does not have any right to the escrowed cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected:

It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those

deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected:

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section 5 below and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. The only exception is when EAs for a future compliance period are received as part of the 3 for 1 increased compliance obligation as these may be re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations. Any recognition of an asset for the right to receive back applied to all EAs would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not a fair presentation.

e) Failure of participant to pay increased compliance obligation:

An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations as they can purchase additional EAs on the market at the market price. EAs do not enhance or create expected economic future benefits for the government for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs and under legislation the Province has a right to demand cash as settlement of the compliance obligation (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues.* However, it would be consistent with PS 3510 and other standard to recognize the receivable at the amount expected to be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance

obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub- accounts.

Analysis

a) Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them for cash or any other financial asset, or exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an

Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to transfer "goods" (being the free EAs) in total or to specific participants. The delivery of free EAs is a transition mechanism and is non-reciprocal (as opposed to the sale of EAs which is a reciprocal transaction). The transfer of EAs is not technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section 6 below.

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

6. Revenue recognition under the cap and trade program as sponsoring government

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix C for details.

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

Preliminary position: Revenue is recognized for the sale of EAs on the date of delivery of the EAs as this is when the performance obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) <u>What is the performance obligation for the sale of EAs?</u> A performance obligation is defined in IFRS 15 a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the Revenue SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". The following analysis has applied the IFRS concept, as permitted under PS 1150.

   In both IFRS 15 and the Revenue SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

   Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix C for definition of "distinct goods and services")

   Based on the above analysis, a contract is created when a participant successfully bids at auction as confirmed in the auction certification process. The Province has distinct performance obligations to deliver each EA to each successful bidder under these contracts.

   <u>Alternative positions considered and rejected:</u> It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon

in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in 5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions as settlement of their compliance obligations. Therefore Ontario has no obligation to redeem an EA that arises from the original exchange transaction and therefore there is no performance obligation that exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) <u>When is the performance obligation satisfied?</u> There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15 the performance obligations are satisfied as control

of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the Revenue SOP proposes a "control" model similar to IFRS 15, so this approach has been applied in the analysis. Under IFRS 15 an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15 provides indicators of when a point-in-time obligation has been satisfied. These are also included in the Revenue SOP and have been considered in this analysis. See IFRS 15.38 in Appendix C. The indicators have been assessed as follows:

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset.				

Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or suffering from the fluctuations in the market price of EAs	Possibly – the price that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	Yes – From this date the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	N/A already met	N/A already met

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected:

Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.

- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.
- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the

requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted.

7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

10. Implementation risks and audit considerations

Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049).

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Cap and Trade accounting implications - memor.pdf

Cap and trade accounting implications memorandum to file – proposed outline

1. Executive summary

2. Background and outline of cap and trade legislation and regulations [INTD – MOECC to provide comments on accuracy of background terminology]

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The *Climate Change Mitigation and Low-Carbon Economic Act, 2016* (the "Act") was recently enacted that establishes, amongst other things, a framework for a cap and trade program for the Province of Ontario (the "Province" or "Ontario"). Two regulations, Ontario regulation 144.16 and Ontario regulation 143.16 (together "the Regulations") have been passed under the Act.

Only registered participants to the program (mandatory participants, voluntary participants and market participants) can purchase, hold, sell or trade emission allowances (EAs). Mandatory participants are those that are mandated to participate in the program. Voluntary participants are those that are not mandatory participants but choose to participate in the program for a compliance period. (Voluntary participants may opt out of future compliance periods if they do not meet the criteria to be a mandatory participant for that period). Together mandatory and voluntary participants are referred to as "capped participants" or "capped emitters". Market participants are those that do not have compliance obligations but choose to participate in the program so they can hold, sell and trade EAs.

EAs can be obtained in the following ways:

- Purchased at auctions at the auction price.
- Distribution as a free allowance (~~mandatory~~capped participants only).
- Acquired from other participants in a market trade.

EAs are held in holding accounts that are maintained in the "CITTS" system, which records participant accounts and trades between participants. CITSS is a web-based tool that facilitates participation in the cap and trade program and is administered by the Western Climate Initiative, Inc (WCI Inc) on behalf of participating jurisdictions. Market trades are reported to the MOECC and the MOECC monitors the participant's accounts for compliance with regulations, such as holding levels are within holding limits. If holding limits are exceeded and not remedied within 5 days, the Minister of the Environment and Climate Change (the "Minister") has the ability to remove the excess allowances for no compensation that could then be re-sold at future auctions. However, our understanding is that the systems should not allow sales over the individual limits to be processed so examples of this should be very limited in practice.

Auction process: ~~There~~In accordance with the Regulations there are four auctions a year. ~~MOECC determines~~ EAs are sold at auction classified by "vintage". The Regulations set out how many EAs are created for each vintage and how many EAs of each vintage will be available at each auction, ~~and how many of each "the vintage"~~after the distribution of ~~the EAs is available.~~free EAs. The vintage of an EA determines which compliance period the EA can be submitted for. For example, in 2017 the auctions will be for the "2017" vintage and some for the "2020 vintage~~", but more~~". More than one "vintage" may be sold in any one auction. The first auction will be held March 2017. There is a floor price for each auction. Not all the allowances available at a particular auction may be sold, in which

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case unsold allowances may be offered at a future auction under some circumstances. 5% of EAs are held back as a strategic reserve that may be sold at a later date for a higher value~~.~~, not through the auction process. Only capped emitters may purchase from the reserve. The strategic reserve accumulates over time.

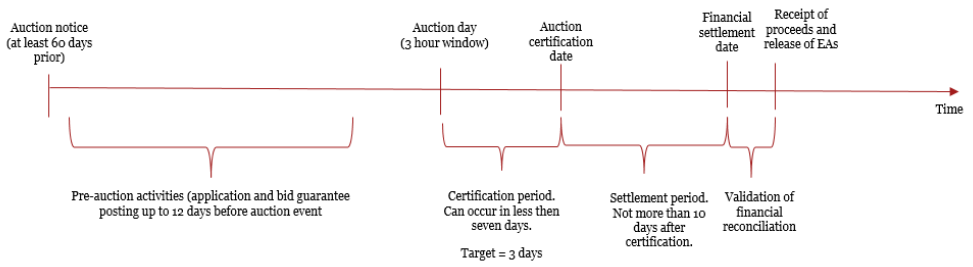
Prior to the auction registered participants must post a bid guarantee. This may be in the form of an irrevocable letter of credit (LOC), letter of guarantee (LOG) or cash, both of which are held in escrow by Deutsche Bank (DB~~).~~.) in the participant's sub-account under the jurisdiction's Escrow account. The Province's escrow account is in the name of WCI, Inc for the benefit of the Ontario Minister of the Environment and Climate Change. The bid guarantee may be posted up to 60 days before the auction, and must exceed the total amount of bids that will be submitted by the participant in the auction.

At the auction the participants place bids for the number of EAs they will purchase at any price point. At the end of the three-hour auction window the auction administrator runs the auction algorithm through a predetermined auction settlement calculation to provide the auction result report indicating the set of successful participants and the number of allowances they won at the auction settlement price.

After the auction, the Province ~~(and a market monitor, for WCI auctions)~~ reviews the results for compliance with the ~~Province's regulations.~~regulatory requirements over the auction process and to obtain the required internal jurisdiction approvals. These steps include reviewing the auction results provided by the auction platform, analyzing bid data in detail and reviewing and accepting the auction report submitted by the market monitor (a third party contractor called Monitoring Analytics). When the results of the auction are confirmed (the "certification date") the results are published on the jurisdiction's website, invoices made available to participants and the process of settlement begins. If a participant is successful in the auction then the participant is invoiced for the amounts due for the EAs purchased. If the participant submitted a cash bid guarantee this cash amount is used to settle the invoices~~.~~ by the amounts being transferred from the participant's sub-account into Ontario's escrow settlement account. If an LOC or LOG was used, the participant can pay separately within 7 days~~, in~~ into their sub-account, which ~~case~~ is then transferred to Ontario's escrow settlement account and the LOC is dissolved or returned. Alternatively if the participant does not submit cash payment within 7 days the invoice is settled by calling on the LOC or LOG. Once ~~payment has~~all the payments have been received from participants and transferred to Ontario's escrow settlement accounting and Ontario's staff have confirmed that the amount in the escrow account match payments due from auction participants, then the escrowed amounts are transferred to the GGRA bank account and the EAs are transferred to the respective participant CITSS accounts. ~~[Question for MOECC – up to the date of auction can a registered participant remove themselves from the auction and get back their cash/LOC or are they locked in until after the auction date?]~~

~~[o/s is to determine if there is an insolvency risk prior to the auction period; if there is, has the Province effectively guaranteed the return of the bid collateral if the escrow holder became insolvent]~~

Auction timeline illustration



Free allowances

~~Mandatory and capped~~Capped emitters may receive free allowances. To receive free allowances the participant must apply each year. The amounts of these are determined by the Minister using formulas applied to the entity specific situation of the participant~~.~~ and are expected to diminish over time as transition to the cap and trade program is completed and inter-provincial "leakage" declines (leakage is where carbon producers move economic activities to a jurisdiction with no or low carbon pricing). Once issued, these EAs are identical to those sold at auction and may be held or traded by participants.

Emissions Compliance

The program operates within 3-year compliance periods (with the first period being a 4-year period). The first compliance period runs from January 1, 2017 – December 31, 2020. EAs are linked to a specific compliance period. For example, EAs with 2021-2023 vintages cannot be used to meet normal emissions obligations under the program for the 2017-2020 compliance period~~.~~ (although they can be used to settle increased compliance obligations). However, EAs from earlier vintages can be carried forward to meet obligations in future compliance periods. EAs do not expire. Participants may purchase EAs from other participants in market trades to be able to meet their obligations. Market trades are negotiated between participants and are then reported to the MOECC, who ensures that the agreed upon EAs or credits are transferred between the participants CITSS accounts. The number of EAs ~~available~~issued for the compliance period is capped by regulation. Therefore if total emissions from all participants are significantly lower than the cap, it should be easy for participants to obtain the necessary EAs in the marketplace at an inexpensive price. Unused EAs for the compliance period can be carried forward and used in future compliance periods. If the total emissions from all participants exceed the cap then there will not be sufficient EAs available for all participants to meet their compliance obligations~~.~~ and the price of any available EAs will increase. The market mechanism allows those participants who can most cheaply reduce their emissions an incentive to do so in order to either sell excess EAs to other participants at a higher price or to save the need to purchase a high priced EA to meet their obligations.

At the end of the compliance period mandatory and voluntary participants report their attributed carbon emissions (greenhouse gas emissions must be quantified, reported and verified) for the compliance period and ensure they have transferred sufficient EAs or credits (see below) from their holding accounts into their compliance accounts. At the compliance "true-up" deadline (by November 2021 for the first compliance period), EAs and offset credits (see below) are removed in a number equal to the participant's obligations under the Regulations (1 EA per 1 tonne of emissions). If a participant does not have sufficient EAs in their account at the true-up date then there is a shortfall. In addition to the EAs required to fulfil the shortfall, the obligation increases on a 3-1 basis; for each EA required to cover the shortfall the participant is required to acquire and submit an additional 3 EAs (the "increased compliance obligation"). This increased compliance obligation may be settled with EAs from future vintages (e.g. 2021 vintages may be used to settle the increased compliance obligation for the 2017-2020 period, however, they cannot be used to settle the original compliance obligation or shortfall).

Due to the increased compliance obligation mechanism if a participant does not expect to have sufficient EAs in their compliance accounts at the true-up deadline there is an incentive for participants to either reduce their emissions over the compliance period or to purchase additional EAs (of vintages valid for the compliance period) in the market prior to the true-up deadline; the market price of which would be expected to increase due to demand exceeding supply.

The EAs that are remitted to the MOECC for a compliance period are ~~cancelled~~retired. They are not re-sold. The exception to this is EAs that are remitted as part of the increased compliance obligation may be re-sold at auction. The purpose of the exception is so that the overall number of available EAs for future compliance periods is not reduced because of the failure of participants to comply at the true-up date.

A participant has a certain period of time (30 days after a notice of a shortfall is issued) to acquire and remit sufficient EAs to meet their compliance obligation, including additional compliance obligations for shortfalls. If

they fail to remedy the shortfall, the Director can issue an order that the outstanding obligation be settled in cash to the Ministry of Finance, based on the settlement price from the most recent auction.

The removal of EAs from a participant's account is without payment to the participant. Specifically Section 70 (3) of the Act states that "No amount is payable by the Crown with respect to any action taken by the Minister or Director under this Act, or by any person acting on their behalf, including any action relating to the removal of emission allowances and credits from a participant's cap and trade accounts".

Credits and offsets

Other than EAs, entities may also obtain "early reduction credits ~~for early action~~" or "offset credits" in certain circumstances. These credits are also tracked by participant and can be used in place of EAs to settle a compliance obligation. Credits can also be sold or purchased by participants on the market. There are limits on how much of a compliance obligation can be settled with credits as opposed to EAs. As emissions can be settled by either EAs or credits and offsets, the creation of credits or offsets essentially increases the total "cap" amount of emissions under the cap and trade program for the compliance period.

Linking to the Western Climate Initiative (WCI)

It is anticipated that Ontario will link to the WCI in 2018. The WCI currently includes Quebec and California. When linked to the WCI, there will be one market for EAs – all participants from participating jurisdictions can buy, sell, hold and trade EAs with other participants. There is one auction process for all participating jurisdictions, with proceeds from the auction being allocated on a pro-rata basis. For example, each jurisdiction determines the number of EAs that they will put up for auction in that vintage based on their cap for the compliance period. This results in a total amount of EAs available of which, say 30% are part of the Ontario emissions cap, 15% for Quebec and 55% for California. The proceeds of the auction would be split 30:15:55 between the participating jurisdictions, regardless of which participants purchase the EAs. If not all the EAs are sold, the sales are attributed on these same rations and unsold EAs from the jurisdiction may be sold at future auctions under certain conditions. EAs are not attributed back to a jurisdiction of issuance and can be used to settle a compliance obligation in any of the participating jurisdictions. For example, an Ontario participant must ensure there are an adequate number of EAs or credits in their compliance account to meet their compliance obligation based on their emissions. It does not matter whether they purchased the EAs at auction or from a California or Quebec participant. The effect is that Ontario participants may produce emissions that exceed the Ontario cap for any compliance period, but this excess would be offset by reductions in Quebec or California below their caps, thus reducing emissions overall~~.~~, and in the jurisdiction where the reduction is the cheapest (most efficient). There is no mechanism by which Ontario transfers or receives cash, financial assets or EAs between jurisdictions. There is no requirement to redeem EAs issued in other jurisdictions by issuing cash or other "Ontario" EAs as all EAs are interchangeable once issued.

Termination of the program

The program does not have a termination date. There is nothing in the current legislation that outlines how the cap and trade program might be terminated. The program could only be terminated through a change in the legislation. We are not aware of any terms in the arrangements with the WCI that would specify how a withdrawal from the WCI might be undertaken.

Greenhouse Gas Reduction Account

The Act establishes an account with the Public Accounts of Ontario called the Greenhouse Gas Reduction Account (GGRA). ~~Any~~Other than limited exceptions, proceeds from the distribution of EAs are included in this account. Amounts of fees, penalties and the settlement of increased compliance obligations in cash are also included in the GGRA. The funds in the GGRA may be used for initiatives that are reasonably likely to reduce, or support the reduction of, greenhouse gases. Such uses include the research and development of new technologies or processes, innovation, education and training, and informing the public. The amounts in the GGRA may also be used to fund costs of administration and enforcement of the Act. Annually, the Minister will issue a public notice regarding the evaluation of initiatives funded by the GGRA. In addition an annual report will be prepared describing the activities

of the GGRA. Eligible costs that were incurred by the Crown on or after November 1, 2015 may be reimbursed from the GGRA, even if they were incurred prior to the Act coming into force.

Federal actions to reduce carbon emissions

In October 2016 the federal government announced that Canadian provinces that do not have a carbon pricing mechanism will be subject to a federal benchmark "floor price" for carbon in 2018. Ontario's cap and trade program means that it will not be subject to the federal carbon floor price as the Ontario targets are in excess of the targets imposed by the federal government. As such, actions by the federal government are not expected to have an impact on Ontario's cap and trade program. This must be monitored as subsequent federal actions and/or changes to Ontario's cap and trade program in response to the federal government actions may have accounting impacts.

3. What is the nature of EAs

Relevant guidance - See Appendix C for details.

PS 3450, Financial Instruments ("PS 3450") (effective for years on or after April 1, 2019)

PS 3510, Tax revenue ("PS 3510") (for definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles ("Revenue SOP") (non-authoritative due process document)

IPSASB staff paper "Emissions Trading Schemes" Agenda Item 14 March 2016.

Preliminary position:

The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.

Analysis:

In order to determine the appropriate accounting for EAs it is important to understand what they are and what they are not.

An EA is separately identifiable and is a permit (a non-exclusive, non-expiring right) that allows the holder to settle the legislative compliance obligation that arises from producing one ton of emissions. This is subtly different from a "quotas" (for example a milk or fishing quota) that gives a holder the right to produce a certain level of product that the producer can then sell for economic benefit, because the ultimate benefit of the EA to the participant is the permission to avoid a fine or payment that would otherwise be required for non-compliance with the Act[1].

Is it a financial instrument?

Current PSAS does not define financial instruments. However, PS 3450 (effective in 2019) define financial instruments as "any contracts that give rise to financial assets of one entity and financial liabilities or equity instruments of another entity". An EA is clearly not an equity instrument, and so it will only meet the definition of a financial instrument if it creates a financial liability to one party (and a financial asset to another). A financial liability is defined in PS 3450 as any liabilities that are contractual obligations (a) to deliver cash or another financial asset to another entity; or (b) to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government. A financial instrument by definition a contract. It could be argued that EAs are statutory instruments created by legislation and issued in a unilateral transaction (see "is it similar to a "tax" on emissions?") in which case an EA could never be a financial instrument. For purposes of this analysis an

[1] This is consistent with the conclusions of Mr. Stephen Morris QC in hearing a case regarding the EU ETS system and the nature of European Union Allowances in Armstrong DLW GmbH v Winnington Networks Ltd (2012).

EA is considered to be a contract between the holder and the Province as both parties know their respective rights and obligations that arise from holding and issuing EAs.

An EA does not create an obligation for any party to pay cash or other financial assets. The province has no contractual requirement to pay cash to redeem an EA and is never required to exchange an EA for another financial asset under any circumstances. (The province may accept cash payment in lieu of EAs for an increased compliance obligation at its discretion). Similarly, once they are the holder of an EA they are not obligated to pay cash or other financial assets to another party under the terms of the individual EA. A participant may be obligated to obtain the necessary number of EAs to meet their compliance obligations under the cap and trade program, to reduce their emissions accordingly, or in some cases to pay an increased compliance obligation in cash, these are obligations that arise through the act of emitting pollutants and not an obligation that is incurred through holding an EA. Rather holding an EA permits the participant to avoid an outflow of cash otherwise payable.

Is it similar to a currency?

Governments are unique in that they have the power to issue currency as legal tender. By analogy the EAs could be viewed as similar to a form of "currency" – a medium of exchange - that must be accepted by the government to settle compliance obligations. Compliance obligations only exist through government legislation, and the government also provides the means by which to settle those obligations (EAs). The maintenance of EAs in circulation is required by Cap and Trade regulation. The issuance of EAs at auction could be an issuance of this "currency" for cash. The distribution of EAs could be similarly a distribution of currency for no consideration (similar to a government grant). EAs can be traded like a currency (with a varying exchange rate to Canadian dollars depending on the market price). This is the position taken by certain governments in accounting for their Emissions Trading Systems such as New Zealand (See Appendix A). The arguments that the EAs are a form of "currency" have some merits. However unlike currency, the EAs in circulation are retired after they are submitted for a compliance obligation and not recirculated. In addition the amount of EAs in circulation is planned to decline over time as emissions are reduced. These caps may also be influenced by external parties such as the Federal Government setting emissions reduction targets that must also be complied with. Further, once Ontario is linked to the WCI it is not the only jurisdiction issuing EAs in circulation that can be used to comply with an Ontario emissions obligation. This means that Ontario could accept back "currency" in excess of that which it issued, or equally never receive back "currency" that it has issued. These factors mean that unlike a currency in circulation, Ontario does not control the EA supply that can be used to settle the compliance obligations. However, for completeness Appendix B considers how the circulation in currency model could be applied to the Ontario cap and trade system.

Is it similar to a "tax" on emissions?

While the mechanics of a cap and trade system are different than a carbon tax, the policy objectives are the same - a price is put on pollution with the purpose of reducing pollution. The primary purpose of the cap and trade system is to reduce emissions and any revenues earned from the sale of EAs is incidental and similar to revenues obtained from taxing other undesired behaviours (such as taxes on alcohol or cigarettes).

The cap and trade legislation requires mandatory participants to purchase EAs in order to settle a legislative obligation to the extent that the participant's emissions exceed their allowance of freely distributed EAs. Under this approach any amounts received, regardless of the timing of those receipts, are considered to be a non-reciprocal transaction as the participants did not have to pay these amounts prior to the implementation of the cap and trade legislation, therefore these costs to the participants are created by legislation in respect of their emissions.

It is the act of emitting in excess of "free" EAs that creates an obligation of participants to pay for a certain amount of EAs. While Participants must obtain EAs in order to meet their compliance obligations which are created by legislation and initially EAs are only available from the Province, it is not the act of auctioning the EAs itself that gives rise to a right to the revenues as there is no legislative requirement that forces a participant to purchase an EA prior to them creating emissions that must be settled through EAs. Further, once linked to the WCI there is no legislative requirement that the participant purchase an EA from the Province.

If the scheme is considered to be in substance like a tax, it would be appropriate that the recognition of revenue would be accounted for in accordance with PS 3510. This would result in "revenue received in advance" for EAs that are sold, and something similar to a "tax concession" for participants that receive free EAs. There would be no accounting recognition for EAs. If the scheme was considered to be another form of unilateral transaction created by the constitutional rights of the Province then it is relevant to consider the proposed guidance in the Revenue SOP. Although not authoritive until a standard is approved, the proposals indicate that revenue for unilateral transactions is recognized when the Authority to collect the revenue exists and the event that gives a right to those revenues has occurred. Paragraph .114 of the SOP states "The past event is specific to the nature of the transaction and the legal authority that gives the public sector entity a right to the revenue. The desired effect is that the past event should be readily identifiable and consistent, both over time and amongst those jurisdictions with similar sources of unilateral revenue. In TAX REVENUE, Section PS 3510, the equivalent concept is the taxable event". It is considered that the event that gives rise to a right to the revenue is the participant's emissions and not solely the auction of EAs.

The key determination to support this view is whether the sale of EAs is an exchange transaction or a non-exchange transaction as those terms are defined in PS 3510. It might be argued that the Province has not given up anything by issuing the EAs regardless of whether they sell the EAs in an auction or freely distribute them because the EAs do not cost anything to create and are to be used only to settle obligations created by the cap and trade regulations. Therefore any amounts received are non-reciprocal.

However, the sale at auction seems to meet the definition of an "exchange transaction" because one entity (the auction participant) receives assets (the EAs – which are assets from the perspective of the participant and assets to the Province immediately prior to the auction) and directly gives approximately equal value in the form of cash to another entity (the Province) as the amount of cash paid for an EA equates to the fair value of the EAs. This is supported by the following facts

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- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see also Section 4 (a) below).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- The Province's right to payment from a participant arises from the auction process and not solely from legislation. If no EAs are purchased at auction the Province has no right to payment. The province has an obligation to deliver the EA to a participant's CITSS account as part of the auction process.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

Is it a "good or service" and if so, of what nature?

The analysis in the above section supports the sale of EAs as being an exchange transaction. This is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the Revenue SOP. Because of the exchange nature of the auctions as the EAs can be considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no inflows to the Province or inflows are less than expected.

Prior to pollution pricing mechanisms the ability to emit pollution was a "free good". There was no cost to companies from emitting pollution - rather the costs were born by society as a whole. The cap and trade legislation forces companies to internalize the costs of pollution, thus turning a "free good" into a "good" that has a price. The price of being able to emit pollution is the cost of obtaining an EA i.e. a permit to settle the compliance obligation.

From the perspective of the participant, the EA is a "good or service". Accounting standards do not clearly define the difference between a "good" or a "service". Often it is evident. Goods are usually understood to be tangible items for which physical possession can be transferred. Services are usually understood to be actions that benefit the recipient that are consumed as the service is provided. Other examples of "goods and services" that are less clear are:

- Stand ready obligations, such as standby charges levied to have good or service providers ready to act
- Rights to use tangible or intangible assets, such as leases or licences for intellectual property
- Options to purchase future goods and services (for example, gift cards or future discounts)
- Providing a decision (for example, fees to apply for a driver's licence and its issuance to a qualifying driver)

(see "Revenue" Statement of Principles issued by PSAB, August 2013)

An EA does not fit neatly into any of these categories. It is intangible (it does not have physical form). It is not a right to use an existing asset (tangible or intangible) of the Province as the right relates to an action of the participant (emissions). As the participant can transfer the EA to other participants, it is clear that the issuance of an EA is not provide a benefit to the recipient that is consumed as it is delivered. The EA does not give a participant the right to future goods or services to be provided by the Province, nor does it represent that the province is on "stand-by" to deliver future goods and services as there is no transfer of further goods and services when the EA is remitted in settlement of a compliance obligation.

As an EA is tradeable and can be transferred or sold to other participants it is most similar to a "good", albeit one in intangible form. If a participant receives a good from the Province in a transaction then the Province must be delivering a good. Therefore although the province creates the EA and the use value of the EA is dependent on the Province's own legislation regarding compliance obligations it makes sense to apply symmetry between participants and the Province in respect of the determination of nature of the EAs.

~~3.~~4. *Identification of assets relating to the cap and trade program as sponsoring government*

Summary of relevant guidance – See Appendix ~~A~~C

PS 1000, Financial statement concepts ("PS 1000")

PS 1200, Financial statement presentation ("PS 1200")/PS 1201, Financial statement presentation, effective April 1, 2019 ("PS 1201")

PS 3210, Assets, effective April 1, 2017 ("PS 3210")

PS 3450, Financial instruments, effective April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to assets under Public Sector Accounting Standards.

a) On creation ~~and sales~~ of free and auctioned EAs: EAs that are created by the government, including EAs held in the strategic reserve, are inventories held-for-sale. EAs that have been remitted to the government as payment for increased compliance obligations or because of breaches of holding limits and are available for re-sale at auctions are also inventories held-for-sale.

   Inventories held-for-sale are measured at cost. Newly created EAs do not cost anything to create and are measured at a nominal amount. EAs that are returned to the government and not ~~cancelled~~retired due to increased compliance obligations or breaches of holding limits will be measured at the cost to re-acquire them (also a nominal amount).

~~b) [NTD preliminary conclusions subject to change, based on further understanding of escrow accounts, whether "delivery of EAs" is substantive, importance of certification date vs auction date and subject to discussion with TBS.]~~

   Note that as it is expected that these amounts will be nominal this preliminary position has not material impact on the Public Accounts.

b) Escrow proceeds held for auctions: Escrow proceeds received for bid guarantees are not recorded by the Province prior to the ~~date of the auction~~transfer of funds into the Province's escrow settlement account.

   ~~On the~~After auction ~~date, a receivable~~certification cash from successful bidders is ~~recognized by the Province for the sale of EAs.~~transferred to the Province's escrow settlement account, resulting in recognition of an asset (cash in Escrow). A corresponding amount is recognized ~~in Revenue~~as deferred revenue until the contract is settled by the transfer of EAs to the participants (see ~~Part 5).~~section 6 below). On settlement EAs held in inventory are removed from inventory and included in Cost of Sales, although these are expected to be at nominal amounts and so this entry would not be material.

c) Period between the auction certification date and the delivery date of the EAs: From the date of the contract between the Province and the successful bidder and the settlement of the contract by delivery of EAs there is no derivative instrument required to be recognized.

~~c)~~d) EAs in circulation: EAs in circulation or the right to receive back EAs in circulation as emissions are produced by participants are not recognized as assets, whether sold at auction or issued as free allowances.

~~d)~~e) Failure of participant to pay increased compliance obligation: The right to demand payment in lieu of EAs for an increased compliance obligation is recognized after the time period that a participant has to rectify the shortfall by remitting EAs as expired, e.g. on the deadline specified in a notice issued under Section 14 (8) of the participant's outstanding obligations.

The above can be summarized in the following journal entries:

On creation of EAs or receipt of EAs that can be re-sold:

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Dr Inventory held-for-sale (expected to be nil cost)

Cr Cash (expected to be nil cost)

~~*On auction date:*~~

On distribution of "free" EAs to capped emitters (see section 6 - included here for completeness of entries)

Dr ~~Receivable (from successful participants/Escrowed amounts)~~

~~Cr Revenue~~

~~Dr Cost of sales~~Expense (expected to be nil as at cost of inventory)

Cr Inventory held-for-sale (expected to be nil cost)

~~*On settlement date:*~~

~~Dr Cash~~

~~Cr Receivable (~~*As payment from successful bidders is received and placed into Ontario Settlement account:*

Dr Cash (in Escrow)

Cr Deferred Revenue

On date of receipt of proceeds to GGRA and transfer of EAs to participant CITSS accounts:

Dr Deferred revenue

Cr Revenue

Dr Cash (GGRA account)

Cr Cash (in Escrow)

As emissions are made by participants~~/Escrowed amounts~~

No journal entry required

On receipt of EAs for the current compliance period in respect of compliance obligations or increased compliance obligations:

No journal entry required

On receipt of any EAs of future vintages settled in respect of a 3 for 1 compliance obligation:

Dr Inventory held for sale (expected to be nil cost)

Cr Revenue (expected to be nil cost)

On expiration of deadline for rectifying increased compliance shortfall by remitting EAs:

Dr Receivable

Cr Revenue

Analysis

~~*Analysis*~~

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a) On creation ~~and sales~~ of free and auctioned EAs:

EAs are "goods" created to be sold or distributed to participants~~. These~~ (see analysis in section 3 above). The sales occur on a regular basis and generate revenues in the ordinary course of running the cap and trade program. ~~Therefore despite being intangible in nature,~~ PS 1200.048 notes that inventories for sale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. The EAs ~~also~~therefore meet the definition of inventories held-for-sale ~~and~~as they are held for sale in the ordinary course and the revenues can be used to finance future operations. Despite being intangible in nature these could be given accounting recognition as an asset. Consistent with current policies of the Province, inventories held-for-sale are measured at the lower of cost or recoverable amount.

~~EAs that are returned to the government and not cancelled due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).~~ PSAS does not provide further guidance on what is included in "cost" for inventory. Following the guidance for tangible capital assets that are constructed would result in only direct costs of creation and directly attributable overhead costs being included. The definition of "cost" for inventories in under other frameworks such as IFRS or ASPE includes both direct costs and a systematic allocation of fixed and variable production overheads. As the EAs are intangible in nature it is not expected that any production overheads would be incurred. General overheads (such as general management) are not allocated to inventory. ~~[ASK MOECC CREATION PROCESS – EXPECTATION IS THAT NO FIXED PRODUCTION OVERHEADS EITHER – ALL WOULD BE GENERAL MANAGEMENT I.E. IF NO PRODUCTION OCCURRED WOULD ANY OVERHEAD COSTS BE ELIMINATED.]~~

~~It is noted that upon the adoption of PS 3450 in fiscal 2020, inventories held-for-sale would be in scope of PS 3450 as they are classified as financial assets under PS 1201 (currently PS 1200). PS 3450 requires financial assets other than equity instruments that are quoted in an active market to be measured at amortized cost, net of any allowance for recovery. While EAs may be considered to trade in an active market, if an active market develops, EAs are not equity instruments and therefore will not be required to be measured at fair value.~~

~~Under PS 3450 financial assets can be designated as measured at fair value when they are part of a portfolio of instruments that is managed at fair value or contain an embedded derivative. It is unlikely that the Province would be considered to manage newly created EAs on a fair value basis and there have not been any embedded derivatives identified in the EAs. Therefore EAs held as inventory must be measured at cost.~~ EAs that are returned to the government and not retired due to increased compliance obligations or breaches of holding limits are measured at their cost, which is expected to be a nominal amount as no cash or other financial asset is paid to acquire them, and no liability is derecognized in respect of the receipt of these (see Section 4 on recognition of liabilities).

Alternative positions considered and rejected: EAs are intangible (without a physical substance) in nature and many participant's accounting framework include them as intangible assets. As the EAs are internally generated and intangible there is an alternative view that they should not be recognized on the books of the Province prior to sale, given the lack of a PSAS definition of what is included the reference to "Intangible Assets" in PS 1000.58. This view is an acceptable view under PSAS, but was ultimately rejected as the preliminary position because the intent of creating the EAs is for re-sale and not for use as a capital asset that is used in the provision of services, for administrative purposes, for

production of goods or for the maintenance, repair, development or construction of other assets. The rationale for scoping out "intangible assets" in PS 1000.58 is because there is no recognition and measurement criteria for intangibles. However there is guidance on how to account for inventories held-for-sale, which can be applied. The selected approach of treating EAs as inventory held-for-sale may create an additional accountability of the number of EAs created and ~~lead to~~provide an opportunity for additional disclosures in the financial statements that would enhance transparency. As the cost is always expected to be nil or nominal because of the nature of the EAs, the accounting for EAs on creation is expected to be immaterial to the financial statements.

b) Escrow proceeds held for auctions:

An asset is recognized by the province as cash is transferred to the Province's escrow settlement account. Prior to the auction process, the Province does not control the ~~proceeds~~ cash or LOC/LOGs held in the participant's escrow sub-account and therefore cannot recognize them as assets. The proceeds are held by a third party ~~(DB)~~ in a sub-account that identifies the participant and legal title and control is not with the Province. The Province does not control whether or how much a participant bids~~, or~~ and therefore if their bids are successful ~~and therefore whether~~. Only successful bids give the Province ~~has~~ any rights to the escrow proceeds ~~prior to the auction being held. Rather~~. Instead the participant controls whether the escrow proceeds will be used to purchase EAs or will be returned to the entity. ~~[NTD – Add additional support if bidders can retract bid guarantees prior to auction date.]~~ If no auction occurs for any reason then the Province does not have any right to the escrowed ~~amounts. [NTD – to confirm]~~cash amounts in the sub-account. After consulting with legal counsel from Ministry of Finance and Treasury Board, it has been determined that at the point in time when money is deposited into Ontario's escrow account, that money is "public money" within meaning of the Financial Administration Act (see subsection 1 (3) of that Act) in that it "belongs" to Ontario. Therefore prior to this point, funds (such as those in the participant's sub-accounts) are not considered to belong to Ontario and should not be recognized as an asset. Further if DB fails to make payment to the Province because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for the FSA's error[2]. As the agreements between DB and the Province are still under negotiation, the final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~From the auction date there is a contract between the Province and the purchasers of EAs. While the Province has not yet credited EAs to the recipient's account, the process of crediting EAs is considered not to be substantive as EAs are not in physical form and the Province controls the recording of EAs in the participants' accounts. Rather, the legal and contractual rights of the EAs are obtained by a purchaser on the auction date. In addition, the participant has also substantially performed under the contract as payment has already been made either through a cash bid guarantee or by the submission of an adequate LOC or LOG. The Province would recognize this as a receivable to the extent that the cash has not been received from Deutsche Bank.~~

~~This position is also analogous to "trade date" accounting which is required by PS 3450.A16 for financial assets traded on a recognized exchange in regular way purchases and sales. While the initial auction of EAs is not on a recognized exchange, they are financial assets and they are auctioned into a~~

[2] Legal position outlined in "Report back on WCI Inc Auction process" Submission to Treasury Board/Management Board of Cabinet, August, 2016.

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~~market place on a regular basis and give rise to a fixed price commitment between the participant and the government, therefore an analogy to the trade date requirement may be appropriate.~~

~~*Measurement of receivable:* The receivable would be measured at the auction price, being the amount of consideration expected to be received from the sale. Due to the bid guarantees it would be expected that the full auction price would be received. [IF EXPOSED TO DB CREDIT RISK MAY NEED TO ADD SOMETHING REGARDING BAD DEBT EXPENSE]~~

On the auction date participants place their bids and indicate what amounts they stand ready to transact at. However, until auction certification date the Province has not accepted the bids and therefore there is no contract for the sale and purchase of EAs on the auction date. This occurs only on the certification date because the certification process is considered to be substantive. Certification is considered substantive because the Province reviews the results, analyses the bid data in detail and reviews and accepts the auction report. The jurisdiction could reject the auction report if the auction has not proceeded in accordance with regulatory requirements and internal jurisdiction approvals must be obtained. Auction results are not fully published until certification has been completed and therefore the participants do not know if they are successful until certification. Based on this analysis there are no additional accounting implications of the auction date.

Once certification has occurred there is a contract between a successful bid participant and the Province and the settlement process begins. Once cash has been transferred from participant's sub-account to the Province's escrow account it is an asset of the Province. It is held for the Province's benefit, notwithstanding that it is not transferred to the Province's own GGRA bank account until the validation of the financial reconciliation, which is considered to be only a matter of time. Therefore during the settlement process, as cash payments are received from participants and deposited into the jurisdiction's escrow account or an LOC/LOG is drawn upon and deposited these would be recognized as cash (in escrow) by the Province. As the EAs have not been delivered to the participant the corresponding side of the entry would be to deferred revenue (see Section 6 below). Any cash recognized for successful bid participants would not be considered to be restricted cash as it is not required to be returned to the bidder and is not externally restricted.

Amounts receivable from participants (i.e. those bid guarantees covered by LOC/LOGs) would not be recognized as an asset of the Province prior to settlement of the LOC/LOG and cash being deposited in the Province's escrow settlement account. While there is a contract between the participant and the province neither party has executed on the contract prior to cash being received into Escrow, and therefore it remains an executory contract until one party performs by paying consideration or delivering the goods. As there is no amount receivable (as the Province will never deliver the EAs prior to cash being received) there is no need to consider any provision for impairment of those receivables.

Note that the cash held in escrow will usually be classified as cash because it is expected to meet the definition of cash and cash equivalents in PS Section 1200.97. The time that the cash is expected to be in the Ontario Settlement account is not more than 20 days, therefore the escrow cash is a "short term highly liquid" amount of cash that is subject to an insignificant risk of changes in value. PSAS considers that anything less than three months might be "short term". However, if there were significant concerns about the amount and timing of cash transfers from the settlement account to the GGRA bank account, for example because of concerns about the Escrow Agent's financial stability, the definition of "cash and cash equivalents" might not be met. In this case the amounts would be recorded as a receivable from the Escrow Agent and the need for a valuation allowance would be considered.

By settlement date all the cash proceeds from the auction would be transferred from the participant's sub-accounts and deposited into the Province's Escrow account. On the settlement date, the Escrowed cash is transferred to the Province's GGRA bank account which would result in a reclassification of the

restricted cash to "cash" as the GGRA account is only internally restricted. (See Section 6 for the discussion on the GGRA account restrictions and other revenue implications at settlement date.)

Alternative positions considered and rejected: ~~Three alternative views were considered for asset recognition – 1) at the posting of bid guarantees; 2) on settlement date; and 3) on auction certification date.~~

~~*Posting of bid guarantees:* For this option, escrow amounts meet definition of an asset when the participant posts a bid guarantee in cash. Under this view it is argued that the Province~~It was considered whether an asset should be recognized by the province when cash is received into a participant's escrow "sub-account" - which is a sub-account of the Province's escrow account - and only released upon the completion and settlement of the auction, which is under the control of the Minister through the certification and settlement process. For example, the province requires participants to place bid guarantees and can control whether an auction goes ahead and therefore when the proceeds are released back to unsuccessful bidders~~, therefore effectively controlling the escrowed amounts. The cash held in escrow is therefore held on behalf of the Province (an asset) with a corresponding liability to either return the cash or EAs. This view was rejected as the use of escrow accounts, as opposed to deposits lodged directly with the Province, sets out the relevant terms as to how and when escrow proceeds are released and therefore the Province does not have discretion to direct the funds as they wish. As the Province has not yet delivered any EAs they do not have a right to the amounts in escrow, and nor do they have legal title. Therefore, the Province does not have any substantive mechanisms of control over the escrow accounts.~~. A bidder cannot retract their posted financial assurance until after an auction has gone ahead.

Therefore any escrowed cash amounts could be considered similar to customer deposits received in advance that should be recognized on the Province's balance sheet, offset by a liability to return those deposits, which will be settled either through a refund of the cash in escrow or through the deposit of EAs in the participant's CITSS account. This view was rejected as based on legal assessment the Province does not own or control the participant's cash in Escrow and has no rights to it prior to the auction process.

Trade date accounting: An alternative view is that recognition of the sale of the EAs should be on a "trade-date" accounting basis. See Section 6 on revenue recognition for discussion on accounting for the sale of the EAs on the trade date and why this view was ultimately rejected. The implications for asset recognition under trade date accounting is that, as the sale is recognized on the trade date not the settlement date, a receivable for the entire proceeds of the auctioned EAs would be recognized on the trade date. Receivables recognized would be subject to impairment considerations, although the bid guarantees would mean a valuation allowance would not be required.

Under trade date accounting it would be determined on what the date is there a fixed price commitment which is the date at which a receivable is recognized. If the certification process is considered to be a substantive process that is undertaken by the Province then there would not be a fixed price commitment until the certification date. If the certification process is not considered to be substantive and the Province is committed to the amounts, prices and bid participants that are shown by the auction algorithm and auction report then this would indicate the auction date is the trade date. As trade date accounting has been rejected this issue has not been considered further.

Auction date as contract date: An alternative view to certification date as the contract date between the Province and the participant for the sale of EAs is that there is a contract on the auction date. This view would indicate that the certification process is not substantive and is a matter of course with changes or rejection of the initial auction algorithm results expected to be rare. It might also be argued

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that while the participant does not know whether they have been successful or not, the Province has run the auction algorithm and does know who the successful bidder are and at what price, and therefore from the Province's perspective there is a contract. This view was ultimately rejected on the basis that the auction certification process is considered to be substantive to ensure the successful bids are legitimate and do not exceed holding limits. Note that based on the preliminary revenue conclusions (revenue recognized on delivery of EAs to CITSS accounts) if this view was taken it would not substantially change any of the accounting entries.

c) Recognition of a derivative

When the province adopts PS 3450 it will need to consider whether the arrangement creates a derivative that needs to be recognized for the contract that exists from the certification date to the settlement of the contract by delivery of EAs date. The contract is a fixed price contract as the Province has agreed to sell a specified number of EAs for the specified price to the successful bid participant. While EAs are financial assets for the purposes of PS 1200/PS1201 it could be argued that they are "non-financial items" because they are inventories held for sale (not in scope of PS 3450) and are not contractual rights to receive cash. PS 3450 scopes out contracts to buy non-financial items from being derivatives when they are made in accordance with the entities normal sale or usage requirements and when those contracts cannot be settled net in cash or another financial instrument. Auction contracts to buy and sell EAs cannot be settled net – they can only be settled gross by exchanging cash for the EAs. Therefore no derivative will be recognized in respect of the contract.

Alternative positions considered and rejected: ~~*On settlement date:* It could be considered that the contract is wholly unperformed until the Province has received the cash released from escrow (or other cash payment from participants) as this cash must be received before the EAs are credited to participant accounts. Under this view an asset and revenue is only recorded once cash has been received. This view was rejected as the bid guarantee and escrow process means it is only a matter of time before the funds are received by the Province and therefore this is not substantive enough to preclude asset recognition as the Province controls a right to cash from the date of auction under the cap and trade auction mechanism.~~

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~~*On auction certification date:* It could be considered was that the certification date is the point for asset recognition as prior to this the auction may not have been valid. This was rejected because the certification date is only to confirm compliance and does not change the date that the contractual arrangements between the Province and the participant for the sale of EAs was made. However, if the certification process rejected certain sales or the auction as a whole, this would be an adjusting subsequent event that would be considered in determining whether assets/revenue from the auction process should be recognized.~~

No alternative views considered on the basis that EAs are not financial assets for purposes of PS 3450 as discussed below in "EAs in circulation".

~~e)~~d) EAs in circulation:

Once sold EAs in circulation do not represent assets to the Province. The EAs are economic resources as participants ascribe value to them. It may also be argued that the Province controls EAs as it can

deny or regulate access to EAs by participants through regulation (PS 3210.16). However, the Province will not obtain any economic future benefits from the existence of EAs in circulation. PS 3210.12 distinguishes between the benefit the public receives and the economic benefit that a public sector entity receives through provision of goods or services, increase in cash inflows or reduction in cash outflow; only the latter resulting in future economic benefits that give rise to an asset. While the Province has a right to receive EAs in the future to settle compliance obligations, those EAs are ~~cancelled~~retired after receipt and never result in an inflow of cash (or reduction in cash outflows) for the Province. Under certain circumstances EAs may be received that are not retired, for example those received as part of a 3 for 1 increased compliance obligation. However, when the EAs are issued the Province cannot expect that any participants will be subject to the 3 for 1 increased compliance obligation and in fact the objective of the cap and trade program is to incentivize participants to purchase their required EAs on the market or reduce emissions and so to avoid the burden of the 3 for 1 increased compliance obligation. Therefore the Province has no basis for expecting future benefits in the form of EAs that will not be retired and can be resold. The EAs do not enhance the government's provision of goods or services as the EAs do not, by themselves, reduce emissions. While EAs exist to further a policy objective of the Province, the benefits of the policy (reduced climate change impact and lower pollution) is a benefit to the Province of Ontario as a whole, not specifically to the government of Ontario.

Alternative positions considered and rejected: An alternative view would be recognize EAs in circulation as an asset based on the Province's right to receive the EAs~~. This alternative view would be consistent with a~~ as a participant emits. This is symmetrical with the participant's accounting for an emission obligation as they emit. However, while the Province arguably has a right to receive an EA due to a past event (the emissions) that the Province controls (through the cap and trade legislation) once returned the EAs do not have future service potential or the ability to generate future economic benefits as they are retired immediately.

Any recognition of a right to receive an EA that is created when a participant emits over time must create revenue as the corresponding credit, as there is no liability that is created by the right to receive an EA. This then results in a write-off to expense when the EA is actually received back. This expense would not reflect the economic substance as it implies that the Province is "better off" financially when emissions are produced despite there being no inflow of economic benefits due to emissions, and "worse off" when EAs are remitted for the pollution, despite there bring no outflow of economic resources (expense) for the Province at the point the EAs are returned and written off. For these reasons this view would not result in a fair presentation.

This alternative view is more consistent when there is a corresponding view that the Province has a liability for EAs in circulation (similar to currency in circulation) and therefore the receipt of the EAs does represent a future economic benefit because it results in the extinguishment of a recognized liability by the Province. This view was rejected because liability accounting for EAs in circulation is rejected as noted in Section ~~4~~5 below~~.~~ and Appendix B.

It was also considered whether the right to receive EAs gives future economic benefits because the EAs are recognized as assets by participants under their accounting frameworks (e.g. IFRS) and therefore the Province has a right to recall an asset. However this view was rejected because while EAs are assets for participants as they can be used to reduce a recognized obligation, they are not assets for the Province as they do not give the Province access to future economic benefits through the provision of goods or services, future cash inflows or reduction of future cash outflows for the reasons noted above. ~~Therefore~~ The only exception is when EAs for a future compliance period are received as part of the ~~right to receive an EA is also not an asset. The~~3 for 1 increased compliance obligation as these may be

re-sold in the future. However for these EAs, the Province does not control how many EAs may be received back that can be re-sold ~~(i.e. those remitted~~ or how many of these are for a future compliance period and so the asset criteria of control cannot be met in respect of this right to receive EAs for increased compliance obligations~~) and so any~~. Any recognition of an asset for the right to receive back ~~was recognized for~~ applied to all EAs~~,~~ would result in a write-off to expense when EAs are remitted for a regular compliance obligation and then ~~cancelled~~retired. This expense would not reflect the economic substance as there has been no outflow of economic resources by the Province at the point the EAs are returned and is therefore not ~~appropriate accounting~~a fair presentation.

~~d)~~e) Failure of participant to pay increased compliance obligation:

~~The~~An increase compliance obligation is similar to a fine or penalty in that it increases the incentive for a capped participant to obtain enough EA "permits" during the compliance period or the participant must obtain a greater number of permits at a greater cost. However, while the compliance obligation is increased for the participant, the Province does not recognize a right to receive cash for increased compliance obligations until the expiry of the notice period because prior to this point participants, not the Province, control whether they have sufficient EAs to meet their compliance obligations or increased compliance obligations~~. As participants~~ as they can ~~settle their obligations with~~purchase additional EAs ~~that~~on the market at the market price. EAs do not enhance or create expected economic future benefits for the government~~. It~~ for the reasons noted in part (d) above in that they are resources that are controlled, but do not lead to future economic benefits for the Province. As participants can settle their obligations with EAs (including those from a future compliance period and after Ontario is ~~only when~~linked, those issued by another jurisdiction of the WCI) there is no asset of the Province until a participant has not settled with EAs ~~that~~and under legislation the Province has a right to demand cash as settlement of the compliance obligation~~.~~ (i.e. to levy a cash penalty for non-compliance with the program). The right to demand cash represents a right to future economic benefits (cash flows) and is an asset, regardless of how the Province ultimately agrees to settle the obligation with the participant.

Measurement of the receivable: ~~The~~ There is no specific guidance in PSAS on the recognition of receivables of fines or penalties as they are scoped out of PS 3510, *Tax revenues*. However, it would be consistent with PS 3510 and other standard to recognize the receivable ~~would be recognized~~ at the amount expected to ~~-~~be received at the time of initial recognition. This would take into account the *expected* settlement of the receivable. For example, some or part of the amount might be settled by a reduction in the free allowances that would otherwise be due to a participant in future years. Settlement in this manner does not result in a direct inflow of economic benefits for the Province as the cost of creating free EAs for distribution is nominal (the benefits are indirect in that more EAs would be available for auction sale) and so would reduce the amount expected to be received.

Alternative positions considered and rejected: It was considered whether the ultimate right for the Province to demand cash in settlement of an increased compliance obligation indicated that the EAs in circulation give rise to future economic benefits because the right to receive EAs *might* ultimately end up being settled in cash. However, this view was rejected as it is only when a participant has chosen not settled with EAs that the Province has a right to demand cash as settlement of the compliance obligation. Therefore there can be no further expected future benefits to be obtained for the Province prior to this point.

~~4.~~5. Identification of liabilities relating to the cap and trade program (excluding deferred revenue) as sponsoring government

Relevant guidance – See Appendix C

PS 1000, Financial statement concepts ("PS 1000")

PS 3200, Liabilities ("PS 3200")

PS 3300, Contingent liabilities ("PS 3300")

PS 3310, Loan guarantees ("PS 3310")

PS 3410, Government Transfers ("PS 3410")

PS 3450, Financial instruments, effective from April 1, 2019 ("PS 3450")

Preliminary positions

We considered whether any attributes of the cap and trade program give rise to liabilities under Public Sector Accounting Standards.

a) Financial liabilities: There are no attributes of the cap and trade program that result in financial ~~liability~~liabilities for the Province.

b) Other liabilities: There are no attributes of the cap and trade program that result in another type of liability for the Province.

c) Loan guarantees and contingent liabilities: There is no exposure for the Province in respect of Participant's cash financial assurance held in escrow in the participant's sub-accounts.

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~~*Analysis*Loan guarantees and contingent liabilities: **EITHER** There may be an implicit loan guarantee by the Province in respect of the funds held in escrow for the participants prior to the auction date and up to the date of settlement. Absent any specific information to the contrary regarding DB's solvency it would usually be considered not likely that the Province would have to pay any amounts in respect of the escrow proceeds and no accrual would be made. To the extent that there are escrowed proceeds held over a balance sheet date disclosures of the implicit loan guarantee should be made, if material.~~

~~**OR** There are no contingent liabilities or loan guarantees by the Province in respect of the funds held in escrow for the participants either prior to the auction date or between the auction date and settlement date.~~
~~[NTD – position to be confirmed based on discussion of insolvency risk with DB~~

~~c)~~ Financial liabilities: As noted in the analysis in part 3 above and Appendix B the EAs themselves are not financial instruments and therefore do not create a financial liability, as once~~accounts. I'm not sure there is, but if it is considered to be "public money" prior or post auction then the Province might have a duty to repay it.]~~

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~~*Analysis*~~

a) ~~Financial liabilities: Under the cap and trade legislation the Province will issue a certain number of EAs under the program (the cap) and, as EAs are financial assets, being inventory held-for-sale (see Section 3 (a) above) this is an obligation to deliver financial assets. However the obligation, such that it exists (see also (b) below), is not a contractual obligation with the participants, as it is brought about through the cap and trade legislation and regulations not individual contracts with participants.~~

a) ~~Once~~ the EAs are issued and in circulation there is no contractual obligation of the Province to redeem them ~~in a manner that results in a sacrifice of economic benefits. Under the legislation, the EAs can only be redeemed to settle a participant's compliance obligation under the legislation and cannot be redeemed~~ for cash or any other financial asset, or ~~exchanged~~exchange them for other financial instruments. For example, if EAs are not required to be remitted by a participant for a compliance period it can be rolled forward for use in a future compliance period, rather than being redeemed for cash or another EA.

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After Ontario links with the WCI it was considered if there is an obligation of Ontario to exchange Ontario EAs for those of other jurisdictions, or accept other EAs in lieu of Ontario EAs on terms that might be unfavourable to the Province. No such obligation appears to exist as there is one market for all jurisdictions in the WCI and once issued there is no way to determine whether an EA is an "Ontario" EA or that of another jurisdiction as all EAs are contractually identical. If a market participant has purchased an EA that was issued as an allocation from California or Quebec and redeems it for an Ontario compliance obligation this does not create any obligation for Ontario to "settle" or return that EA to the originating jurisdiction.

It was considered whether there is any contractual obligation to repurchase the issued EAs or return the purchase price of auctioned EAs in contingent circumstances, such as the termination of the cap and trade program or bankruptcy of a participant. Based on the legislation and regulations there are no terms of the EAs that permit the participant to "put back" the EA to the Province, or require the Province to recall EAs for cash. Rather, Section 70 (3) of the Act specifically notes that the Crown is not obligated to make any payments in respect of ~~cancelled~~retired or removed EAs. The current legislation does not foresee any mechanisms to terminate the program and therefore no current contractual obligation to redeem EAs exists under the terms of the EAs. If the program were to be terminated in the future the settlement of outstanding EAs would be the subject of future legislation and therefore no past event has yet occurred that creates an obligation in the event of termination.

Alternative positions considered and rejected: New Zealand has adopted an accounting policy of accounting for EAs in circulation similar to "currency in circulation", also known as the "Emission Notes" approach ~~and recognizes a liability for the obligation to repatriate or redeem the EAs for their emissions value to the participant (Dr Cash (auction EAs) or Dr Expense (free EAs) and Cr Liability for Emissions Notes for market price), along with a right to receive EAs from participants to settle the EA obligation as emissions occur (Dr Receivable, Cr Revenue). This accounting has the benefit of being most symmetrical with the common accounting methods used by participants under other Frameworks such as IFRS.~~. Whether the EAs can be considered similar to "currency in circulation has been considered in Section 3 above". Whether this view would result in a financial liability being recognized by the Province for EAs in circulation is explored further in Appendix B.

~~Our understanding is that New Zealand took this view, in part, because their EAs (NZUs) are interchangeable with "Kyoto AAU's" (International units), which may create an obligation for New Zealand to accept Kyoto AAUs for NZUs under terms that could be unfavourable. However, this view was rejected as based on the cap and trade program applied by Ontario the obligation to repatriate or redeem the Emissions Notes does not result in an outflow or sacrifice of future economic benefits as~~

there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

b) Other liabilities: There is no liability under PS 3200 for the future issuance of EAs that are predominantly sold through the auction process as these are reciprocal transactions at the market price. The requirement to issue EAs at an auction price does not result in an outflow of economic benefits to the Province, because the Province receives fair value at the time of issuance.

In respect of the EAs that are given away as free allowances, there could be considered to be a constructive obligation to deliver transfer "goods" (being the free EAs) in total or to specific participants. Ultimately however, the The delivery of free EAs is a transition mechanism and is at the discretion of the Province, rather than a contractual or constructive obligation non-reciprocal (as opposed to the participants, as the Province retains discretion over the issuances sale of EAs which is a reciprocal transaction). The transfer of free EAs. [To confirm with MOECC – may have to switch to the alternative view if MOECC EAs is not comfortable with the idea technically in scope of PS 3410 because EAs are neither monetary assets (as they are not claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangements – PS 3410 GLOSSARY) nor are they tangible capital assets as they are not tangible in nature. However the principles in PS 3410 can be applied to determine whether there is no an obligation to deliver free EAs. Under PS 3410 a transferring government has a liability (and expense) for a transfer when the transfer is authorized and all eligibility criteria have been met. The ability to receive free EAs is dependent on the participant registering each year to be eligible to receive the EAs. To the extent that that a capped emitter has registered to get free EAs and the number of EAs that it will receive can be determined under the regulations without continuing discretion from the MOECC to adjust the number then there should be a liability and expense amount recognized for the obligation to issue free EAs]. It is noted however, that PS 3410 does not provide guidance on measurement of that liability and expense. As the obligation is to be settled only in the delivery of the free EAs, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material at any time.

After the issue of free EAs or auction of other EAs, there is no legal or constructive or obligation to make payments or otherwise have an outflow of economic benefits in respect of issued EAs. As the cap and trade program is new, there have been no past practices established by which the Province settles outstanding EAs in cash or by transfer of other economic resources. There are no exchange mechanisms to exchange some EAs for others or to settle them in cash outlined in legislation.

Alternative positions considered and rejected:

~~*Alternative positions considered and rejected:* It could be argued that there is a constructive (rather than contractual) obligation to deliver free allowances to certain participants, due to actions and communications of the Province that have raised valid expectations for specific participants that they will receive free allowances in order to meet their compliance obligations. The obligation would be settled when free allowances are issued. However, even if this view is taken, the best estimate of the amount to settle the obligation by the Province is the cost of the EAs, which is a nominal amount. Therefore, the obligation cannot be material.~~

It was considered whether the Act creates a broader obligation of the Province to reduce greenhouse gas emissions in Ontario in a manner that requires the outflow of economic benefits. Aside from the administration of the cap and trade system, the Act does not require specific actions to be taken by the

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Province that would result in an outflow of future economic benefits that the Province does not have the discretion to avoid. The question of whether the responsibility to spend auction proceeds on initiatives that are reasonably likely to reduce or support the reduction of greenhouse gases creates a liability as discussed in Section ~~5~~6 below.

~~c) Loan guarantees and contingent liabilities: [TBD – To be supported by facts, if any, that indicate the Province may be liable for the return of amounts held in escrow if DB goes insolvent and does not return the escrowed amounts to participants. If it is concluded that there is no implicit guarantee or contingent liability because the Province cannot be liable for the return of the escrowed amounts, the facts will support that position.]~~

It was also considered if there is an obligation of the Province to run the Cap and Trade Program pursuant to legislation and if this creates a liability for the costs of running the program. Under the government's own legislation the Province is responsible for managing the ETS, which will require an outflow of resources in the form of administration costs, including the costs of administering EA issuance, emissions monitoring and compliance settlement activities at the end of the compliance period. There is also a past event that gives rise to this obligation being the enactment of the ETS legislation. However, as the cap and trade program is pursuant to the Province's own legislation there is still discretion to avoid the future outflows through the ability to change the legislation. The federal government has recently announced plans that mean provinces must come up with some form of carbon pricing scheme or else a federal carbon price will be imposed. Currently there is no indication that the federal government is requiring that Ontario continue with its cap and trade program as that program could be replaced with other carbon pricing mechanisms or could be removed and Ontario become subject to any future federal scheme. As such there is no third party that means Ontario has little or no realistic alternative but to continue with the Cap and Trade Program. Indeed, the actions of the federal government indicate that Ontario could stop its own program at its discretion and rely on any federal scheme to achieve carbon reductions.

Loan guarantees and contingent liabilities: It was considered whether the Province has an implied loan guarantee or contingent liability in respect of Participant's cash financial assurance, and whether the Province has the obligation to ensure the amounts are returned to participants if the auction does not run or they are not successful, even in cases of insolvency or error on the part of DB. Based on a legal analysis the Province does not appear to have exposure for loan guarantees or contingent liabilities to the extent that participants have submitted cash bid guarantees in participant's Escrow accounts as there is recourse under both the indemnification clause of the DB contract and required insurance (depending on the nature of the error). Further, if the DB fails to make payment to a participating jurisdiction because it has lost or mishandled funds provided by a successful bidder, the respective rights and obligations of the bidder and participating jurisdiction is governed by the agreed to terms and conditions governing the auction. The participating jurisdiction should not be liable for DB's error.

Alternative positions considered and rejected: No alternative views considered, based on the understanding of the specific arrangements regarding the escrow accounts. The final arrangements between DB and the Province of Ontario should be considered to confirm the above analysis.

~~5.~~6. Revenue recognition under the cap and trade program as sponsoring government

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This section is divided into three sub-sections. The first examines whether the transactions being accounted for are exchange (reciprocal) or non-exchange (non-reciprocal) transactions. The second considers what performance obligations exist. The third section looks at the pattern and timing of revenue recognition for the performance obligations identified.

Sale of EAs as exchange or non-exchange transactions

Revenue recognition on sale and distribution of EAs

Relevant guidance - See Appendix AC for details.

PS 3510, Tax revenue (definition of exchange and non-exchange transactions)

PSAS Revenue Statement of Principles (non-authoritative due process document)

Preliminary position – The sale of EAs are exchange transactions.

***Analysis*:**

The auctioning of the EAs is meets the definition of an "exchange transaction" in PS 3510 as participants receive an asset (an EA) and gives approximately equal value in exchange. This is supported by the following facts

- The province has delivered an asset in exchange for cash. The EAs are assets/economic resources prior to the sale as they are held-for-sale inventory assets prior to the auction (see Section 3 (a) above).
- Purchasers of EAs have obtained an asset in exchange for cash. Purchasers can include market participants and unlike mandatory or voluntary participants, market participants are not subject to compliance obligations. They are purchasing the EAs because EAs are a resource that can be sold or traded on the marketplace. Mandatory and Voluntary participant also do not have to keep their EAs but can sell and trade them on the market speculatively. Participants recognize EAs as assets in their financial statements (typically as intangible assets under IFRS).
- The participant purchases EAs by giving up cash that is approximately equal in value to the EA as, by definition, the "fair value" of an EA is what a market participant is prepared to pay in an unforced transaction, and the auction process is a mechanism to assist in identifying the fair value of the EAs.
- Once Ontario has linked with the WCI, then mandatory and voluntary participants who create emissions in Ontario could obtain some or all their EAs from California, Quebec or other market participants. There is no direct link between the amount of Ontario-based emissions and the amount of proceeds obtained by the Province; emissions in Ontario could exceed (or be less than) the number of EAs issued by Ontario. Therefore the characterization as a tax on emissions does not hold as there is no consistent basis on which this "tax" is calculated.
- The program is not created under tax legislation and is not legally a tax.

The analysis above is consistent with the proposed definitions of "exchange transactions" and "unilateral transactions" in the PSAS Revenue Statement of principles, as the EAs are considered to be a good or service that is provided in exchange for consideration, rather than a receipt of payment without a direct transfer of economic resources to the payor. The Province's right to payment from a participant arises from the auction process and not solely from legislation. For example, for any auction there may be no participants or not all EAs may be sold. In these cases, some EAs are not transferred to participants and there are no or reduced inflows to the Province.

***Alternative positions considered and rejected*:** An alternative view is that the cap and trade legislation forces mandatory participants to purchase EAs in order to settle a legislative obligation. Participants *must* obtain EAs in

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~~order to meet their compliance obligations which are created by legislation, and initially EAs are only available from the Province. Therefore, in substance the purchase of EAs equates to a pre-paid "tax" on emissions, and therefore there is a non-reciprocal transaction as participants do not get anything of economic benefit in exchange, but rather have an outflow of cash to the Province that they previously did not have to pay prior to the cap and trade legislation. This view was rejected for the reasons given in support of "exchange transactions" above as the nature of the cap and trade program and the auction mechanisms are designed to create a carbon market, and under this system EAs become a "good" that has economic value. Therefore the characterization of the sale of EAs as non-exchange transaction would not be consistent with the substance of the cap and trade program.~~

~~Revenue recognition for sale of EAs (Exchange transactions)~~

~~*Relevant guidance* - See Appendix A for details.~~

PS 1000, Financial statement concepts ("PS 1000")

PS 1150, Generally accepted accounting principles ("PS 1150")

PS 3410, Government transfers ("PS 3410")

Other GAAP accounting frameworks including IFRS 15, *Revenue from contracts with customers* ("IFRS 15")

PSAB Revenue – Statement of Principles ("Revenue SOP")

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Preliminary position: Revenue is recognized for the sale of EAs on the ~~auction~~ date of delivery of the EAs as ~~there are no further substantive~~this is when the performance ~~obligations~~obligation is settled by the Province. No revenue is recognized on the distribution of free EAs for no consideration.

Analysis:

The following analysis follows from the preliminary position in Section 3 on the nature of EAs – *The sale of EAs are exchange transactions. The distribution of EAs for no consideration is a non-exchange transaction. EAs are intangible permits (rights) that are "goods" that are transferred to participants.* Given the nature of the EAs as intangible goods it is appropriate to consider revenue recognition requirements for exchange transactions. PSAS does not have a specific standard on revenue from exchange transactions. Therefore other sources of GAAP and consideration of the conceptual framework must be applied to develop an accounting policy.

a) What is the performance obligation~~?~~ for the sale of EAs? A performance obligation is defined in IFRS 15~~/ASC 606~~ a promise in a contract with a customer to transfer a distinct good or service (or bundle of distinct goods or services) or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. This is similar to the proposed definition of performance obligation in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP which defines a performance obligation as an "enforceable promise to provide goods or services to a payor as a result of exchange transactions". ~~This~~The following analysis has applied the IFRS concept, as permitted under PS 1150.

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~~a)~~ In both IFRS 15~~/ASC 606~~ and the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP, performance obligations are identified by reference to a contract – which is an agreement that creates enforceable rights and obligations. A contract does not have to be a formal written bilateral agreement, as long as both parties have an understanding of each party's respective enforceable rights and obligations. In this situation the good or service is the EA that is credited to a participant as a result of the ~~standard auction process. The completion of the auction bid process creates the enforceable right of the province to payment and the obligation to credit the EA to the participant, as well as creating the right of the participant to the EA and the obligation to pay the Province. The auction mechanisms are published and standardized such that each participant understands the~~

~~enforceable rights and obligations that are entered into when an auction occurs.~~auction process or strategic reserve sale. As discussed in Section 4 above, the auction certification date is the date that a contract is considered to exist.

Each EA is "distinct" in that the customer (purchaser) can benefit from each EA individually by selling, trading or using those EAs as the customer sees fit, including using those EAs to sell to other participants in the WCI or to settle compliance obligations in other WCI jurisdictions (once linked), and does not need other goods or services to benefit from the EA and the EA is not combined with other goods and services. A purchaser can only purchase an EA if they are a registered participant, however, becoming a registered participant is available to voluntary participants and market participants and therefore is considered to be readily available to all customers. (See IFRS 15.27 in Appendix ~~A~~C for definition of "distinct goods and services")

Based on the above analysis, a contract is created when a participant successfully bids at auction~~,~~ as confirmed in the auction certification process. The Province has ~~only one~~ distinct performance ~~obligation~~obligations to deliver each EA to each successful bidder under ~~this contract, which is the delivery of the EAs~~these contracts.

Alternative positions considered and rejected: It was considered whether the item delivered to participants in the exchange transaction was a program of carbon (greenhouse gas) reduction rather than the delivery of an EA itself. This was rejected because the individual participants may or may not benefit from a reduction in carbon in Ontario and may or may not benefit in proportion to the cost of the EAs. Further, when Ontario links with the WCI, the participants may not even be located in Ontario. While the province may have promised the public of Ontario and other parties that they will reduce carbon emissions in Ontario to meet emissions targets, this should be separately analysed as to whether it has created a constructive obligation for Ontario to take actions and incur costs to meet this promise (See analysis in ~~4~~5 (b) above). This is separate from the obligation in the exchange transaction with participants in respect of the purchase of EAs.

It was also considered whether the performance obligations to participants is both to issue the EA in the auction process, and also a stand-ready promise to redeem the EA in the future to settle a compliance obligation. In other words an EA is an intangible "right" that has been issued that province is obligated to redeem. Under this view, some or all of the proceeds from the auction would not be earned as revenue until the Province redeems the EA. This view was rejected because the obligation to redeem the EA as settlement of a participant's compliance obligation is an obligation that arises when a participant emits pollution and does not arise from the sale of the EAs. For example, Ontario sells 10,000,000 EAs in a compliance period. However total emissions from Ontario participants are only 100,000 tonnes. Ontario does not have an obligation to redeem all of the 10,000,000 EAs that were sold. Rather, Ontario ~~has an obligation to redeem only~~accepts the 100,000 EAs that are submitted by the participants who emitted the 100,000 tonnes of emissions~~.~~ as settlement of their compliance obligations. Therefore ~~this~~Ontario has no obligation to redeem ~~cannot arise~~an EA that arises from the original exchange transaction and ~~is~~ therefore ~~not a~~there is no performance obligation ~~of~~ that ~~transaction~~exists once the EAs have been sold. Similarly, when Ontario has linked to the WCI as Ontario is only obliged to take back EAs in respect of emissions from Ontario participants. There is no obligation to take back EAs sold to participants in other jurisdictions or to market participants, and likewise there is an obligation to redeem EAs submitted by Ontario participants, even when these were purchased from another WCI jurisdiction or another participant.

It was also considered whether the Province has an obligation to continue to provide the cap and trade program and/or a marketplace where participants can buy and sell EAs, on the basis that participants purchasing EAs are doing so on the understanding that they will be able to buy and sell EAs as well as to remit them for compliance obligations (if necessary). For example, if the termination of the cap and trade program would result in an obligation of the Province to return the sale proceeds to the holders of EAs that had been sold at

auction this could indicate that there is an ongoing performance obligation that has not been fulfilled as the amounts must be refunded in the event of termination of the program. Under the Act, the Director establishes one or more accounts for registered participants for the purpose of allowing the participant to purchase, sell, trade and otherwise deal with emission allowances and credits. However, these are established and maintained in accordance with regulation for any registered participants, regardless of whether they purchase EAs in the auction process. Therefore the responsibility of creating and maintaining these accounts is a requirement and responsibility to registered participants under the Act and not a performance obligation to the purchasers or holders of EAs. The Act permits the trading of EAs between registered participants, but it does not create a provincially controlled market place for these trades. Registered participants may have an *expectation* of the Province continuing the cap and trade program and may make decisions based on this expectation, but this expectation exists in all registered participants including those that receive free allowances, rather than being a performance obligation that arises from the exchange transaction that is the sale of EAs. Section 5 (b) above discusses whether there is a general liability of the Province to continue the cap and trade program. Finally, it is noted that there is no legislative provisions for the termination of the program~~,~~ and there are no contractual provisions embedded in the EAs that give the participants the right to receive cash in respect of outstanding EAs upon termination of the program. As such, there is no evidence of a written ~~of~~or implied contractual performance obligation to continue the program that is part of the sale of EA exchange transaction.

b) When is the performance obligation satisfied? There are a number of models used in practice for determining when a performance obligation is satisfied. Under IFRS 15~~/ASC 606~~ the performance obligations are satisfied as control of the good or service passes to the customer, regardless of whether the performance obligation is a good or a service. Under other standards such as ASPE Section 3400, *Revenue* or IAS 18, *Revenue* there are different criteria for "goods" or "services" and generally revenue is recognized as risks and rewards of ownership are transferred (for goods) or services are provided (for services). Both would be acceptable ways to approach the timing of revenue recognition for exchange transactions under current public sector accounting standards. However, the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP proposes a "control" model similar to IFRS 15~~/ASC 606~~, so this approach has been applied in the analysis. Under IFRS 15~~/ASC 606~~ an "over time" approach is permitted only in specific circumstances (see IFRS 15.35 in Appendix A). In the case of the EAs the customer does not simultaneously receive and consume the benefits of the EA, the EAs do not create or enhance an asset that the customer controls and there is no additional asset that does not have an alternative use that is created by the province to fulfil the contract. Therefore the performance obligation will be satisfied at a point in time.

IFRS 15~~/ASC 606~~ provides indicators of when a point-in-time obligation has been satisfied. These are also included in the ~~PSAS~~ Revenue ~~Statement of Principles~~SOP and have been considered in this analysis. See IFRS 15.38 in Appendix ~~A~~C. The indicators have been assessed as follows:

~~Present right to payment – As noted in Section 3 above, there is a present right to payment at the auction date.~~

~~Legal title to the asset – Legal title is transferred when the EAs are credited to the participants account. This occurs after the auction certification and settlement process is completed. [MOECC implementation group to confirm when legal title transfers is this analysis correct?]~~

~~The entity has transferred physical possession of the asset – This indicator is not relevant as EAs do not have physical form.~~

~~The customer has significant risks and rewards of ownership of the asset – The participant has significant risks and rewards of ownership of the asset from the auction date. If the price of EAs increases after the auction date, the customer can benefit from this increase by selling the EA. Similarly if the price decreases after the auction date, the customer bears this decrease in value. The participant can decide what to do with the EA – sell it, keep it or use it to settle a compliance obligation - from the date of the auction. While EAs are credited to a~~

~~participants account only after auction certification and settlement process are completed, these are administrative processes that do not substantively change the risks and rewards of ownership of the EAs.~~

~~The customer has accepted the asset – There are no customer acceptance clauses. While the auction process is subject to certification this is not performed by the participant, but rather by the Province.~~

Indicator	Auction day	Auction Certification date	Financial Settlement date	Receipt of proceeds and delivery of EAs
Present right to payment	Possible – there is a right to payment from successful bidders but it has not been confirmed who these are.	Yes. Under the contract payment must be received prior to delivery of EAs	N/A payment must be received before this date	N/A payment must be received before this date
Legal title to the asset	Legally EAs are not "property" under the legislation and therefore the concept of legal title does not technically apply to EAs.			However, EAs can only be traded or used after they have been credited to the participant's account. This occurs only on this date.
The entity has transferred physical possession of the asset	This indicator is not entirely relevant as EAs do not have physical form.			However the record of a participant's EAs is maintained in the CITSS account and so the right to use an EA is confirmed only upon this date.
The customer has accepted the asset	There are no customer acceptance clauses. This indicates is not relevant.			
The customer has significant risks and rewards of ownership of the asset. Specifically:				
- Using the EA to settle a compliance obligation (permit to settle a compliance obligation)	No. The EAs cannot be transferred from a participant's holding account to its compliance account to settle an obligation until it has been credited to the holding account.			Yes. Once credited to a holding account a participant can use the EA to settle a compliance obligation.
- Benefiting or	Possibly – the price	Yes – From this date	N/A already met	N/A already met

suffering from the fluctuations in the market price of EAs	that the customer pays is set by the auction process. However the customer does not yet know what price that is or how many EAs will be obtained. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.	the participant knows how many EAs they have and for what price. Any changes in EA value after this date will be obtained or absorbed by the customer if they choose to sell.		

Based on the balance of the indicators above it can be concluded that there is most support for recognizing revenue on a "point in time" basis on the ~~auction date.~~date when the EAs are transferred to the participant. As part of this it was considered that the nature of the EAs is ultimately as a permit to settle compliance obligations and therefore this element of risks and rewards was weighted more heavily.

Alternatives considered and rejected: ~~It was considered whether revenue should be recognized at a point in time when the EAs are credited to the participant account (legal title to the asset has transferred). This was rejected as the delay between the auction date and crediting the participant account is to confirm the settlement of the auction payment and that the auction was carried out legally and in accordance with the regulations. IFRS 15.38 (b) notes that "If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset". Therefore, limited weight was placed on the fact that the participant's accounts are not credited until some time after the auction.~~

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Auction date/Certification date/financial settlement date: See table above for analysis.

Trade date accounting: It was also considered whether "trade date accounting", as required by PS 3450 for regular way purchases and sales, could be applied to the purchase and sale of EAs. Trade date accounting is accepted for financial instruments to avoid having to recognize a derivative that be created for the period of time between when the fixed price commitment is entered into and it is settled because of the presence of an underlying variable that is not specific to either party. "Regular way" purchases and sales are those that are settled in the regular settlement cycle required for that particular investment. The time of that settlement varies depending on the type of instrument and jurisdiction. There could be an argument that the period between certification date and financial settlement date is the regular settlement cycle required for EAs, and therefore trade date accounting could be applied, which would result in the recognition of revenue (gains) on the sale of the EA on the trade date and not on the settlement date when the EA is actually transferred. However, this view was rejected for the following reasons:

- EAs are not sold through a "recognized exchange or securities market" but through the Province's auction process. While there is anticipated to be a market that develops for trades of EAs it will not be a "recognized exchange" under the Ontario Securities Act.
- As the sale is not on a "recognized exchange or securities market" there is not a customary period to settlement date (e.g. three days for equities, two days for forex swaps). Rather the period between the certification date and final settlement can vary depending on how long it takes for

participants to provide cash, the LOCs/LOGs to be drawn upon and the final reconciliation to be approved. Further if the "trade date was considered to be the auction date and not the certification date this would extend the period further and make it more variable as the certification period can vary from 3 – 7 days.

- Trade date accounting is an exception to the usual rules of recognition for executory contracts and/or derivatives. As an exception it should not be extended by analogy to other situations such as EAs which are out of scope of PS 3450 as they are classified as inventories held for sale.

c) What are the implications of free allowances? Free allowances are not sold in an exchange transaction but are distributed in a non-exchange transaction, similar to a government transfer. As noted in Section 5 above, the distribution of EAs are technically not in scope of PS 3410, Government Transfers as they are not tangible capital assets or monetary assets. Further PS 3410 does not provide guidance on the measurement of a government transfer. However, the distribution of EAs to participants is similar to a government grant given that EAs are considered "goods" for which control is transferred at a point in time. This indicates that there is an outflow of economic benefits to participants. Typically under PSAS expenses incurred that are a result of derecognition of assets are measured at the difference between the carrying amount of the asset and the consideration received (in this case nil). The carrying amount of the EAs is at cost; expected to be a nominal amount. This is an acceptable policy under PSAS and consistent with PS 1000.60 (See Appendix C).

Alternatives considered and rejected:

An alternative to measuring the free EAs at cost is to measure them at fair value at the date of distribution being the opportunity cost of the economic resources foregone by not selling the EAs at auction. This policy also appears to be supportable by PS 1000.60 which indicates transactions can be measured at the "fair value ascribed to them when they took place". However this alternative is not proposed because the expense from recognizing the EAs at fair value would be necessarily offset by a gain as the carrying amount of the EAs is nominal. This gain (revenue) does not seem to meet the definition of revenues under the Conceptual framework as there is no inflow of economic benefits to the government from issuing free EAs to participants. Therefore this alternative was rejected as it results in a gross up in the statement of operations that is not a fair presentation of the economic activities of the Province in respect of the issuance of free EAs.

Restrictions on Greenhouse Gas Reduction Account

Relevant guidance – See Appendix ~~A~~C for details

PS 3100, Restricted assets and revenues

PSG-4, Funds and reserves

Preliminary position: The requirement to place the auction proceeds into a Greenhouse Gas Reduction Account is an internal restriction and does not lead to a liability on the statement of financial position.

Analysis:

The legislative requirement to establish the GGRA within the Public Accounts and record the proceeds from the distribution of EAs is found only in the Act, which is legislation of the Province and not of another government. There are no other agreements with other governments or other external parties that restrict the use of the proceeds from the distribution of EAs. Therefore, there are considered to be no external restrictions and the requirements of PS 3100.11 to defer revenue until the resources are spent on the purpose or purpose specified do not apply.

Instead, the GGRA is an internally established reserve of the Province. The reserve is supported by assets that have been formally designated by the Province for specific uses and therefore meet the definition of "designated assets" in PS 3100, as this designation could be readily changed by amending the Act. Disclosure of designated assets may occur in the notes to the financial statements, but cannot occur on the statement of financial position. Similarly, PSG-4 permits reserves supported by designated assets to be disclosed in the notes, but not in the statement of financial position.

Alternative positions considered and rejected: It was considered whether there was an implied external restriction on the proceeds from the auction process, as when the participants purchase EAs they know that, by legislation, the funds are to be placed in the GGRA and spent on eligible programs. This view was rejected because the participants are purchasing the EAs in an exchange transaction (See discussion on "Sale of EAs as exchange or non-exchange transactions above). If the Province were to change the legislation regarding the use of the auction proceeds, the participants would still continue to purchase the EAs that they require or choose to purchase to meet their compliance obligations or to trade in the marketplace. As such, there is no evidence that the participants intend for there to be an external restriction on the proceeds.

It was also considered whether Ontario's commitments to other governments and parties, such as commitments to the WCI, create external restrictions on the use of auction proceeds for specific greenhouse gas reduction purposes. No external restrictions have been noted. ~~[NTD – to confirm that all interested parties agree with this statement]~~

~~6.~~7. Financial statement presentation and disclosure considerations

- Financial statement disclosure consideration
- Other disclosures outside of the financial statements

~~7.~~8. Accounting for Emission Allowances held by government organizations

- Organizations that are consolidated into the Province's financial statements (hospitals, colleges etc.)
- GBEs that are accounted for using the modified equity method (IFRS) and prepare stand-alone financial statements under US GAAP

~~8.~~9. Anticipated fiscal impact over planning horizon

- Impact on balanced budget legislation

~~9.~~10. Implementation risks and audit considerations

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Appendix A – Comparison to other select jurisdictions

	Quebec *Applies Canadian Public Sector Accounting Standards*	New Zealand[3] *Applies International Public Sector Accounting Standards*
Similarities and differences to Ontario	Quebec's cap and trade program substantially the same design as Ontario, as it is intended that Ontario will link into the WCI within the first compliance period	Similarities: Entities must provide New Zealand Units (NZUs) (not cash) to the government based on total emissions. NZUs can be traded between entities. Differences: New Zealand (NZ) had an obligation to the United Nations to keep emissions within the prescribed cap. NZUs are interchangeable with International Assigned Amount Units (AAUs) and New Zealand has an obligation to hold a quantity of international units equal to 90% of its AAU allocation. These units can be used to settle the New Zealand Government's Kyoto obligation. There is no hard domestic cap. International units can be used to settle emissions obligations. If the amount of NZUs are not sufficient for New Zealand to meet its international obligations the government must purchase more AAUs. For every NZU the government stands ready to swap it into an AAU (or equivalent international unit)
Asset recognition	None.	a) Creation of NZUs as "currency" results in inventory prior to issuance b) As Participants emit NZ has a "right to receive" the NZUs, created by legislation. The emissions are similar to a "taxable event"

[3] Information regarding the New Zealand ETS taken from the IPSASB paper "Emissions Trading Schemes" Agenda Item 14, March 2016 and "The Emissions Trading Scheme – Summary information for public entities and auditors"

Liability recognition	None. Although linked to the WCI, there is no cash changing hands with California, therefore no obligations/additional transactions that arise from a combined market.	When issued an NZU is an obligation, similar to "currency in circulation" that represents the obligation to redeem the NZU for their emissions value. NZUs are exchangeable for AAUs and an AAU or equivalent unit can be surrendered instead of an NZU, emphasizing that NZUs are a "medium of exchange" for settling the obligations. The liability is measured by reference to the cash received. For an grant of NZUs it would be nil. For NZUs issued for cash it is measured at the cash amount received. At the end of the compliance period the liability is settled by the return of NZUs (or other acceptable units) recorded under the "right to receive NZUs" asset. There are no assets or liabilities at the end of the compliance period.
Accounting for free allowances	Not recognized in the public accounts as revenue/expense.	Revenue is recognized when the "right to receive" NZUs is recognized – i.e. as the emissions are created by participants. Cash received from sale of NZUs is used to measure the liability representing the obligation to redeem NZUs and is not recognized as a revenue directly.
Accounting for sold/auctioned allowances	Revenue recognized immediately on sale/auction. Rationale was that sold rights are in scope of "unilateral rights" in the Revenue Statement of Principles and therefore result in immediate revenue recognition as government has sole authority to grant the right under constitutional powers and the past event (the auction) has occurred. No further obligations of the government. The revenues are non-refundable. Currently unknown whether recognized on auction date/certification date/settlement date/delivery date. Note that based on auction dates for WCI this is unlikely an issue for the Province of Quebec.	

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Appendix B – Currency in circulation model

If the currency in circulation model is applies, as has been applied in New Zealand, the following analysis would be relevant for consideration. It is noted that the results are similar in respect of revenue recognition and liability recognition as for the "exchange transaction model".

The accounting for currency in circulation is not dealt with specifically in PSAS, however central banks typically recognized a liability for currency in circulation when it is issued as the central bank has an obligation to take back or issue notes and coins from banks with an offset to the bank's reserve liability with the central bank – in other words currency in circulation is exchangeable by holders into a different form of financial asset/ financial liability from the perspective of the central bank. In July 2016 IPSASB released a consultation paper on "Public Sector Specific Financial Instruments" that includes a discussion of currency in circulation[4]. This consultation paper lays out the critical questions to the application of this model. It is noted that the consultation paper considers the issuance of currency in circulation for its face value to be an "exchange transaction".

1. Is there a liability created?
2. What are the revenue implications?

Is there a liability created?

The consultation paper analyses the circumstances under which a liability may be created for currency in circulation by reference to the conceptual Framework. The analysis below considered the factors in the Consultation Paper in reference to the PSAS definition of a liability in PS 1000 and Section 3200 (Note that the IPSASB definition of a liability contains similar concepts to the PSAS definition in PS 1000 and PS 3200 although the words used are different).

- A past event has occurred when the EAs are issued, whether distributed for free or sold for cash.
- The issuance of a currency will embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation when there are legally enforceable obligations of the issuing government. For example, laws requiring the government to exchange damaged currency for new currency, hold collateral for the amount in circulation or establish explicit claims against the assets of the government for the currency in circulation. Where these legal obligations exist to redeem currency there is likely to be an outflow of resources required to discharge the obligation.
- If there are not legally enforceable obligations, the issuance of currency may still be a liability if the government has indicated they will accept certain responsibilities, have raised a valid expectation in others

[4] https://www.ifac.org/system/files/publications/files/IPSASB-Consultation-Paper-Public-Sector-Financial-Instruments.pdf

and have little or no alternative to avoid an outflow of economic resources. It may be less clear whether there will be an outflow of economic resources to settle these obligations, but a past practice of settling them (e.g. redeeming for cash) may create a valid expectation that will be settled by an outflow of economic resources.

There are a number of aspects that indicate the Ontario issued EAs do not meet the definition of a liability (and are not similar to the New Zealand Units):

- When they are remitted to the Province they are retired and not re-sold into circulation (with some limited exceptions)
- EAs issued in Ontario do not require the Province to exchange the EA into any other unit that is in turn can be sold by the Province for cash or used to settle a Provincial obligation, and does not require the Province to exchange an EA for cash. Ontario is not obligated to:
    - Hold collateral for amounts of EAs in circulation
    - Exchange EAs for "new" EAs
    - Honour any claims against other assets of the Province through the redemption of EAs
- In the absence of any legal obligation to redeem EAs for cash or another claim on an asset there is also no constructive obligation created by past practice of such claims/redemptions.
- This contrasts with the New Zealand system where New Zealand has an government Kyoto obligation to settle with international units and the government stands ready to exchange New Zealand Units into Assigned Amount Units (AAUs) or equivalent international unit. This may be on terms that are unfavourable or result in the requirement for New Zealand to pay cash to obtain the necessary AAUs for exchange.

Based on an analysis of the cap and trade program applied by Ontario the obligation to repatriate or redeem the EAs does not result in an outflow or sacrifice of future economic benefits as there are no circumstances when the Province must pay cash or other financial assets to settle the obligation to take back EAs for a participant's compliance obligation. Therefore the presentation of an obligation to redeem EAs would not reflect the substance of the arrangements, as the terms of the EAs do not meet the definition of a liability.

What are the revenue implications?

The consultation paper goes on to discuss whether, if no present obligation exists upon the issuance of currency in circulation if and when would revenue be recognized. Similar to IPSASB, under PSAS revenue is an increase in net financial position of the entity. (IPSASB also has the concept of ownership contributions, which are not relevant in this situation). The Consultation paper paragraph 3.43 notes that "when the issuance of currency does not satisfy the definition of a liability in the Conceptual Framework and recognition criteria, it should be recognized as revenue". This indicates that the test for a currency in circulation model is whether any attributes of the issuance of the EAs create a liability, and if not, any proceeds received from their issuance would be immediately credited to revenue as an inflow of economic resources to the government.

Appendix C – Technical guidance

Definition and nature of Assets

The definition of an "Asset" is currently set out in PS 1000.35~~-.37.~~.

1000.35 Assets are economic resources controlled by a government as a result of past transactions or events and from which future economic benefits are expected to be obtained.

PS 3210, *Assets* is effective from April 1, 2017, which expands on this definition. In light of the timing and multi-year nature of the cap and trade program PS 3210 is considered relevant.

PS 3210 defines assets as "economic resources controlled by a public sector entity as a result of past transactions or events and from which future economic benefits are expected to be obtained". Assets have three essential characteristics:

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

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

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

(PS 3210.03-.04 and PS 1000.36)

Assets may be classified as financial assets or non-financial assets. A financial asset is an asset that can be used to discharge existing liabilities or finance future operations and is not for consumption in the normal course of operations (PS 1000.39). Examples of financial assets include cash, receivables and inventories held-for-sale. A non-financial asset is an asset that is acquired, constructed or developed and does not normally provide resources to discharge existing liabilities, but instead is normally employed to deliver government services, consumed in the normal course of operations and is not for sale in the normal course of operations (PS 1000.42). Examples of non-financial assets include tangible capital assets, supplies inventory or prepaid expenses.

Inventories are not ~~defined under PSAS.~~specifically defined under PSAS, although PS 1200.48 provides guidance that Inventories for resale and other assets held for sale are items that are held for sale in the ordinary course of operations and, therefore, are expected to provide resources to discharge existing liabilities or finance future operations. Other frameworks such as IFRS define inventories as assets that are held-for-sale in the ordinary course of business, used in the process or production for sales in the ordinary course of business or are consumed in the production process or rendering of services. This definition is consistent with the PSAS terminology of inventories held-for-sale and inventories held for consumption or use (consumed in the production process or rendering of services).

Intangible assets may meet the definition of an asset under PS 1000 and ~~OS~~PS 3210. However, in the absence of appropriate public sector recognition and measurement criteria for intangible assets, no intangible assets are recognized in government financial statements (PS 1000.58). There is no definition provided for "intangible asset" in PSAS, although PS 4230 (applicable only to NPOs) does define Intangible Properties as "capital assets that lack physical substance". Other frameworks such as IFRS define Intangible Assets more broadly as "an identifiable non-monetary asset without physical substance".

Measurement of Assets

There is no specific guidance in PSAS on the initial recognition amounts for inventories. PS 1000.60 notes that generally financial statements are prepared on the "historical cost basis" being the cash or cash equivalents paid or received or the fair value ascribed to them when [the transactions] took place. Inventories held-for-sale are financial assets. Subsequent to initial recognition inventories are measured at their recoverable amount, net of any valuation allowance (PS 1200.049). ~~After the adoption of PS 3450, which is currently effective for the Province for~~

~~fiscal 2020, financial assets may be designated into the "fair value" category but only if they are managed and evaluated on a fair value basis in accordance with a risk management or investment strategy or they contain embedded derivatives.~~

Definition and nature of liability

The definition of a "Liability" is currently set out in PS 1000.44-.45 and PS 3200, *Liabilities* which expands on this definition.

PS 3200 defines liabilities as "present obligations of a government to others arising from past transactions or events, the settlement of which is expected to result in the future sacrifice of economic benefits". Liabilities have three essential characteristics:

a) They embody a duty or responsibility to others, leaving a government little or no discretion to avoid settlement of the obligation;

b) The duty or responsibility to others entails settlement by future transfer or use of assets, provision of goods or services, or other form of economic settlement at a specified or determinable date, on occurrence of a specified event or on demand;

c) The transactions or events obligating the government have already occurred.

(PS 3200.05)

PS 3200 states that discretion can be removed by an entity's own actions when this creates a constructive obligation to others. For a constructive obligation to exist the government must accept responsibility for the obligation, create a valid expectation among others and have no realistic obligation but to settle the obligation. This can arise from past practice, established policies, cabinet minutes, orders-in-council, ministerial orders, approved plans, ministerial letters and legislation.

PS 3200 states that the obligation to sacrifice economic benefits must be to a third party, and that entity exists at the financial statement date. The timing of the sacrifice of economic benefits must also be specified.

~~PS 3200 does not contain measurement guidance for liabilities. Other standards such as PS 3250, *Retirement benefits* and PS 3260, *Liability for contaminated sites* use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate).~~

PS 3450 includes a definition of financial liabilities as "contractual obligations to deliver cash or another financial asset to another entity; or to exchange financial instruments with another entity under conditions that are potentially unfavourable to a government". While PS 3450, *Financial instruments* is not mandatorily effective for the Province until fiscal 2020, given the long term nature of the cap and trade program, it has been considered in the analysis. Under PS 3450 there is no guidance on initial measurement of financial liabilities – typically transaction price is used, although fair value may be appropriate in some circumstances. Subsequently, financial liabilities are measured at amortized cost, unless they are eligible to be designated at fair value.

PSAS also contains guidance on loan guarantees (PS 3310), which are a form of contingent liability (PS 3300). Loan guarantees, as with other contingent liabilities, are accounted for as a liability when a loss is likely and the amount can be reasonably estimated.

Measurement of Liabilities

There is no general measurement guidance for liabilities in PS 3200, although specific standards specify measurement bases to be used. Other standards such as PS 3250, Retirement benefits and PS 3260, Liability for contaminated sites use a measurement model of the best estimate of the "cost" or cash outflows to settle the liability (discounted where appropriate). It is also noted that PS 1000.60 includes the following guidance:

PS 1000.60 Measurement is the process of determining the amount at which an item is recognized in the financial statements. There are a number of bases on which an amount can be measured. Government financial statements are, however, prepared primarily using the historical cost basis of measurement, whereby transactions and events are recognized in financial statements at the amount of cash or cash equivalents paid or received or the fair value ascribed to them when they took place. Other bases of measurement are also used, but only in limited circumstances.

(a) Replacement cost is the amount that would be needed currently to acquire an equivalent asset. This may be used, for example, when inventories are valued at the lower of historical cost and replacement cost.

(b) Realizable value is the amount that would be received by selling an asset. This may be used, for example, to value portfolio investments. Market value may be used to estimate realizable value when a market for an asset exists.

PS 3410 Government Transfers - Scope

04 Government transfers are transfers of monetary assets or tangible capital assets from a government to an individual, an organization or another government for which the government making the transfer does not:

(a) receive any goods or services directly in return, as would occur in a purchase / sale or other exchange transaction;

(b) expect to be repaid in the future, as would be expected in a loan; or

(c) expect a direct financial return, as would be expected in an investment.

.05 This Section does not deal with:

(a) transfers made through a tax system that are authorized through tax legislation;

(b) grants in lieu of taxes;

(c) settlements of lawsuits or other types of legal compensation provided by governments;

(d) Canada Pension Plan (CPP) and Quebec Pension Plan (QPP) payments; and

(e) transfers of non-monetary assets other than tangible capital assets. Examples of transfers of non-monetary assets that are excluded from the scope of the Section are: transfers of purchased natural resources and rights, transfers of equity investments, transfers of items inherited in right of the Crown or transfers of works of art and historical treasures. 4

(footnote 4 - In accordance with FINANCIAL STATEMENT CONCEPTS, Section PS 1000, all intangibles, and items inherited by right of the Crown, such as Crown lands, forests, water and mineral resources, as well as works of art and historical treasures, are not recognized as assets in government financial statements)

PS 3410 Government Transfers - Expense (and liability) recognition

.12 A government transfer should be recognized by a transferring government as an expense in the period the transfer is authorized and all eligibility criteria have been met by the recipient.

Exchange transactions and non-exchange transactions

PS 3510.07 – (a) *Exchange transactions* are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

(b) *Non-exchange transactions* are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

PSAS Revenue Statement of Principles –

.026 "Exchange transactions are transactions where goods or services are provided for consideration. These transactions create performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor"

.032 "Unilateral revenues increase the economic resources of a public sector entity without a direct transfer of economic resources to the payor. The right to the economic resources is attributable to legislation grounded on a constitutional authority, or delegated constitutional authority, and an event entitling the public sector entity to recognize revenue".

Definition of revenue

PS 1000.46 - "Revenues, including gains, are increases in economic resources, either by way of increases of assets or decreases of liabilities, resulting from the operations, transactions and events of the accounting period." Revenues are distinguished from gains because gains arise from peripheral or incidental transactions and events affecting a government.

Revenue recognition

PS 1000.59 - "Items recognized in government financial statements are accounted for in accordance with the accrual basis of accounting.... Accrual accounting recognizes a liability until the obligation or condition(s) underlying the liability is partly or wholly satisfied."

PS 1150 - When there is no primary source of PSAS that addresses an issue a government uses professional judgement to develop an appropriate accounting policy that is consistent with the primary sources of GAAP and PS 1000. Additional sources can be referred to which include pronouncements of other standard setters (such as IPSASB, GASB, FASAB in the public sector or FASB, IASB or AcSB for private sector equivalents). Exposure drafts and other due process documents may also be considered, although care should be taken when using such documents as they may change before finalization.

The table below various approaches to revenue recognition taken by other standard setters and the pronouncements that could be taken into account in developing an accounting policy.

Source	Standard reference	Revenue recognition model for sale of goods
Public sector standard setters		
IPSASB	IPSAS 9 – Revenue from exchange transactions	As risks and rewards are transferred; no continuing managerial involvement or control; revenue can be reliably measured; probable economic benefit will flow; costs incurred can be measured reliably.
GASB	Principles covered in 1600, Basis of accounting. Some specific issues covered in other standards.	Revenue from exchange transactions generally should be recognized when an exchange, in the ordinary course of operations, is effected unless the circumstances are such that the collection of the exchange price is not reasonably assured.
PSAB	Statement of principles, Revenue (Exposure draft, standard not finalized)	Revenue is recognized as a performance obligation is satisfied. Based on principles of IFRS 15.
Private sector standard setters		
IASB	IAS 18	Same as IPSAS 9
	IFRS 15 (effective 2018)	Recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expected to be entitled in exchange for those goods or services
FASB	ASC 605	As risks and rewards are transferred; no continuing managerial involvement or control; reasonable assurance of the measurement of consideration. Specifically, there must be persuasive evidence of an arrangement, delivery has occurred or services have been rendered and the sellers price is fixed or determinable
	ASC 606 (effective 2018)	Same as IFRS 15
AcSB – Part II (ASPE)	Section 3400, Revenue	Same as ASC 605

IFRS 15.27 - A good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (ie the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (ie the good or service is distinct within the context of the contract).

IFRS 15.35 - An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:

(a) the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (see paragraphs B3–B4);

(b) the entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (see paragraph B5); or

(c) the entity's performance does not create an asset with an alternative use to the entity (see paragraph 36) and the entity has an enforceable right to payment for performance completed to date (see paragraph 37).

IFRS 15. 38 - If a performance obligation is not satisfied over time in accordance with paragraphs 35–37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

(a) The entity has a present right to payment for the asset — if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

(b) The customer has legal title to the asset — legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer's failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.

(c) The entity has transferred physical possession of the asset — the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.

(d) The customer has the significant risks and rewards of ownership of the asset — the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.

(e) The customer has accepted the asset — the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.

Restricted assets and designated assets

PS 3100 applies to funds and reserves that are externally restricted, PSG-4 applies to funds and reserves that are not externally restricted.

PSG-4.3 - .4 - Some funds and reserves are supported by assets. These may meet the definition of designated assets set out in PS 3100.04 (c). PS 3100.30 requires that when a government chooses to provide information about designated assets it does so in the notes and not on the statement of financial position.

PSG- 4.7 - "Therefore, when a government chooses to provide information about any funds or reserve, it does so only in the notes and schedules and not on the statement of financial position. The creation of, addition to or deduction from funds and reserves does not create a revenue or expense, and would therefore not be reported on the statement of operations."

PS 3100.04 (a) - "External restrictions are stipulations imposed by an agreement with an external party, or through legislation of another government that specify the purpose or purposes for which resources are to be used."

PS 3100.11 - "Externally restricted inflows should be recognized as revenue in a government's financial statements in the period in which the resources are used for the purpose or purposes specified. An externally restricted inflow received before this criterion has been met should be reported as a liability until the resources are used for the purpose or purposes specified."

PS 3100.27-.28 - Designated assets – "...Assets may be designated for a specific purpose as a result of government legislation, by-law or resolution that limits the use of assets to specified purposes. Designated assets are distinct from restricted assets. Unlike restricted assets, governments can readily change the legislation, by-law or resolution and use the designated assets for another purpose if the need arises...."

IPSASB discussions

The International Public Sector Accounting Board (IPSASB) debated a paper in March 2016 that outlined a number of different accounting options that could be applied to various emissions trading schemes including conceptual considerations for and against each model. To date the IPSASB has not concluded on an appropriate model for accounting for emissions trading schemes such as Ontario's cap and trade scheme. The various approaches outlined in the paper were considered in developing the preliminary positions of this memorandum. The proposed approach for Ontario is most closely aligned with "Approach 2" of the paper, altered where necessary to account the specifics of the Ontario cap and trade system and the application within the PSAS Framework.

This paper can be found at: http://www.ipsasb.org/system/files/meetings/files/Agenda-item-14.pdf

Formatted: Normal, Space Before: 0 pt, After: 0 pt, Line spacing: single

Meeting with E & Y.pdf

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Fong, Pauline (TBS); Li, Wendy (TBS); Sun, Alicia (TBS); Ma, Patricia (TBS); Shayan Jafrani; "chiristina.chan@ca.ey.com"; christina.chan@ca.ey.com
Cc:	Patel, Bharat (TBS)
Subject:	Meeting with E & Y
Start:	February 7, 2017 10:30:00 AM
End:	February 7, 2017 11:30:00 AM
Location:	APFR Boardroom
Attachments:	Actuarial Support Services Kickoff Meeting r.docx

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Agenda attached

Actuarial Support Services Kickoff Meeting r.pdf

Office of the Provincial Controller
Accounting Policy and Financial Reporting Branch
Actuarial Support Services Kick-Off Meeting
February 7, 2017

Agenda

1. Introductions

2. Scope of pensions reflected in Public Accounts

3. Budget Support

4. Public Accounts

    - Audit considerations
    - Preparer considerations

5. Pension Policy Division (Assumptions/Management's Best Estimates)

6. Contemplated support opportunities:

    - Review pension expense calculation model
    - Review assumptions used in the model
    - Treatment of one-time or unique transactions
    - Provide assistance in variance analysis
    - Calculation of valuation allowance (asset ceiling test?)
    - Specific issues related to individual plan (e.g. Share the Pain for OTPP)
    - Review OPEB Calculations

7. Other

Meeting with PwC.rtf

From: Virani, Shyrose (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; 'david.c.greenall@ca.pwc.com' [david.c.greenall@ca.pwc.com]; michael.hawtin@ca.pwc.com [michael.hawtin@ca.pwc.com]; Provis, Ian (TBS) [Ian.Provis@ontario.ca]; Keates, James (TBS) [James.Keates@ontario.ca]; Saboor, Ibrahim (TBS) [Ibrahim.Saboor@ontario.ca]
Subject: Meeting with PwC
Date: Friday, November 04, 2016 14:46:19

Meeting with PwC.pdf

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Veinot, Cindy (TBS); lucy.durocher@ca.pwc.com; "david.c.greenall@ca.pwc.com"; michael.hawtin@ca.pwc.com; Provis, Ian (TBS); Keates, James (TBS); Saboor, Ibrahim (TBS)
Cc:	"michael.hawtin@pwc.com"; "david.c.greenall@pwc.com"; "lucy.durocher@pwc.com"; Li, Wendy (TBS)
Subject:	Meeting with PwC
Start:	November 15, 2016 10:00:00 AM
End:	November 15, 2016 11:00:00 AM
Location:	7 Queen"s Park Crescent, 2nd Floor, APFR Boardroom

hi.rtf

From: Virani, Shyrose (TBS) []
To: shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]
CC: uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]
Subject: hi
Date: Monday, February 06, 2017 11:03:42
Attachment 1: confidentiality agreement.doc
Attachment 2: tax declaration form.docx

Hi Shayan:

I work for Nadine Petsche and she advised me that you and other folks will be coming to our office tomorrow for the meeting. Since I have to register you all, can you please provide me with the names of all staff attending tomorrow's meeting so that I could register you at the security desk. We are located at 7 Queen's Park Crescent, 2nd Floor, Frost South, upon arrival, please call Shyrose at 416 325 1448 from the lobby phone to gain the entry into our office building.

Thanks

Shyrose

p.s. at the same time time, I need the names and email address of the staff who will be working on the actuarial file so that I could get the clearances for all of you. Attached, please find:

1. Confidentiality Agreement form, please have everyone involved in this file complete the form and return it to me at your earliest.

2. Tax Declaration form – to be completed and return to me.

Thanks

Shyrose Virani

confidentiality agreement.pdf

CONFIDENTIALITY AGREEMENT

Confidentiality Agreement

During and following the term of the Agreement between **Ernst & Young LLP** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and Listed Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the *Freedom of Information and Protection of Privacy Act* ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: _____ Signature: _____

Date: _____

Witness: _____ Signature: _____

Date: _____

tax declaration form.pdf

Appendix D – Tax Compliance Declaration Form

The Ontario Government expects all suppliers to meet their Ontario tax obligations on a timely basis. In this regard, proponents are advised that their Ontario tax obligations, if any, must be in good standing in order to be considered for a contract award (see Section 3.2.3 of the RFP). In order to be considered for a contract award, the proponent must submit the following tax compliance status statement and the following consent to disclosure:

Declaration

I/WE hereby certify that **Ernst & Young LLP** (the "Proponent") at the time of submitting its proposal, is in full compliance with all applicable Ontario tax statutes, whether administered by the Treasury Board Secretariat or by the Canada Revenue Agency, and that, in particular, all returns required to be filed have been filed and all taxes due and payable under those statutes have been paid or satisfactory arrangements for their payment have been made and maintained; or the Proponent will take all necessary steps prior to being considered for contract award in order to be in full compliance with all applicable Ontario tax statutes.

(Please check applicable box)

The Proponent ❑ is / ❑ is not a corporation subject to Ontario corporate tax under the *Taxation Act, 2007* (Ontario).

(Please insert Proponent's Business Number) _____

Consent to Disclosure

The Proponent consents to the Ministry of Finance releasing the taxpayer information to the Ministry of Finance as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

The Proponent consents to the Ministry of Finance releasing taxpayer information to the Requesting Ministry as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

Dated at _____ this _____ day of _____ 20 _____

_____

(Authorized signing officer)

_____

(Print Name) **(Title)**

I have authority to bind the Proponent.

hi.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: hi
Date: Thursday, September 01, 2016 14:13:08

When do you want me to schedule next teleconference?

hi.rtf

From: Virani, Shyrose (TBS) []
To: gregory.winston@ca.ey.com [gregory.winston@ca.ey.com]
Subject: hi
Date: Tuesday, September 05, 2017 12:44:07

Did you get chance to complete your security clearance for Triton?

Thanks

Shyrose

hi.rtf

From: Virani, Shyrose (TBS) []
To: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]; christina.chan@ca.ey.com [christina.chan@ca.ey.com]
Subject: hi
Date: Thursday, March 30, 2017 09:24:04

Are you folks planning to come to our location today?

if it helps.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: if it helps
Date: Saturday, September 17, 2016 07:39:42

Good morning Lucy.

Just in case it helps, the OTPP accounts for the bulk of our reported pension assets, so a focus on that plan for purposes of the analysis would be appropriate

N

invoces.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: invoces
Date: Thursday, March 02, 2017 12:33:14

Hi Lucy

Our year end is March 31st and I was wondering if I could expect to receive any invoices for:

1. Cap and Trade
2. Pension.

Your early response will be appreciated.

Thanks

Shyrose

letter and agreement.rtf

From: Virani, Shyrose (TBS) []
To: anna.pesme@ca.ey.com [anna.pesme@ca.ey.com]
CC: Uros Karadzic [uros.karadzic@ca.ey.com]
Subject: letter and agreement
Date: Friday, December 01, 2017 14:53:17
Attachment 1: 20171201133902317.pdf
Attachment 2: confidentiality agreement.doc
Attachment 3: tax declaration form.docx

Hi Anna:

Attached, please find:

1. Covering letter
2. Agreements (2 copies)
3. Tax Declaration Form
4. Confidentiality Agreement

Kindly have Uros sign the agreement and e-mail it back to me at your earliest. Original agreements are in the mail, once you receive it, please have Uros sign the original and send it to me via mail. Also, please have Uros sign the Tax Declaration form and Confidentiality Agreement, Christina has to sign Confidentiality Agreement as well.

Thanks
Shyrose Virani

20171201133902317.pdf

Treasury Board Secretariat

Office of the Treasury Board
Office of the Provincial Controller Division
Accounting Policy & Financial Reporting Branch
Frost Building South, 2nd Floor
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel. (416) 325-8027

Secrétariat du Conseil du Trésor

Bureau du Conseil du Trésor
Bureau du contrôleur provincial
Direction de la méthode comptable et des rapports financiers
Édifice Frost Sud, 2e étage
7 Queen's Park Cr.
Toronto ON M7A 1Y7
Téléphone: 416-325-8027

Ontario

December 1, 2017

Ms. Anna Pesme
Ernst & Young LLP
222 Bay Street
Toronto ON
M5K 1J7

Ms. Pesme

RE: RFS-TBS-OTB-OPCD-22

The Ministry is pleased to advise that you are the selected proponent pursuant to the above-noted procurement process.

Enclosed please find two (2) copies of the Agreement for your signature. Please return one copy of the executed Agreement within five (5) business days of receipt of this notice:

Please be advised that this notice of selection letter should not be construed as permission from the Ministry to begin the work detailed in the Agreement. The Ministry will not be responsible or liable for any expenses related to the Deliverables, and the selected proponent is not to accept work requests prior to the execution of the Agreement by the Ministry. Work may begin pursuant to the Agreement when:

(a) the Agreement signed by both parties is returned to the selected proponent, and

(b) written permission is expressly given to the Supplier by the Ministry Representative to begin work under the Agreement.

.../2

If you have any questions concerning this process, please feel free to contact me at 416-325-8027.

Sincerely,

Mark Donaldson
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller Division

FORM OF STATEMENT OF WORK – OPS ENTITY

Statement of Work for Management Consulting Services

This statement of Work No. **RFS-TBS-OTB-OPCD-22** made in **duplicate and effective December 11, 2017 ending on June 15, 2019.**

Ernst & Young LLP (the "vendor" or "EY") and her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of June 16, 2014 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* – The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term of provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* – The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price* - C$75,000.00 does not include HST.

4. *Project Start Date* – December 11, 2017

5. *Project End Date* – June 15, 2019

6. *Scope of Services and Deliverables* – The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

    - Working with management of the Office of the Provincial Controller's Accounting Policy and Financial Reporting Branch (APFRB), the provider will provide actuarial/accounting services related to the following possible areas:
        - Review the economic assumptions (i.e. management best estimates) used for the accounting valuations of the pension plans and non-pension benefits reported by the Province.
        - Review the actual and forecast numbers prepared by APFR staffs for the Province's various pension and non-pension benefits, including assessing the reasonableness

and completeness of assumptions used by APFRB staff in the models, including any sensitivity analysis as required.
    - From time to time provide recommendations, if any on improvements in the pension and non-pension benefits accounting models.
    - Perform ceiling test requirements in accordance with PS3250.50 to PS3250.59 for all sole sponsor or joint sponsor pension plans that are in an accrued benefit asset position.
    - Provide advice on any accounting issues related to pension and non-pension benefits, as required.
    - Participate in discussions with internal and external stakeholders, as required.

- The Vendor will participate in meetings as necessary to support the engagement objectives.

7. *Ownership and Licenses* – Attachment D of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* – The structure of Ernst & Young's working relationship with OPCD is vital to the success of their engagement. The Project Lead that will handle OPCD work is Uros Karadzic. Ernst & Yong's communication strategy will be centered on periodic project update meetings, the frequency of which will be determined by the OPCD and Ernst & Young.

9. *Work Location* – All meetings will be within Greater Toronto.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:30 a.m. to 4:30 p.m. Monday to Friday inclusive.

    If required by the Client, the Vendor must provide Services outside of the normal working hours and/or non-Business days. The Vendor will not be entitled to charge more than the Fixed Price or Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Billing and Payment Process* – The Vendor shall provide the Client with quarterly billing statements that outline the per diem charges no later than 10 Business Days after the end of each quarter.

    Billing statements should include all billing information as set out in the Master Agreement.

13. Names of Roles of Vendor's Personnel:

Name of Individual	**Level**
Uros Karadzic	Senior Consultant/Project Lead
Christina Chan	Intermediate Consultant/Project Analyst

14. *Invoices* – Invoices for payment of any charges under this Statement of Work shall be sent to:

    Client: Treasury Board Secretariat
    Office of the Provincial Controller
    Accounting Policy and Financial Reporting Branch
    Mark Donaldson
    Director, Accounting and Policy Reporting
    Tel: 416 325 8027
    E mail: mark.donaldson@ontario.ca

15. *Knowledge Transfer* – The Vendor will work closely with the Client to ensure knowledge transfer to the Client's designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* – The Vendor shall destroy all information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Indemnity* – the indemnity set out in the Master Agreement applies to this assignment.

18. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	Treasury Board Secretariat
Client Representative:	Mark Donaldson
Telephone Number:	416 325 8027
E-mail:	mark.donaldson@ontario.ca

19. *Vendor Representative and Receipt of Notices*

    Uros Karadzic, Partner
    Ernst & Young LLP
    Ernst & Young Tower
    P O Box 251
    222 Bay Street
    Toronto ON M5K 1J7

    IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

Her Majesty the Queen in right of Ontario as
represented by the President of the Treasury Board

Per:

Signature:

Name: Mark Donaldson

Title: Director, Accounting Policy and
Financial Reporting

Pursuant to delegated authority

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor

confidentiality agreement.pdf

CONFIDENTIALITY AGREEMENT

Confidentiality Agreement

During and following the term of the Agreement between **Ernst & Young LLP** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and Listed Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the *Freedom of Information and Protection of Privacy Act* ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: _____ Signature: _____

Date: _____

Witness: _____ Signature: _____

Date: _____

tax declaration form.pdf

Appendix D – Tax Compliance Declaration Form

The Ontario Government expects all suppliers to meet their Ontario tax obligations on a timely basis. In this regard, proponents are advised that their Ontario tax obligations, if any, must be in good standing in order to be considered for a contract award (see Section 3.2.3 of the RFP). In order to be considered for a contract award, the proponent must submit the following tax compliance status statement and the following consent to disclosure:

Declaration

I/WE hereby certify that **Ernst & Young LLP** (the "Proponent") at the time of submitting its proposal, is in full compliance with all applicable Ontario tax statutes, whether administered by the Treasury Board Secretariat or by the Canada Revenue Agency, and that, in particular, all returns required to be filed have been filed and all taxes due and payable under those statutes have been paid or satisfactory arrangements for their payment have been made and maintained; or the Proponent will take all necessary steps prior to being considered for contract award in order to be in full compliance with all applicable Ontario tax statutes.

(Please check applicable box)

The Proponent ❑ is / ❑ is not a corporation subject to Ontario corporate tax under the *Taxation Act, 2007* (Ontario).

(Please insert Proponent's Business Number) _____

Consent to Disclosure

The Proponent consents to the Ministry of Finance releasing the taxpayer information to the Ministry of Finance as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

The Proponent consents to the Ministry of Finance releasing taxpayer information to the Requesting Ministry as necessary for the purpose of verifying the Proponent's compliance with Ontario tax statutes.

Dated at _____ this _____ day of _____ 20 _____

_____

(Authorized signing officer)

_____

(Print Name) **(Title)**

I have authority to bind the Proponent.

letter attached.rtf

From: Virani, Shyrose (TBS) []
To: 'Uros Karadzic' [uros.karadzic@ca.ey.com]
CC: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: letter attached
Date: Thursday, July 13, 2017 13:46:27
Attachment 1: 20170713134338996.pdf

Hi Uros

Attached, please find a letter and if you are in agreement, please sign and return it back to me.

Thanks
Shyrose Virani

20170713134338996.pdf

Treasury Board Secretariat

Office of the Treasury Board
Office of the Provincial Controller Division
Accounting Policy & Financial Reporting Branch
Frost Building South, 2nd Floor
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel. (416) 325-8027

Secrétariat du Conseil du Trésor

Bureau du Conseil du Trésor
Bureau du contrôleur provincial
Direction de la méthode comptable et des rapports financiers
Édifice Frost Sud, 2e étage
7 Queen's Park Cr.
Toronto ON M7A 1Y7
Téléphone: 416-325-8027

Ontario

July 12, 2017

Ernst & Young LLP
222 Bay Street P O Box 251
Ernst & Young Tower
Toronto ON M5K 1J7

Attention: Mr. Uros Karadzic

RE: Proposed change to Statement of Work No. TBS-OTB-OPCD-20 dated February 3, 2017, as amended, ("the Statement of Work") made between Her Majesty the Queen in right of Ontario as represented by the President of Treasury Board and Ernst & Young LLP.

The purpose of this letter is to document our agreement to increase the Ceiling Price under the Statement of Work by $149,000.00 for the additional support to a new Maximum Price of $299,000.00.

This letter is sent to you in duplicate. Please indicate your receipt of this letter and your agreement to the change in Ceiling Price by signing where indicated on both copies, and returning the duplicate copy within five days of receipt of this letter.

This letter, when signed by both parties, will constitute a Change Order to the Statement of Work. The parties confirm that, except for the change referred to above, the Statement of Work will remain unchanged and unmodified.

.../2

Thank you for your continued cooperation and support.

Sincerely,

N. Petsche

Nadine Petsche
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller Division

The undersigned hereby acknowledges receipt of this letter and agrees to the above on behalf of Ernst & Young LLP as of the date indicated above.

Ernst & Young LLP

Date:

Per: _____
Name:
Title:
Ernst & Young

I have authority to bind Ernst & Young LLP

Treasury Board Secretariat

Office of the Treasury Board
Office of the Provincial Controller Division
Accounting Policy & Financial Reporting Branch
Frost Building South, 2nd Floor
7 Queen's Park Crescent
Toronto ON M7A 1Y7
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.../2

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Nadine Petsche
Director, Accounting Policy and Financial Reporting Branch
Office of the Provincial Controller Division

The undersigned hereby acknowledges receipt of this letter and agrees to the above on behalf of Ernst & Young LLP as of the date indicated above.

Ernst & Young LLP

Date:

Per: _____
Name:
Title:
Ernst & Young

I have authority to bind Ernst & Young LLP

Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Nadine Petsche
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100100764
Please include this number with payment

Invoice Date:	03 August 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

For professional services rendered: 20 July 2017 to 02 August 2017
- Advice and discussion related to accounting for various benefit provisions
- Updates to financial reporting and projection models for OTPP, OPSEU, PSPP, HOOPP and CAATT pension plans

		Net	Tax	Rate	Tax Amount	CAD Total
Fee		55,000.00	HST	13 %	7,150.00	62,150.00
		55,000.00			**7,150.00**	**62,150.00**
Invoice summary		**55,000.00**				
Tax :	13% HST				7,150.00	
Total:		**55,000.00**			**7,150.00**	**62,150.00**

A member of Ernst & Young Global

Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

Electronic payment instructions:
Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

Wire transfer instructions: Transit #2411 Account #24111000237. Reference the name and address of remitter, invoice number and engagement number.

Electronic fund transfer instructions: Bank ID: 0001 Transit# 24112 Account# 1000237. To ensure accurate allocation of funds sent electronically, please email your remittance detail to gss.canadaaccountsreceivable@xe02.ey.com including the amount paid, the invoice number and your company name.

Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Nadine Petsche
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100100765
Please include this number with payment

Invoice Date:	03 August 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

For professional services rendered: 01 July 2017 to 19 July 2017
- Updates to financial reporting and projection models for OTPP, OPSEU, PSPP HOOPP and CAATT pension plans
- Updates to letters documenting calculation of future economic benefit and accrued benefit asset

		Net	Tax	Rate	Tax Amount	CAD Total
Fee		40,000.00	HST	13 %	5,200.00	45,200.00
		40,000.00			**5,200.00**	**45,200.00**
Invoice summary		**40,000.00**				
Tax :	13% HST				5,200.00	
Total:		**40,000.00**			**5,200.00**	**45,200.00**

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Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Nadine Petsche
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100100766
Please include this number with payment

Invoice Date:	03 August 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

For professional services rendered: 01 June 2017 to 30 June 2017
- Preparation of letter to Cindy Veinot providing additional information on asset ceiling calculation
- Advice and discussion relating to year-end balance sheet adjustments

		Net	Tax	Rate	Tax Amount	CAD Total
Fee		10,000.00	HST	13 %	1,300.00	11,300.00
		10,000.00			**1,300.00**	**11,300.00**
Invoice summary		**10,000.00**				
Tax :	13% HST				1,300.00	
Total:		**10,000.00**			**1,300.00**	**11,300.00**

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Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

Electronic payment instructions:
Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

Wire transfer instructions: Transit #2411 Account #24111000237. Reference the name and address of remitter, invoice number and engagement number.

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Ernst & Young LLP
Toronto, ON

Invoice

Treasury Board Secretariat
Mark Donaldson
Office of the Provincial Controller Div.
Office of the Treasury Board
Frost Bldg S, 7 Queen's Park Cres E
Toronto, ON M7A 1Y7
Canada

Invoice No.: CA01C100109767
Please include this number with payment

Invoice Date:	19 October 2017
Due Date:	Upon receipt
Client No.:	0011426981
Engagement No.:	E-65089409

Remit To:
P.O. Box 57104, Postal Station A
Toronto, Ontario M5W 5M5
A/R Queries:
1-416-943-3851
1-800-311-1104

Final billing for professional services rendered: 03 August 2017 to 30 September 2017

- Completion of the final reviewed versions of the projection models for OTPP, OPSEU, PSPP, HOOPP and CAATT pension plans
- Preparation and delivery of training material (Pension 101, PS 3250, Use of Models) to Ontario TBS employees on September 12, 14 and 15.
- Summary description document of the work performed by EY related to the projection models

		Net	Tax	Rate	Tax Amount	CAD Total
Fee		22,970.00	HST	13 %	2,986.10	25,956.10
		22,970.00			**2,986.10**	**25,956.10**
Invoice summary		**22,970.00**				
Tax :	13% HST				2,986.10	
Total:		**22,970.00**			**2,986.10**	**25,956.10**

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Terms: Payment due upon receipt. Interest is charged at the rate of 12 % per annum on balances unpaid after 30 days from date of invoice. Any disbursements not charged to your account on the date of this invoice will be billed later.
GST/HST: R130866262 **QST:** 1006241791

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Toronto, ON

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Send direct and pay to: Bank of Montreal, International Banking, H.O. Montreal, SWIFT BIC Address BOFMCAM2, Ernst & Young LLP, 6 King Street West, Toronto, Ontario, Canada, M5H 1C3.

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Monday.rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]; Christina Chan [Christina.Chan@ca.ey.com]
Subject: Monday
Date: Thursday, March 30, 2017 10:56:05
Attachment 1: image001.gif

Hi Nadine,

Following up on our earlier discussion, would it be convenient/useful if I were to come up with Shayan and Christina to your office on Monday? Please let me know what works for you/Cindy.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP

Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7, Canada

Office: +1 416 943 2087 | Fax: +1 416 943 2201 | uros.karadzic@ca.ey.com

Mobile: +1 416 970 2087 | EY/Comm: 1685272

Website: http://www.ey.com/ca

Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

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Any tax advice in this e-mail should be considered in the context of the tax services we are providing to you. Preliminary tax advice should not be relied upon and may be insufficient for US penalty protection. Tout conseil de fiscalité contenu dans le présent courriel doit être pris dans le contexte des services de fiscalité que nous vous offrons. Aucune décision ou position ne doit être prise à la lumière de conseils de fiscalité préliminaires, lesquels pourraient ne pas permettre d'éviter des pénalités aux États-Unis.

image001.pdf

New Model Output.rtf

From: Petsche, Nadine (TBS) []
To: Raymond, Martin (CA - Montreal) (maraymond@deloitte.ca) [maraymond@deloitte.ca]
CC: allan.shapira@aonhewitt.com [allan.shapira@aonhewitt.com]; Killoch, Alex (MOF) [Alex.Killoch@ontario.ca]; Pomykacz, Rob (MOF) [Robert.Pomykacz@ontario.ca]; Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
Subject: New Model Output
Date: Friday, September 23, 2016 15:09:49

Martin,

We are on a call with Matt and he is describing your most recent model run for the OTPP. Can you please share that with Allan Shapira and cc. Alex Killoch and Rob Pomykacz as soon as possible.

Thanks.

Nadine

OPSEU - Accounting for Plan surpluses_V4 (PPU_REDLINE).doc.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]; Colavecchia, Pina (CA - Toronto) (pcolavecchia@deloitte.ca) [pcolavecchia@deloitte.ca]
Subject: OPSEU - Accounting for Plan surpluses_V4 (PPU_REDLINE).doc
Date: Tuesday, November 29, 2016 16:03:18
Attachment 1: OPSEU - Accounting for Plan surpluses_V4 (PPU_REDLINE).doc

---

Matt/Pina,

Please find attached comments and edits from our internal SMEs. Please let me know if you have any questions regarding their feedback.

We look forward to receiving a revised draft.

Thanks. Nadine

OPSEU - Accounting for Plan surpluses_V4 (PPU_REDLINE).pdf

1.0 Preamble

This document addresses the accounting for a net pension asset under Public Sector Accounting Standards (PSAS) by the Province of Ontario in relation to the Ontario Public Sector Employee Union Pension Plan (OPSEUPP).

As at March 31, 2016, OPSEUPP had an accrued asset position for accounting purposes of $520.

The details of the accounting valuation for the plan as of March 31, 2016 are as follows:

(all figures in $M)	**Total plan**	**50% Share of the plan**
Market related value of assets	17,380	8,690
Value of obligation	15,557	7,778
Surplus (deficit)	1,823	912
Unamortized (gains) losses	(96)	(48)
Adjustment for March 31, 2016	(583)	(292)
Asset (liability) position	1,144	572
Specific Government adjustment		(52)
Final Asset (liability) position on balance sheet		520

2.0 Issue to be considered

1. For accounting purposes, how should OPSEUPP be classified under PSAS?
2. As a result of the classification, how should the Province of Ontario recognize the pension surplus (for accounting purposes) of OPSEUPP in the Public Accounts?
3. How should a pension asset of OPSEUPP be measured in the Public Accounts of the Province of Ontario?

3.0 Conclusions

1. OPSEUPP is a Joint Defined Benefit Plan under PS 3250
2. The Province of Ontario should account for the OPSEUPP as a defined benefit plan for its proportionate share of the surplus or obligation that arises under the plan.
3. The Province of Ontario should record ~~is~~ its proportionate share of the asset and apply the asset ceiling test under PS 3250. The Province believes that the asset is recoverable through the reduction of future contributions and as such, no valuation allowance is necessary.

Commented [MPM1]: Province versus Government. Should one term be used for consistency (excluding the times Province of Ontario is used)?

4.0 Background information

4.1 Overview of OPSEUPP

The OPSEU Ppension Pplan (the "Plan") is jointly sponsored by the Ontario government and the executive of OPSEU. The Plan is managed by ~~OP Trust~~OPTrust, a 10-member Board of Trustees, five of whom are appointed by OPSEU and five by the Government. ~~OPSEU represents the various public servants, while the Government represents~~ employers.

Commented [MPM2]: The Government does not represent employers. As a Plan sponsor, they are subject to general legal obligations at common law, as well as in legislation (Pension benefits Act). Different obligations apply to the plan sponsor depending on whether it is acting in its capacity as "employer" or as "plan administrator" in performing a particular duty.

DRAFT

OPSEU and the Government are equally responsible for ensuring the pension plan has enough money to meet its long-term pension obligations. Section 4.6 of the Plan Text notes that the Employer, shall pay into the Fund an amount equal to the aggregate amount of all contributions deducted from the members.

~~In addition, they appoint experienced, professional experts to the pension plan's Board.~~

~~The assets of the Plan are held by OP Trust~~OPTrust ~~in trust for the beneficiaries of the plan – Ontario public servants. The Government does not have unilateral access to the assets of the trust (including changing contribution amounts, taking contribution holidays, or withdrawals). Actions of this nature require negotiation and agreement between the two sponsors.~~

In addition, they appoint experienced, professional experts to the pension plan's Board.

The assets of the Plan are held by OPTrust in trust for the beneficiaries of the plan – Ontario public servants. The Government does not have unilateral access to the assets of the trust (including changing contribution amounts, taking contribution holidays, or withdrawals). Actions of this nature require negotiation and agreement between the two sponsors.

Commented [MPM3]: This is not always true.

Commented [NP4]: Expand, if details available, how many appointed by whom (understand that it is equal appointees, with joint appointment of the Chair)

Commented [NP5]: More specific please

Commented [NP6]: However, there is a question w.r.t. unilateral access to 'surplus' vs. the assets generically. Confirm.

The Funding Policy, Board-Approved Policy, dated July 17, 2014

~~OP Trust~~OPTrust provides the following regarding the use of Plan Surpluses:

~~OP Trust~~OPTrust recognizes that decisions on the use of surplus are reserved to the Sponsors. However, in the interests of providing information to the Sponsors, ~~OP Trust~~OPTrust has recommended a number of principles for the Sponsors to consider when determining how to use surplus that arises from time to time, designed to minimize the risk to future Plan funding. They are as follows, in order:

1. Use surplus to pay for any past unfunded liability that has not been fully paid through previous valuations where amortization of prior deficits is incomplete.

2. Restore benefits previously lost due to prior deficits.

3. Restore stabilization reserves to recommended levels to protect against future adverse actuarial and investment experience.

4. If the current employee and employer contribution rates are above the normal rate specified in ~~OP Trust~~OPTrust Management studies, use surplus to return contributions back to the normal rate.

5. If surplus is still available, consider temporary contribution reductions as the most predictable way to reduce the surplus in the Plan.

DRAFT

6. When considering Plan improvements, establish a preference for temporary benefit improvements over permanent Plan changes since temporary improvements will be prepaid from existing surplus and are less likely to have an impact on future contribution rates.

7. When considering permanent Plan improvements, recommend those that better rationalize the overall Plan design, such as provisions that present an undue hardship or level of unfairness to Plan members.

Member and Employer Rate Stabilization Reserves

The Sponsors of the OPSEUPP have established two stabilization reserves to deal with ~~surpluses~~ actuarial gains when they arise. The Employer and Member Stabilization ~~Funds~~ Reserves are the remaining employer's and members' share of the net actuarial gain. These ~~funds~~ reserves are to be used as a buffer against any future actuarial losses that may arise.

Gains (and losses) are shared equally by the employer and OPSEU, subject to the following:
(i) 50% of the gain or such other amount as may be collectively bargained shall be used for the benefit of employers, to be applied against any special payments required to be made by any employers and thereafter to reduce employers' normal costs [SA, s. 56 (c) (i)]; and
(ii) 50% of the gain or such other amount as may be collectively bargained shall be used for the benefit of Plan members [SA, s. 56 (c) (ii)].

Excerpts from Plan Text on Withdrawal of Surplus

Section 18.2 of the Plan text notes that, if the Plan is wound up in whole or in part, the assets in the Fund shall first be allocated for the provision of benefits in accordance with terms of the Plan, the Pension Benefits Act, the Income Tax Act (Canada) and any other applicable legislation or agreement between the sponsors.

Section 18.3 also notes that if after provision for benefits payable to or in respect of members of the wind up, in whole or in part, of the plan, assets remain in the Fund or the part of the Fund affected by a partial windup, such assets shall be applied as determined by OPSEU subject to the Pension Benefits Act and the Income Tax Act (Canada) for the exclusive benefit of the members and former members, their beneficiaries and dependents.

4.2 Accounting for OPSEUPP by the Province

The Province of Ontario's Public Accounts include a pension asset of $520M that represents the employer's share of the OPSEUPP surplus position based on the accounting actuarial valuation for the plan. This situation has arisen because, to this point in time, the government's share of the total contributions to the Plan plus the actual investment returns on the Plan's assets have exceeded the government's share of the accumulated retirement benefit expense. The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame.

Commented [MPM7]: "Very long"? Is the timeframe the remaining expected participant's working lifetime? Do we have this measure? Is it closer to 80 or to 18 years.

DRAFT

The Province recognizes 50% of the Accounting Surplus on the statement of financial position, which represents the Province's Share of the Pension Plan.

5.0 Question 1 – Classification of the OPSEUPP

5.1 Relevant Guidance on Classification

PS 3250 has specific application guidance to Joint Defined Benefit Plans:

Joint defined benefit plans

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

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

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans*. [SEPT. 2001]

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

5.2 Conclusion on classification

Application of PS 3250 to Joint Defined Benefit Plans

A joint defined benefit plan is a unique retirement benefit plan where the sponsors have shared control over the plan. No one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. Paragraph .081 of PS 3250 clearly states that a government should account for its portion of the Plan in accordance with the standards for defined benefit plans. As a result, the Province of Ontario accounts for its proportionate share of the Plan and has historically recorded its share as 50% of the plan.

DRAFT

6.0 Question 2 – Recognition of surplus

6.1 Standards in the PSA Handbook

The following standards were considered relevant when determining whether an asset can be recognized on the Public Accounts:

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans*. [SEPT. 2001]

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

6.2 Analysis

PS 3250.50 requires that an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. This comparison between the adjusted benefit asset and the expected future benefit informs whether a valuation allowance is required and if so, how much of a valuation allowance should be recorded.

PS 3250.52 contemplates that there are two ways in which a government can benefit from an accrued benefit asset. A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. As such, an expected future benefit would include the ability to either withdraw plan assets from the plan or reduce future contributions.

PS3250.52 also goes on to consider that an accrued benefit asset may become impaired when there is a plan surplus that the government is not entitled to benefit from fully. The paragraphs in the standard

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that follow determine how a government would go about considering the extent of any impairment, which would give rise to a valuation allowance. In order to make this determination, the government is required to consider the "expected future benefit", which would effectively create a ceiling for the asset. Here the guidance diverges between benefit expected to be realized through future reductions in contributions and those to be realized through withdrawal of surplus.

Specifically with respect to withdrawal of surplus, PS 3250.59 is very clear that expected future benefit can only be asserted where the government has a current legally enforceable right to withdraw assets from the Plan. This guidance was considered as to whether it should be applied to cases where the expected future benefit related to the Pension Asset is expected to be realized through reduced ~~contributions,~~contributions; however it was concluded that the guidance does not apply in this situation. While PS 3250.59 does introduce the concept of a legally enforceable right, it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions.

OPSEUPP has established two rate stabilization ~~funds~~reserves, being one for the employers and one for the employees. The Funding Management Policy establishes that gains must be shared equally amongst the sponsors. As actuarial gains are generated, the Province has the ability to use its 50% of the gain to reduce contributions.

6.3 Conclusion

The Province should account for OPSEUPP as a joint defined benefit plan, which means applying PS 3250 defined benefit accounting for its share of the plan. As the plan is in an asset position, the Province should reflect its proportion of the asset (50%) subject to any valuation allowance.

7.0 Question 3 – Measurement of a pension asset

7.1 Standards in the PSA Handbook

The following standards are relevant to determining how the Pension Asset should be measured

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

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

.055 The objective of the standard in paragraph PS 3250.50 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

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

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

7.2 Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250 paragraphs .053 to .058 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus". A valuation allowance is recorded against the pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test

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under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province calculated the expected future benefit as the sum of:

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

Each of these is discussed separately.

7.3 Considerations re: withdrawal of the surplus (Section PS 3250 paragraph .056 (b))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph .059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

For OPSEUPP, the Funding Policy does not contemplate surplus withdrawal and so for the purposes of this analysis, it is assumed that any surplus withdrawal would have to be negotiated between the sponsors.

There are no provisions in the ~~HOOPP~~ OPSEU Plan text to permit the withdrawal of a surplus. PS 3250.59 indicates that the expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal. As there is no certainty that the Province will be able to access ~~the~~ an OPSEUPP ~~s~~Surplus through withdrawal, the Province does not rely on withdrawal of surplus to support the measurement of the OPSEUPP asset.

Commented [MPM8]: OPSEU correxct?

7.4 Considerations re: reduced future contributions (Section PS 3250 paragraph .056 (a))

Section PS 3250 paragraph .056(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus.

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In the event of a surplus, ~~the OP Trust~~OPTrust recommends to the sponsors that certain principles be followed when determining how to use the surplus. The recommendation from ~~the~~ OP~~T~~ Trust is to ~~use~~ allocate ~~surpluses~~ actuarial gains to ~~fund~~ any unfunded liabilities or restore cuts to benefits due to prior deficits, before moving into ~~replenishing~~ the stabilization reserves, reducing contributions, and then restoring benefits. As such, there are two significant indicators that lead the Province to believe that future contributions can be reduced, which are:

1. The Province has its own stabilization reserve that can be utilized to reduce future contributions (so the Province has some autonomy and segregation of its 50% of the surplus)
2. The Funding Principles of the plan put an emphasis on restoring unfunded liabilities (which will reduce contributions in the future), and reducing current contributions, before enhancing benefits.

In determining the expected future benefit of the asset, the Province has looked at the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the Province is required to make regardless of any surplus. As there are no minimum contributions that the Province is required regardless of surplus, the expected future benefit will exceed the plan asset because the expected future benefit will equate to the expected future accruals for service for the current active employees (less employee contributions).

Commented [MPM9]: I do not understand what is being described here. Are you saying the Government does not have a minimum cash contribution requirement? Not sure what's the thought here.

7.8 Conclusion on measurement

The OPSEUPP is in an Accounting ~~S~~surplus position and can recognize an asset on the balance sheet. The measurement of that asset is subject to the asset ceiling test. The expected future benefit from the asset is the amount of contributions that could be reduced in the future from this surplus. As management has its own stabilization reserve and the Funding Policy promotes contribution reduction ahead of benefit improvement, the expected future benefit exceeds the net plan asset, which means that no valuation allowance should be recorded.

Commented [MPM10]: Capitalized Accounting Surplus consistent with pg 3 sec. 4.2 last paragraph.

Commented [MPM11]: As of December 31, 2015, the Plan is fully funded on a going-concern basis. The excess actuarial surplus, pursuant to section 147.2(2) of the Income Tax Act (Canada), is $0. Based on the solvency of the Plan, a deficit exists, as defined in the Regulation to the Pension Benefits Act (Ontario) of $(691) million.

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OPSEUPP paper.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]; Colavecchia, Pina (CA - Toronto) (pcolavecchia@deloitte.ca) [pcolavecchia@deloitte.ca]
Subject: OPSEUPP paper
Date: Thursday, December 01, 2016 13:28:29
Attachment 1: OPSEU - Accounting for Plan surpluses_dec 1.doc

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Matt/Pina,

Please find attached the OPSEUPP paper with comments and suggested edits. It would be helpful to include information on the history of use of surpluses which I believe was provided previously (perhaps as an appendix). In addition, reference to the ceiling test work that Martin performed should be included.

Thanks. Talk to you soon.

n

OPSEU - Accounting for Plan surpluses_dec 1.pdf

1.0 Preamble

This document addresses the accounting for an accrued benefit asset under Canadian Public Sector Accounting Standards (PSAS) by the Province of Ontario in relation to the Ontario Public Sector Employees Union ("OPSEU") Pension Plan ("OPSEUPP" or the "Plan").

As at March 31, 2016, OPSEUPP had an accrued asset position for accounting purposes of $~~520~~ 521 million.

The details of the accounting valuation for the plan for purposes of reporting by the Province as of March 31, 2016 are as follows:

(all figures in $M)	**Total plan**	**50% Share of the plan**
Market related value of assets	17,380	8,690
Value of obligation	15,557	7,778
Surplus (deficit)	1,823	912
Unamortized (gains) losses	(96)	(48)
Adjustment for March 31, 2016	(583)	(~~292~~291)
Asset (liability) position	1,144	~~572~~ 573
Specific Province of Ontario adjustment		(52)
Final Accrued Benefit Asset (liability) position on balance sheet		~~520~~521

2.0 Issue to be considered

1. For accounting purposes, how should OPSEUPP be classified under PSAS?
2. As a result of the classification, how should the Province of Ontario recognize the pension surplus (for accounting purposes) of OPSEUPP in the Public Accounts?
3. How should a pension asset of OPSEUPP be measured in the Public Accounts of the Province of Ontario?

3.0 Conclusions

1. OPSEUPP is a Joint Defined Benefit Plan under PS 3250
2. The Province of Ontario should account for ~~the~~ OPSEUPP as a defined benefit plan for its proportionate share of the surplus or obligation that arises under the plan.
3. The Province of Ontario should record its proportionate share of the asset and apply the asset ceiling test under PS 3250. The Province of Ontario believes that the asset is recoverable through the reduction of future contributions and as such, no valuation allowance is necessary.

4.0 Background information

4.1 Overview of OPSEUPP

The Plan is jointly sponsored by the Province of Ontario and the executive of OPSEU. The Plan is managed by OPTrust, a 10-member Board of Trustees, five of whom are appointed by OPSEU and five by the Province of Ontario. OPSEU and the Province of Ontario are equally responsible for ensuring the

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pension plan has the financial resources to meet its long-term pension obligations. Section 4.6 of the Plan Text notes that the Employer, shall pay into the Plan an amount equal to the aggregate amount of all contributions deducted from the members.

In addition, ~~they~~ the sponsors appoint experienced, professional experts to the ~~pension plan's~~OPTrust's Board. More specifically, the Province of Ontario and OPSEU each appoint to the Board of Trustees one experienced member to fill the position of Chair and Vice-Chair, with the roles alternating between Province of Ontario and OPSEU appointees every two years

The assets of the Plan are held by OPTrust in trust for the beneficiaries of the plan – Ontario public servants who work in the broader public sector (approximately 130,000 members across Ontario). The Province of Ontario does not have unilateral access to the assets of the trust (including changing contribution amounts, taking contribution holidays, or withdrawals). Actions of this nature require negotiation and agreement between the two sponsors. While access to the assets of the Trust is not in the Province of Ontario's sole control, it should be noted that the Province of Ontario, as a sponsor of the plan, has established a rate stabilization reserve in which surpluses are allocated to so that the Province's share of the surplus from the plan is identified and can be used for future decision making on funding and benefit improvements.

The Funding Policy, Board-Approved Policy, dated July 17, 2014

OPTrust provides the following regarding the use of Plan Surpluses:

OPTrust recognizes that decisions on the use of surplus are reserved to the Sponsors. However, in the interests of providing information to the Sponsors, OPTrust has recommended a number of principles for the Sponsors to consider when determining how to use surplus that arises from time to time, designed to minimize the risk to future Plan funding. They are as follows, in order:

1. Use surplus to pay for any past unfunded liability that has not been fully paid through previous valuations where amortization of prior deficits is incomplete.

2. Restore benefits previously lost due to prior deficits.

3. Restore stabilization reserves to recommended levels to protect against future adverse actuarial and investment experience.

4. If the current employee and employer contribution rates are above the normal rate specified in OPTrust Management studies, use surplus to return contributions back to the normal rate.

5. If surplus is still available, consider temporary contribution reductions as the most predictable way to reduce the surplus in the Plan.

6. When considering Plan improvements, establish a preference for temporary benefit improvements over permanent Plan changes since temporary improvements will be prepaid from existing surplus and are less likely to have an impact on future contribution rates.

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7. When considering permanent Plan improvements, recommend those that better rationalize the overall Plan design, such as provisions that present an undue hardship or level of unfairness to Plan members.

Member and Employer Rate Stabilization Reserves
The Sponsors of the OPSEUPP have established two stabilization reserves to deal with actuarial gains when they arise. The Employer and Member Stabilization Reserves are the remaining employer's and members' share of the net actuarial gain. These stabilization reserves are intended to be used as a buffer against any future actuarial losses that may arise.

Gains (and losses) are shared equally by Plan members, subject to the following:
(i) 50% of the gain or such other amount as may be collectively bargained shall be used for the benefit of employers, to be applied against any special payments required to be made by any employers and thereafter to reduce employers' normal costs [SA, s. 56 (c) (i)]; and
(ii) 50% of the gain or such other amount as may be collectively bargained shall be used for the benefit of Plan members [SA, s. 56 (c) (ii)].

Excerpts from Plan Text on Withdrawal of Surplus

Section 18.2 of the Plan Text notes that, if the Plan is wound up in whole or in part, the assets in the Fund shall first be allocated for the provision of benefits in accordance with terms of the Plan, the Pension Benefits Act, the Income Tax Act (Canada) and any other applicable legislation or agreement between the sponsors.

Section 18.3 also notes that if after provision for benefits payable to or in respect of members of the wind up, in whole or in part, of the plan, assets remain in the Fund or the part of the Fund affected by a partial windup, such assets shall be applied as determined by OPSEU subject to the Pension Benefits Act and the Income Tax Act (Canada) for the exclusive benefit of the members and former members, their beneficiaries and dependents.

4.2 Accounting for OPSEUPP by the Province of Ontario

The Province of Ontario's Public Accounts as of March 31, 2016 include an accrued pension asset of $521~~0~~M that represents the employer's share of the OPSEUPP surplus position based on the accounting actuarial valuation for the plan. This situation has arisen because, to this point in time, the Province of Ontario's share of the total contributions to the Plan plus the actual investment returns on the Plan's assets have exceeded the Province of Ontario's share of the accumulated retirement benefit expense. The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering the remaining life time of the employees.

The Province of Ontario recognizes 50% of the accrued benefit asset on its consolidated statement of financial position, which represents the Province of Ontario's Share of the Pension Plan.

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5.0 Question 1 – Classification of the OPSEUPP

5.1 Relevant Guidance on Classification

PS 3250 has specific application guidance to Joint Defined Benefit Plans:

Joint defined benefit plans

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

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

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans*. [SEPT. 2001]

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

5.2 Conclusion on classification

Application of PS 3250 to Joint Defined Benefit Plans

A joint defined benefit plan is a unique retirement benefit plan where the sponsors have shared control over the plan. No one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. This is the case for OPSEUPP where the Province and OPSEU are joint sponsors. This classification has been applied consistently by the Province for OPSEUPP for over the last 10 years. Paragraph .081 of PS 3250 clearly states that a government should account for its portion of the Plan in accordance with the standards for defined benefit plans. As a result, the Province of Ontario accounts for its proportionate share of the Plan and has historically recorded its share as 50% of the Plan.

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6.0 Question 2 – Recognition of surplus

6.1 Standards in the PSA Handbook

The following standards were considered relevant when determining whether an asset can be recognized ~~on~~ in the Public Accounts:

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans*. [SEPT. 2001]

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

6.2 Analysis

PS 3250.50 requires that an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. This comparison between the adjusted benefit asset and the expected future benefit informs whether a valuation allowance is required and if so, how much of a valuation allowance should be recorded.

PS 3250.52 contemplates that there are two ways in which a government can benefit from an accrued benefit asset. A government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. As such, an expected future benefit would include the ability to either withdraw plan assets from the Plan or reduce future contributions.

PS3250.52 also goes on to consider that an accrued benefit asset may become impaired when there is a Plan surplus that the government is not entitled to benefit from fully. The paragraphs in the standard

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that follow determine how a government would go about considering the extent of any impairment, which would give rise to a valuation allowance. In order to make this determination, the government is required to consider the "expected future benefit", which would effectively create a ceiling for the asset. Here the guidance diverges between benefit expected to be realized through future reductions in contributions and those to be realized through withdrawal of surplus.

Specifically with respect to withdrawal of surplus, PS 3250.59 is very clear that expected future benefit can only be asserted where the Province of Ontario has a current legally enforceable right to withdraw assets from the Plan. This guidance was considered as to whether it should be applied to cases where the expected future benefit related to the Pension Asset is expected to be realized through reduced contributions; however it was concluded that the guidance does not apply in this situation. While PS 3250.59 does introduce the concept of a legally enforceable right, it does so solely in the context of a government's future withdrawal of a Plan surplus, and not in the context of a government's reduction of future contributions.

OPSEUPP has established two rate stabilization reserves, being one for the employers and one for the employees. The Funding Management Policy establishes that actuarial gains must be shared equally amongst the Sponsors. As actuarial gains are generated, the Province of Ontario has the ability to use its 50% of the gain to reduce contributions.

6.3 Conclusion

The Province of Ontario should account for OPSEUPP as a joint defined benefit plan, which means applying PS 3250 defined benefit accounting for its share of the Plan. As the Plan is in an asset position, the Province of Ontario should reflect its proportion of the asset (50%) subject to any valuation allowance.

7.0 Question 3 – Measurement of a pension asset

7.1 Standards in the PSA Handbook

The following standards are relevant to determining how the Pension Asset should be measured

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

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

.055 The objective of the standard in paragraph PS 3250.50 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

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

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

7.2 Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250 paragraphs .053 to .058 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus". A valuation allowance is recorded against the pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test

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under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province of Ontario calculated the expected future benefit as the sum of:

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

Each of these is discussed separately.

7.3 Considerations re: withdrawal of the surplus (Section PS 3250 paragraph .056 (b))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph .059 indicates "The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal."

For OPSEUPP, the Funding Policy does not contemplate surplus withdrawal and so for the purposes of this analysis, it is assumed that any surplus withdrawal would have to be negotiated between the sponsors.

There are no provisions in the OPSEU Plan text to permit the withdrawal of a surplus. PS 3250.59 indicates that the expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal. As there is no certainty that the Province will be able to access an OPSEUPP surplus through withdrawal, the Province cannot rely on withdrawal of surplus to support the measurement of the OPSEUPP accrued benefit asset.

7.4 Considerations re: reduced future contributions (Section PS 3250 paragraph .056 (a))

Section PS 3250 paragraph .056(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus.

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In the event of a surplus, OPTrust recommends to the Sponsors ~~that~~ certain principles be followed when determining how to use the surplus. The recommendation from OPTrust is to allocate actuarial gains to any unfunded liabilities or restore cuts to benefits due to prior deficits, before moving into the rate stabilization reserves, reducing contributions, and then restoring benefits. As such, there are two significant indicators that lead the Province to believe that future contributions can be reduced, which are:

1. The Province has its own rate stabilization reserve that can be utilized to reduce future contributions (so the Province has some autonomy and segregation of its 50% of the surplus)
2. The Funding Principles of the plan put an emphasis on restoring unfunded liabilities (which will reduce contributions in the future), and reducing current contributions, before enhancing benefits.

In determining the expected future benefit of the asset, the Province has looked at the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the Province is required to make regardless of any surplus. As there are no minimum contributions that the Province is required regardless of surplus, the expected future benefit will exceed the plan asset because the expected future benefit will equate to the expected future accruals for service for the current active employees (less employee contributions).

7.5 Conclusion on measurement

The OPSEUPP is in an ~~Accounting S~~surplus position for accounting purposes and therefore it is appropriate to recognize an accrued benefit asset on the Province of Ontario's consolidated statement of financial position. The measurement of that accrued benefit asset is subject to the asset ceiling test. The expected future benefit from the asset is the amount of contributions that could be reduced in the future from this surplus. As each of the Plan Sponsors have their own stabilization reserves, and the Funding Policy promotes contribution reduction ahead of benefit improvement, the expected future benefit exceeds the net plan asset, which means there is no basis to require the recording of a valuation allowance.

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OPSEUPP recognition of accrued benefit asset.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Uros Karadzic [uros.karadzic@ca.ey.com]; Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: OPSEUPP recognition of accrued benefit asset
Date: Friday, April 07, 2017 16:44:27
Attachment 1: image002.jpg
Attachment 2: OPSEUPP Recognition of accrued benefit asset (EY 7 April 2017) - draft.pdf

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Hi Nadine,

Attached is the asset ceiling test document for OPSEUPP. The context of this document is similar to the document for OTPP. We will make the same changes to this document to address for any additional comments you/Cindy may have on the last version of the document for OTPP.

The most significant difference between the two documents is that we have reflected the RSF for OPSEUPP in our analysis. As you are aware, the most updated RSF information we've received from your team is as at 31 December 2014.

Once you have a chance to review the attached, we think it's best for us to schedule a call to discuss.

I will be following up with our weekly status update email shortly.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP

Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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image002.pdf

EY

OPSEUPP Recognition of accrued benefit asset (EY 7 April 2017) - draft.pdf

Ernst & Young LLP
Ernst & Young Tower
222 Bay Street, PO Box 251
Toronto, ON M5K 1J7

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Nadine Petsche
Director, Accounting Policy and Financial Reporting
Office of the Provincial Controller Division
7 Queen's Park Crescent, 2nd Floor
Toronto ON M7A 1Y7

7 April 2017

Ontario Public Service Employees' Union Pension Plan - DRAFT
Accrued benefit asset recognition

The Office of the Provincial Controller Division ("OPCD") has asked EY to undertake an asset ceiling test to inform OPCD's decision as to whether a valuation allowance is required in relation to the Province's share of the Ontario Public Service Employees' Union Pension Plan ("OPSEUPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").

This document provides the results of our analysis and recommendations to OPCD management regarding the recognition of an accrued benefit asset for OPSEUPP as at 31 March 2017. The purpose of this document is to support OPCD in forming its opinion on appropriate accounting related to OPSEUPP in the Province's financial statements. This document does not constitute an accounting opinion and should not be used as such. This document is intended for OPCD's use only. Please inform us in writing if you would like to share this document more broadly.

As at 31 March 2017, prior to considering the possible need for a valuation allowance, OPCD determined the following:

- Plan's accrued benefit asset is $1.95B (obligation of $16.60B, market related-value of asset of $18.51B, unamortized actuarial loss of $0.04B)
- The Province's portion (50%) of the accrued benefit asset is $0.61B[1]. This amount does not reflect any adjustment for the differential use of the Rate Stabilization Fund ("RSF") by the joint sponsors discussed later in this document.

Since our analysis determined that a valuation allowance is not required at 31 March 2017, it would appear appropriate to report the Province's portion of the accrued benefit asset of $0.65B ($0.61B, adjusted for the estimated differential use of the RSF) for its respective portion of the Plan.

1 Background Information

1.1 Key characteristics of the Plan

Following key characteristics of the Plan are most relevant to our analysis:

- The Plan is a Joint Defined Benefit Plan ("JDBP") under PSAS.

[1] Reflects specific downward net adjustment of $0.37B by OPCD to the Province's portion of the Plan for the Province's financial statements

- The Plan is jointly sponsored by the Province, represented by the Chair of the Management Board of Cabinet, and the Ontario Public Service Employees' Union ("OPSEU"), representing the employees.
- Funding valuations must be filed at least once every three years.
- The Province's portion of the Plan is 50% of the overall Plan, reflecting the sharing principle between the sponsors in accordance with the plan text and sponsorship agreement:
  - Employers match the contributions of the members.
  - Any emerging actuarial gains and losses are to be shared equally between the sponsors.
  - Any surplus is to be shared equally between the joint sponsors under the current arrangement (the proportion may be collectively bargained).
  - Any deficit is to be funded by the joint sponsors and required contributions will increase in equal amounts.
- The Plan has established a Rate Stabilization Fund ("RSF"), as the sum of past unspent surpluses which were evenly allocated between the joint sponsors. Each sponsor may decide, without the other joint sponsor's consent, the use of its portion of the surplus.
- As at 31 December 2014, the date of the most recently completed funding valuation, the Province's RSF balance was $0.1B and the OPSEU's RSF balance was $0.01B. This means that the OPSEU joint sponsor has historically used $0.09B more surplus than the Province.
- While the joint sponsors established a trust ("OPTrust"), the Board of Trustees is responsible for the administration of the Plan and the investment of the assets. Decisions related to amendments to the trust agreement, plan text, and sponsorship agreement (e.g. contribution level, benefit to be provided) are the responsibility of the joint sponsors.
- The funding policy provides the joint sponsors a recommended framework for addressing the priorities for surplus use and deficit funding.
- The Plan documents explicitly state that no surplus shall be paid out of the fund to either sponsors.
- Contribution holiday does not constitute a surplus withdrawal according to the sponsorship agreement. Furthermore, the sponsorship agreement permits contribution holiday (i.e. sponsors may use their respective RSF to meet any additional contribution requirements).

1.2 Assumptions for financial reporting

The following highlights key assumptions applied for the valuation of the obligation and costs at 31 March 2017 for the purpose of Province's financial statements. The assumptions represent best estimate assumptions, selected by the Province:

- The Province's financial statement year-end reporting is as at 31 March 2017 (the "measurement date")
- The measurement of assets and obligations are as at 31 December 2016 (the use of this earlier measurement date is permitted under PSAS 3250.039). We do not anticipate that the conclusion would be different at 31 March 2017
- Valuation discount rate: 5.90%
- Inflation rate: 2.00%
- Salary escalation rate: 1.75% per annum to 2019 and 2.75% thereafter

2 Considerations for the accrued benefit asset recognition

PSAS contains relevant guidance for recognition of an accrued benefit asset in respect of the Province's share of the Plan at 31 March 2017. We have considered the guidance under PS 3250 relating to recognition of an accrued benefit asset based on an expected future benefit available to the Province, in the context of accounting for a JDBP under PS 3250.

Joint Defined Benefit Plans

PS 3250.081 states "*when a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.*"

Under the current arrangement, the Province has an equal share (50%) in the costs and risks of the OPSEUPP. Both entitlement to any surplus and responsibility for any deficiency are shared equally between the Province and the employee sponsor. The determination of a net asset or liability (and valuation allowance, if applicable) is therefore performed on an aggregate Plan basis, and the Province's portion of that asset/liability is determined subsequently by applying 50% portion to the Province. A further adjustment may need to be made to account for differential use of RSF by each of the joint sponsors. The need for RSF adjustment was also noted in the Pension Asset Expert Advisory Panel report.

Province's ability to benefit from an accrued benefit asset

PS 3250.050 states "*an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs"*.

PS 3250.052 states "*a government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. The accrued benefit asset may become impaired when there is a plan surplus for accounting purposes that the government is not entitled to benefit from fully. For example, there may be a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus*".

The Province is only able to recognize an accrued benefit asset to the extent that they are able to derive an expected future benefit from such asset. As per PS 3250.052, an expected future benefit may arise from (i) withdrawal of surplus or (ii) by taking a contribution holiday or receiving a refund of contributions. The Plan text explicitly prohibits any surplus withdrawal by both joint sponsors. However, contribution holidays are permitted by the Ontario PBA and the Plan documents. As such, the Province has access to an expected future benefit through future contribution reductions. The Province may use its portion of the RSF for contribution reduction without any restriction and does not require consent by the other sponsor. Therefore, the joint sponsors can each benefit from their respective portion of plan surplus for accounting purposes.

3 Determination of the accrued benefit asset recognition

This section provides details on the determination of the accrued benefit asset in respect of the Plan. Based on PS 3250.50 to 3250.059 (Limit on the carrying amount on accrued benefit asset), we have estimated the adjusted benefit asset, the expected future benefit, the valuation allowance, and the accrued benefit asset (net of valuation allowance) to be recognized by the Province under PSAS as at 31 March 2017.

3.1 Adjusted benefit asset

PS 3250.053 states "*To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset. The adjusted benefit asset is the accrued benefit asset less net unamortized actuarial losses (determined on a basis using market value of assets)*".

Based on the financial information for the Plan as at the measurement date provided by OPCD, we have determined the unamortized actuarial gains/losses for the Plan on a basis using the market value of assets as follows:

Market value of assets ("MVA")	$18.90B
Market-related value of assets ("MVRA")	$(18.51)B
Actuarial gains/(losses) not recognized due to smoothing	$0.39B
Unamortized actuarial gains/(losses), on MRVA basis	$(0.04)B
Unamortized actuarial gains/(losses), on MVA basis	$0.35B

As there is an unamortized actuarial gain (determined on a basis using market value of assets), the adjusted benefit asset is equal to the Plan's surplus position on a market basis:

Market value of assets	$18.90B
Obligation	$(16.60)B
Plan surplus	$2.30B
Unamortized losses	$0.00B
Adjusted benefit asset (PS 3250.053)	$2.30B

The adjusted benefit asset for the Plan is $2.30B.

3.2 Expected future benefit

PS 3250.56 states **"***a government determines its expected future benefit the sum of:*

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

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

Present value of the Plan's expected future accruals

PS 3250.57 further states "*A government's expected future accruals for service for the current number of active employees are determined on a basis consistent with that used to determine its accrued benefit obligation…"*

According to the accounting results letter provided by OPTrust, the Plan's actuary (Willis Towers Watson, "WTW") has determined the following using the Province's assumptions for financial reporting under PSAB:

- The 2017 total service cost is $0.39B
- The total present value of expected future accruals is $13.88B as at 31 December 2016

The letter indicates that the present value of expected future accruals has been calculated on an open group basis (i.e. the current number of active employees). This is in line with PSAS requirements.

We have validated the actuary's calculation of the total present value of expected future accruals of $13.88B. We have estimated the present value of the Plan's expected future accruals to be approximately $12.38B, on an open group basis using a perpetuity approach (i.e. the current number of active employees) and the province's assumptions for financial reporting under PSAB as at the measurement date:

- Annual salary increase of 2.75% (ultimate rate)
- Discount rate of 5.90%

Our estimate of the present value of expected future accrual has been determined as follows: 2017 current service cost / (discount rate – ultimate rate of salary increase) = $0.39B / (0.059-0.0275) = $12.38B.

We note that our estimate is approximately $1.5B lower than the amount determined by the actuary. The actuary's result is likely more refined; however, the use of either figure will result in a valuation allowance of nil as the expected benefit exceeds the adjusted benefit asset. Therefore, we have not followed up with the actuary to reconcile this difference.

Minimum contributions the Province is required to make regardless of any surplus

As there is no minimum fixed contribution (as a percentage or dollar amount) requirement which is independent of the Plan's funding status, our interpretation is that there are no minimum contributions that the Province is required to make, regardless of any surplus. Moreover, since there is no restriction on the sponsor's use of its RSF, the contribution can be reduced to zero for the sponsors without each other's consent. The sponsorship agreement explicitly explains that a contribution holiday can be taken when there

is a surplus. Therefore, there is no minimum level of contribution required "regardless of any surplus". This interpretation is consistent with the interpretation we see applied in practice for other Canadian plan sponsors reporting under PSAS. It is also consistent with the conclusions of the Pension Asset Expert Advisory Panel report.

Present value of the required employee contributions

We note that PS 3250.056 is written in the context of a single sponsor Plan while the OPSEUPP is a joint-sponsored Plan. As such, the present value of the required employee contributions for OPSEUPP is nil (i.e. the employee contributions being referenced by PS 3250.056 is in respect to contributions made by employees who are not sponsor of the Plan). This interpretation is also consistent with the conclusions of the Pension Asset Expert Advisory Panel report.

Plan surplus that can be withdrawn

No plan surplus can be withdrawn by the joint sponsors.

Expected future benefit

Using the actuary's estimate of the present value of the Plan's expected future accruals, the expected future benefit for the Plan is the present value of the Plan's expected future accruals:

Present value of the Plan's expected future accruals (PS 3250.57)	$13.88B
Present value of the required employee contributions (PS 3250.056a)	(0.0)B
Minimum required contributions regardless of any surplus (PS 3250.056a)	(0.0)B
Plan surplus that can be withdrawn (PS 3250.056b)	0.0B
Expected future benefit (PS 3250.056)	$13.88B

The Plan's expected future benefit is $13.88B.

3.3 Valuation allowance

PS 3250.054 states "*the adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required*".

Per 3.1 and 3.2 of this letter, we have determined that the Plan's expected future benefit exceeds the Plan's adjusted benefit asset:

Plan's adjusted benefit asset (PS 3250.053)	$2.30B
Plan's expected future benefit (PS 3250.056)	$13.88B
Valuation allowance (PS 3250.054) [max (0, $2.30B – 13.88B)]	$0.0B

The Plan's accrued benefit asset is not impaired, and accordingly, no valuation allowance is required.

3.4 Accrued benefit asset recognition

The Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Accrued benefit asset	$1.95B
Valuation allowance (PS3250.054)	0.0B
Accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$1.95B

Based on the RSF allocation as at 31 December 2014, the most recent funding valuation date, OPSEU has utilized their RSF $0.09B more than the Province:

OPSEU's RSF balance at 31 December 2014	$0.01B
Province's RSF balance at 31 December 2014	0.10B
Adjustment for the differential use of RSF by the joint sponsors	$0.09B

In other words, the Province has $0.09B more of unused RSF than OPSEU at 31 December 2014.

Accordingly, the Province's portion of the Plan's accrued benefit asset, adjusted for the relative position of the sponsors' RSFs and net of valuation allowance as at the measurement date is:

Plan's accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$1.95B
Adjustment for the differential use of RSF by the joint sponsors	(0.09)B
Plan's accrued benefit asset to be divided equally between the joint sponsors	1.86B
Province's portion of the accrued benefit asset to be divided evenly (50% x 1.86B)	0.93B
Province's unused RSF in excess of OPSEU's RSF	0.09B
Other Province specific adjustment made by OPCD	(0.37)B
Accrued benefit asset to be recognized by the Province (PS3250.050)	$0.65B

Based on the results of the analysis above, OPCD may conclude that an accrued benefit asset of $0.65B could be recognized for the Province's financial reporting under PSAS. This asset is after an adjustment for the differential use of RSF by the joint sponsors. No asset impairment is required.

While the analysis in this document has been prepared independently, the conclusions overall are consistent with the conclusions of the Pension Asset Expert Advisory Panel report.

Appendix
Information Provided

Our analysis is based on the following information we received:

- Province's financial reporting information under PSAS as at 31 March 2017, prepared by OPCD
- Actuarial Information for the OPESU Pension Plan provided by OPSEU Pension Trust (related to 2016 year-end financial information, including to actuarial calculations performed by Willis Towers Watson)
- Analysis of Pension Asset ceiling Accounting Considerations for the Office of the Provincial Controller Division re: OPESU Pension Plan prepared by Deloitte for 31 March 2015 financial reporting
- OPSEUPP actuarial valuation funding report as at 31 December 2014 by Willis Towers Watson
- OPSEU actuarial gain or loss allocation history (up to 31 December 2014)
- OPSEUPP plan text
- The Sponsorship Agreement for OPESUPP
- Ontario Public Service Employees' Union Pension Act
- OPTrust Funding Policy: Board-Approved Policy
- Pension Asset Expert Advisory Panel report

Appendix
Applicable guidance under PS 3250

Measurement date

.39 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Limit on the carrying amount on accrued benefit asset

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

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

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

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

.54 The adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required.

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

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

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

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

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

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

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

Joint defined benefit plans

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

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

accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.

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

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

Glossary

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

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

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

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

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

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

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

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

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

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

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

benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.

OSS-00426611-AppG-ConfidentialityAgreement-October2014.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
CC: Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: OSS-00426611-AppG-ConfidentialityAgreement-October2014
Date: Friday, September 23, 2016 09:34:42
Attachment 1: OSS-00426611-AppG-ConfidentialityAgreement-October2014.docx

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Hi Lucy

Can you please sign the attached Confidentiality Agreement and return it to me asap. Please back date it to when the contract was signed. Also, if you can please have Martin, Sean and Michael sign as well.

Thanks

Shyrose

OSS-00426611-AppG-ConfidentialityAgreement-October2014.pdf

Confidentiality Agreement

During and following the term of the Agreement between **Pricewaterhouse Coopers LLP** (the "Vendor") and Her Majesty the Queen in right of Ontario as represented by the **President of Treasury Board Secretariat** and during and following the term of each Statement of Work entered into by the Vendor and pursuant to the Agreement (collectively, the "Agreements"), the undersigned agrees with the Vendor to keep confidential and secure all Confidential Information to which the undersigned may have access to in the course of the performance of services pursuant to any of the Agreements (including requests for services) or otherwise in connection with any of the Agreements (including requests for services). "Confidential Information" means all information of the Ontario Public Service and of the Client's subcontractors at any tier of subcontracting that is confidential by its nature or in the circumstances in which it is received, including all confidential information in the custody or control of the Ontario Public Service, regardless of whether it is identified as confidential or not, and whether recorded or not, and however fixed, stored, expressed or embodied, which comes into the knowledge, possession or control of the Vendor in connection with any of the Agreements. "Ontario Public Service" means the ministries and other administrative units of Her Majesty the Queen in right of Ontario ("Ontario") over which ministers of Ontario preside, and for the purposes of this Confidentiality Agreement, includes Ontario and Ontario's agencies, boards, commissions and Crown corporations, offices of an officer of the Legislative Assembly or of the Ontario Legislature and OPS Entities, and "**OPS**" has the same meaning.

The undersigned acknowledges that the Client is bound to maintain custody of or control over information, material and records, however recorded, within the meaning of the Freedom of Information and Protection of Privacy Act ("FIPPA"). The undersigned agrees to comply with the privacy provisions of the Agreements in the course of providing services pursuant to the Agreements.

The undersigned shall not directly or indirectly disclose, destroy, exploit or use any Confidential Information except for the purpose of performing services pursuant to the Agreements. The undersigned shall not copy any Confidential Information, in whole or in part, unless copying is essential for the performance of services pursuant to the Agreements. On each copy, the undersigned must reproduce all notices that appear on the original.

The undersigned acknowledges that the Vendor is obliged to implement and maintain measures to ensure the security and integrity of Confidential Information and to protect it against loss, alteration and destruction and against access by unauthorized persons, and to select, implement, use and maintain the most appropriate products, tools, measures and procedures to do so. The undersigned covenants and agrees to adhere to all of the measures instituted by the Vendor.

The undersigned agrees to return all Confidential Information, including all copies and portions thereof, to the Vendor or to the Client with no copy kept by the undersigned as soon as the need to possess them ends, at the request of the Client, and in any event, prior to concluding the performance of services pursuant to the applicable Agreements.

Name: _____ Signature: _____

Date: _____

Witness: Signature: _____

Date; _____

OTPP (additional materials).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: OTPP (additional materials)
Date: Friday, September 16, 2016 21:37:49
Attachment 1: Key Funding Decisions.pdf
Attachment 2: AnnRepCommentary2000 (1).pdf
Attachment 3: Financials2000.pdf

Lucy,

Attached are a few excerpts from a few documents that might help with your analysis. This information was provided by our Income Security and Pension Policy Division. I will send additional document in separate emails as well. Nadine

From the 2000 Financials – p. 17-18

Pursuant to the *Partners' Agreement* between the Ontario Teachers' Federation (OTF) and the Province, the Partners entered into negotiations to decide how to utilize the gain. Pursuant to the agreement reached on April 18, 1998, the Partners agreed to share the 1998 actuarial gain of $6.78 billion and future gains in the following sequence:

(i) $2.24 billion would be spent on improving benefits;

(ii) special payments on the pre-1990 unfunded liability would be eliminated at an estimated cost

of $8.45 billion; and

(iii) a further $8.45 billion less the $2.24 billion would be spent on improved benefits or member contribution rate reductions, subject to the Province's consent prior to April 1, 2001; or held in a contingency reserve as determined by the OTF.

As a result, $2.24 billion of the gain was used to improve benefits under the Plan, and the remaining $4.54 billion of the gain was used to eliminate the obligation of the Province to make special payments after November 30, 2008.

From this summary of Key funding Decisions

A preliminary $6.8 billion surplus was distributed: $2.2 billion to pay for the 85 factor window from 1998 to 2002 and further lower the CPP reduction to 0.6%;

$4.6 billion to reduce the value of special payments owed by the Ontario government.

OTF and the Ontario government agree future surplus would be used to eliminate the government's remaining special payments, and the next $6.2 billion surplus would be available to OTF for benefit improvements.

From the Annual Report 2000 (pg. 6)

In 1998, the Ontario Teachers' Federation (OTF) and the Ontario government signed an agreement under which they improved benefits and allowed the government to use surplus to eliminate the special payments it was making to pay off the pre-1990 unfunded liability.

This occurred in 1998 and 1999. The OTF would then receive a similar amount, set at $6.2 billion, for use at its discretion. The plan started 2001 with a funding surplus of $6.8 billion. Effective April 1 2001, $6.2 billion of this surplus will be used by the OTF to improve benefits.

Key Funding Decisions.pdf

Key Funding Decisions Since 1990

The Ontario Teachers' Federation (OTF) and the Ontario government, which jointly sponsor the Ontario Teachers' Pension Plan, must file a funding valuation with the provincial pension regulator at least every three years. A valuation must be filed with assets and liabilities (the cost of future pensions) in balance.

OTF and the Ontario government can file a valuation earlier than required to help manage the plan's funding status.

The following chart shows how OTF and the Ontario government have used surplus funds or resolved funding shortfalls for each valuation filed with the regulator since the inception of the Ontario Teachers' pension plan as an independent entity in 1990.

For more information on plan funding, visit the Corporate section of our website at www.otpp.com.

Funding decisions

YEAR	VALUATION STATUS AND KEY DECISIONS
1990	A preliminary unfunded liability of $7.8 billion to be amortized over 40 years by special payments from the Ontario government; basic contribution rate increased to 8% from 7%.
1993	A preliminary $1.5 billion surplus was distributed: $1.2 billion used to reduce government's special payments; $0.3 billion used to offset government cost reductions in the education sector (social contract days).
1996	A preliminary $0.7 billion surplus was distributed: $0.6 billion used to reduce early retirement penalty to 2.5% from 5% for each point short of 90 factor and lower the CPP reduction after age 65 (to 0.68% from 0.7%).
1998	A preliminary $6.8 billion surplus was distributed: $2.2 billion to pay for the 85 factor window from 1998 to 2002 and further lower the CPP reduction to 0.6%; $4.6 billion to reduce the value of special payments owed by the Ontario government. OTF and the Ontario government agree future surplus would be used to eliminate the government's remaining special payments, and the next $6.2 billion surplus would be available to OTF for benefit improvements.
1999	A preliminary $3.5 billion surplus was distributed to eliminate government's remaining special payments.

YEAR	VALUATION STATUS AND KEY DECISIONS
2000	$4.5 billion surplus; no changes to benefits or contribution levels.
2001	A preliminary $6.8 billion surplus was distributed: $6.2 billion to pay for benefit improvements, including a permanent 85 factor; 10-year pension guarantee; reduced pension as early as age 50; lower CPP reduction (to 0.45%); 5-year average Year's Maximum Pensionable Earnings (YMPE) to calculate CPP reduction; pension recalculation based on approximate best-5 salary years for older pensioners; and top-up waived for Long-Term Income Protection (LTIP) contributions. The remaining $76 million was set aside in a contingency reserve to be used by OTF at a later date.
2002	$1.9 billion surplus; no changes to benefits or contribution levels.
2003	$1.5 billion surplus; no changes to benefits or contribution levels. Funding Management Policy adopted by plan sponsors.
2005	A preliminary $6.1 billion shortfall was resolved, leaving plan with a $0.1 billion surplus. Shortfall resolved with special contribution rate increases, totalling 3.1% of base earnings by 2009 for teachers, the Ontario government and other employers. OTF used the $76 million contingency reserve set aside in 2001 to reduce contribution rate increases for members in 2008.
2008	A preliminary $12.7 billion shortfall was resolved with the introduction of conditional inflation protection for pension benefits earned after 2009 and an increase in the basic contribution rate for members and the government to 9% from 8%. Employers agree to make special payments equal to any annual pension increases retirees forgo to a maximum of 50% missed inflation.
2009	A preliminary $2.5 billion shortfall was resolved primarily by assuming a slightly higher long-term rate of return on investments: yield on real-return bonds plus 1.5%, versus real-return bonds plus 1.4%. Other minor changes made to assumptions to reflect recent plan experience.
2011	A preliminary $17.2 billion shortfall was resolved with a 1.1% contribution rate increase (phased in over three years), slightly smaller annual cost-of-living increases for teachers who retired after 2009, and recognition of current contribution rate as the permanent base rate.
2012	$9.6 billion preliminary shortfall adjusted to reflect changes in mortality assumptions and impact of two-year freeze on teachers' salaries. 2012 shortfall resolved by making inflation protection for pension credit earned after 2013 fully conditional on plan's funded status and providing slightly smaller pension increases, beginning in 2014, for members who retired after 2009. These changes enabled the plan to assume a slightly higher discount rate. The changes left the plan with a $200 million surplus at Jan. 1, 2012.

YEAR	VALUATION STATUS AND KEY DECISIONS
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.

AnnRepCommentary2000 (1).pdf

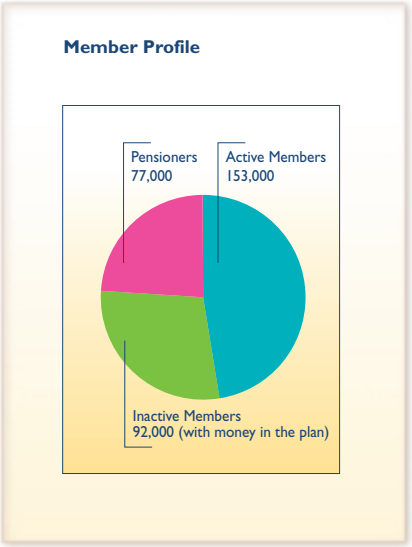
Teachers' Pension Plan Board

Conseil du régime de retraite des enseignantes et des enseignants

2000 ANNUAL REPORT

CORPORATE VISION

OUTSTANDING SERVICE TODAY, RETIREMENT SECURITY TOMORROW



CORPORATE PROFILE

The Ontario Teachers' Pension Plan Board is responsible for the future retirement income of 153,000 elementary and secondary school teachers, 77,000 retired teachers and their survivors, and 92,000 former teachers with entitlements in the plan. The plan is sponsored by a partnership between the Ontario government and the plan members, represented by the Ontario Teachers' Federation. The co-sponsors negotiate the use of surplus and have an equal say in the plan's design, including changes in benefits.

The pension board's current asset-mix policy is 60 percent equities, such as shares in public and private companies and equity-return derivative contracts; 22 percent inflation-sensitive assets such as real estate, real-rate bonds and commodities; and 18 percent fixed-income securities, largely federal and provincial government bonds.

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CORPORATE DIRECTORY

FINANCIAL HIGHLIGHTS

AS AT DECEMBER 31

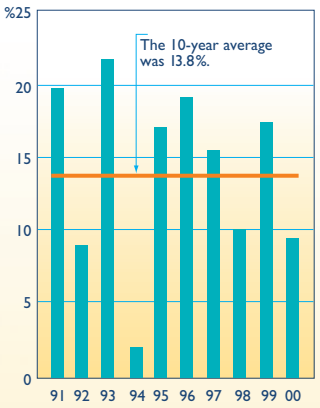
INVESTMENT PERFORMANCE

Rate of return on investments (%)	2000	1999
Annual	**9.3%**	17.4%
Composite benchmark	**5.3**	17.6
Four-year average	**13.0**	15.4
Four-year benchmark	**12.5**	15.8

Average annual compound rates of return (%)

	1 yr	4 yr	5 yr	10 yr	SINCE INCEPTION
Our return	9.3	13.0	14.2	13.8	13.1
Benchmark	5.3	12.5	13.6	12.7	10.7

Rates of Return



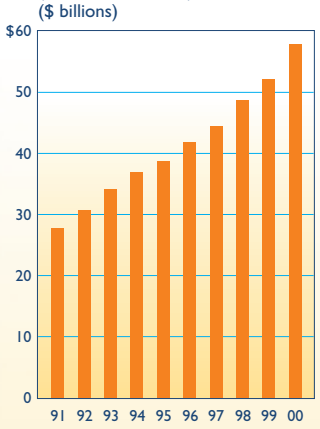
FINANCIAL OVERVIEW

($ Billions)	2000	1999[2]
Net investments	**$ 72.0**	$ 67.1
Net receivables	**1.1**	1.2
Net assets	**73.1**	68.3
Smoothing reserve[1]	**4.3**	8.3
Actuarially adjusted net assets	**68.8**	60.0
Cost of future pensions	**58.6**	52.1
Surplus	**$ 10.2**	$ 7.9

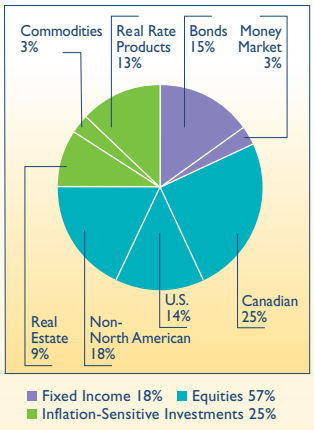
[1] We smooth equity gains (or losses) over five years to reduce the impact of market volatility on plan surplus. The smoothing reserve consists of investment gains in excess of the rate of return assumptions used in the financial statement valuation.

[2] Restated

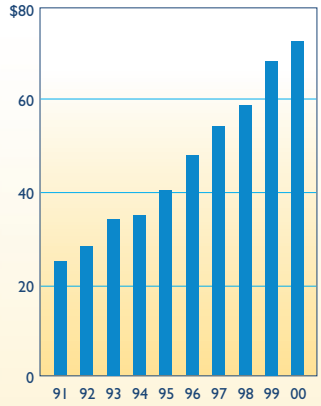
Cost of Future Pensions
(as at December 31)
($ billions)



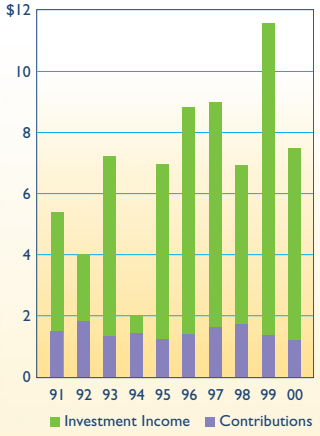
Asset Mix
(as at December 31, 2000)



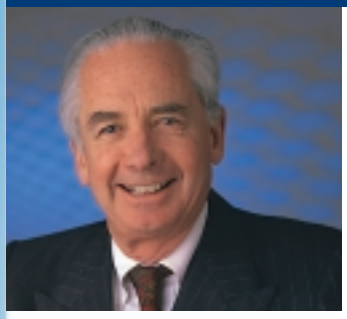
Net Assets
(as at December 31)
($ billions)



Income
($ billions)



CHAIR'S REPORT



ROBERT W. KORTHALS
CHAIR

Financial markets were highly volatile in 2000, a trend we expect to continue. Despite the less reliable investment climate, the pension board's investment staff have done a great job of creating value by exceeding market returns.

Since 1990, strong stock markets around the world have helped the fund grow faster than the increase in the cost of future pension benefits. However, what has really made the difference are deliberate decisions that allowed us to do better than the market.

Over the past decade we have gained exposure to foreign markets through equity-based derivatives and partnerships with external managers to earn value-added returns from active equity selection. We have built one of the largest merchant banks in Canada to earn premium returns from private equity markets. We have introduced innovative portfolio management techniques to earn above-market returns from equity and fixed-income index funds. Most recently, we purchased The Cadillac Fairview Corporation, making us one of the largest Canadian owners of North American real estate.

BEST-EVER VALUE ADDED

These and other initiatives paid off handsomely in 2000, with portfolio managers achieving $2.6 billion in value added. This amount is the difference between the total fund return of 9.3 percent and the 5.3 percent return for the composite benchmark. All this confirms the importance of actively managing the asset base and rewarding investment managers and senior executives for their effort.

Looking back at the value added to the fund over the last four years, the investment team averaged 13 percent against a benchmark of 12.5 percent. Since inception, they averaged 13.1 percent, beating the benchmark of 10.7 by 2.4 percent. In dollar terms, that means our investment team has created $6 billion in value added since 1990.

On behalf of the Board of Directors, I want to congratulate our entire investment team for their professionalism, foresight and innovation to meet the growing needs of the pension plan with value added investment income. It has been, and continues to be, a job well done.

AVOIDING UNDUE LOSS

The emphasis on maximizing returns also means trying to avoid unnecessary losses when markets turn for the worse. It is difficult, of course, for a large investment fund to predict short-term trends. Nevertheless, the pension board is attentive to prudent opportunities.

A good example in 2000 concerned technology stocks. Going into the year, we believed that most technology stocks were overvalued. The pension board took proactive action by reducing its technology holdings in Canadian and American stocks. As a result, we avoided substantial losses that would otherwise have occurred.

Managing Our Technology Exposure

(percent)	Q1	Q2	Q3	Q4
Technology Stocks % of TSE 300 Index	31.1	41.5	38.4	26.0
% Underweight in our portfolios	3.4	4.8	5.8	3.6

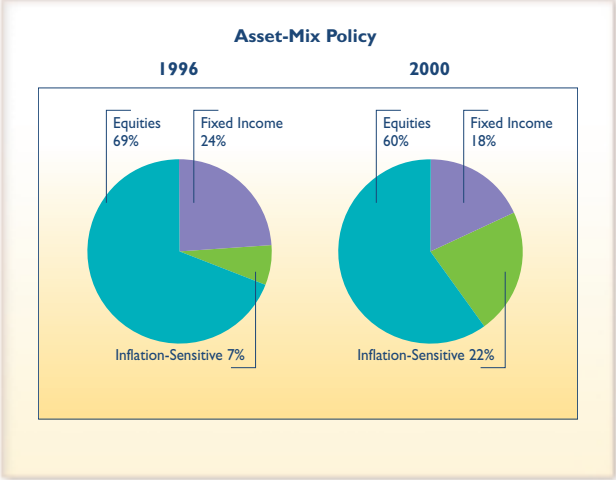
We reduced our exposure to technology stocks as a percentage of the TSE 300 Index throughout 2000.

PROTECTING THE FUND

Finding ways to add value by maximizing returns without incurring undue loss is a priority in view of the increasing number of pensioners. Since the mid-1990s, we have modified our investment approach to meet the changing needs of the pension plan.

Our asset mix continues to shift from equities and bonds to inflation-sensitive assets, especially commercial real estate properties, real-rate bonds and

commodities. These investment classes have been chosen specifically for their ability to rise in value with inflation, mitigating the long-term cost impact of inflation on growing liabilities, and safeguarding the fund if current expectations of lower returns from investment in stocks over the next decade are realized.



The asset-mix policy has changed over the past five years as we strive to better match assets that react to inflation with the indexed nature of pension benefits.

ACKNOWLEDGEMENTS

We are pleased with the investment performance of the pension fund in 2000 and prior years, and remain confident that our investment strategy, implemented by innovative portfolio managers, will continue to add value to the fund. We are impressed with the progress made to provide members of the plan with faster, more personalized service.

We are also pleased that both partners recognize the need for a strong and independent Board of Directors to oversee the pension board. We thank them for appointing directors with the skills and knowledge relevant to governing both a large investment and customer service organization.

ROBERT W. KORTHALS

CHAIR

BOARD OF DIRECTORS

ROBERT W. KORTHALS
Former President of the Toronto-Dominion Bank
Chair of the Board and Chair of Human Resources and Compensation Committee

JALYNN H. BENNETT
President of Jalynn H. Bennett & Associates Ltd., a consulting firm specializing in strategic planning and organizational development
Chair of the Investment Committee and member of the Governance Committee

GEOFFREY W. CLARKSON
Fellow of the Institute of Chartered Accountants of Ontario and former senior partner with Ernst & Young
Chair of the Benefits Adjudication Committee and member of the Audit and Actuarial Committee

ANN FINLAYSON
Journalist, speaker, freelance editor and consultant, author of three books, including *Whose Money is it Anyway? The Showdown on Pensions* (1988)
Member of the Audit and Actuarial Committee

LUCY G. GREENE
Former Vice-President of Human Resources with Sun Life Assurance Company of Canada
Chair of the Governance Committee and Vice-Chair of the Benefits Adjudication Committee

JOHN S. LANE
Former Senior Vice-President of Investments for Sun Life Assurance Company of Canada, and a Chartered Financial Analyst
Member of the Audit and Actuarial Committee

RALPH E. LEAN, Q.C.
Senior partner with the law firm Cassels Brock & Blackwell in Toronto
Member of the Governance Committee

DAVID J. LENNOX
Former Secretary of the Ontario Public School Teachers' Federation, former school principal
Chair of the Audit and Actuarial Committee

GARY PORTER
Chartered accountant and founding partner of the accounting firm Porter Hétu International, and a past president of the Certified General Accountants Association of Ontario
Member of the Audit and Actuarial and Governance Committees

All board members serve on the Investment and the Human Resources and Compensation Committees.

CLAUDE LAMOUREUX
PRESIDENT AND CHIEF EXECUTIVE OFFICER

The pension plan enjoyed another strong year in 2000, despite the negative performance of foreign equity markets, where we had about one-third of our assets invested. The total fund return of 9.3 percent produced $6.2 billion in investment income, increasing the value of net assets to $73.1 billion at year end. These results compared with a 17.4 percent total fund return and $10.1 billion in investment income in 1999.

IMPORTANCE OF THE FUNDING SURPLUS

As most readers of annual reports know, the most important number is often hidden in a footnote in the back of the report. This report is no exception – if you look at page 41, you'll find the surplus based on the funding valuation. I want to explain its significance and the resulting funding surplus. It is this figure – the funding surplus – that is particularly important to active and retired teachers because it is the amount available to the co-sponsors for plan changes.

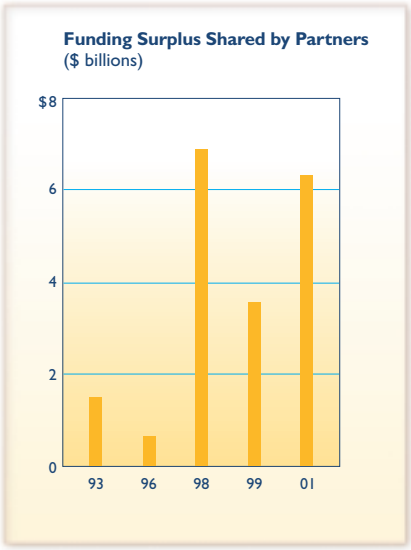
However, in our annual report, we focus on the "financial surplus" for financial statement purposes (sometimes called "management's best-estimate"). Both the annual and funding valuations look to the future, estimating the length of a teaching career, inflation and salary increases, and how long teachers will live. However, the annual valuation only looks at the financial situation at year-end and does not include the benefits that members will accrue in the future. For example, if a teacher taught for 10 years, the financial statement surplus takes into account that the plan has enough money to pay the pension equivalent for 10 years' credit.

The funding valuation, used to determine the funding surplus available to spend on benefit improvements, is a different calculation. In addition to the factors already mentioned, the funding valuation takes into account the pension that will be earned in the future, not just what has been earned up to the end of last year. In comparison, if a teacher taught for 10 years, the funding valuation includes 10 years of credit plus estimates how much money will be needed to pay the pension if he or she teaches to the 85 factor in 20 more years. It also includes how much more the teacher and the government will contribute over that time, and how much investments will grow.

USE OF SURPLUS

In 1998, the Ontario Teachers' Federation (OTF) and the Ontario government signed an agreement under which they improved benefits and allowed the government to use surplus to eliminate the special payments it was making to pay off the pre-1990 unfunded liability. This occurred in 1998 and 1999. The OTF would then receive a similar amount, set at $6.2 billion, for use at its discretion.

The plan started 2001 with a funding surplus of $6.8 billion. Effective April 1 2001, $6.2 billion of this surplus will be used by the OTF to improve benefits.



The partners will have used $18.7 billion in surplus by April 2001 to pay off the pre-1990 unfunded liability and make benefit improvements, including early retirement incentives.

A funding valuation by an independent actuary is required at least every three years. It determines whether the plan has sufficient funds to meet all future pension obligations resulting in a funding surplus or deficit, and is used as a guide to set contribution rates.

The funding valuation is a comprehensive calculation about the pension plan's financial future. It estimates the length of a teaching career, inflation and salary increases, teacher and government contributions over the length of a career, how long teachers will live, and how much investments will grow in the future.

The accompanying chart demonstrates how the funding valuation surplus is calculated.

Funding Valuation Results (before surplus allocation)

($ Billions) (at January 1)	**2001**	2000	1999	1998	1996	1993	1990
Net assets	**73.1**	68.3	59.1	54.5	40.1	29.4	21.0
Smoothing reserve	**4.3**	7.3	5.1	6.0	1.8	—	—
Value of assets	**68.8**	61.0	54.0	48.5	38.3	29.4	21.0
Future contributions	**14.4**	13.4	12.0	12.6	14.5	14.3	12.2
Future special payments*	**—**	—	3.7	8.5	8.4	8.4	—
Actuarial assets	**83.2**	74.4	69.7	69.6	61.2	52.1	33.2
Future benefits	**76.4**	69.8	66.2	62.8	60.5	50.6	41.0
Surplus (deficit)	**6.8**	4.6	3.5	6.8	0.7	1.5	(7.8)

* Payments by the government toward the pre-1990 unfunded liability.

Most of the surplus will be used in April 2001 to improve benefits, including a permanent 85 factor.

Value of assets is the value of net assets minus the smoothing reserve.

Actuarial assets refers to the value of assets as determined by the market plus the present value of future contributions by existing plan members.

Future benefits is an actuarial estimate of what it will cost to pay promised pensions over the lifetime of all current members. The cost fluctuates with market conditions and is not smoothed.

Surplus refers to the "funding surplus" (or deficit) above the cost of all future pension benefits for current members.

ASSUMPTIONS

Underlying the valuation are economic and demographic assumptions. The three most important assumptions are identified in the accompanying table.

Funding Valuation Assumptions

(percent) (at January 1)	**2001**	2000	1999	1998	1996	1993	1990
Discount rate	**6.25**	6.5	7.5	7.5	8.0	8.0	8.5
Salary escalation	**3.20**	3.25	4.5[2]	4.5[1]	5.0	5.0[1]	5.75
Inflation rates	**2.20**	2.25	3.5[3]	3.5[1]	4.0	4.0[1]	4.5

[1] except 2% for 2 years.
[2] except 2% for 2 years, 3.25% for 1 year
[3] except 2% for 2 years, 2.75% for 1 year

Salary changes affect the cost of future benefits because pension calculations are based on each member's best five years' salary. Pensions are fully indexed to inflation, which also increases pension costs.

Starting in 2000, we use the same assumptions for the annual valuation included in the financial statements.

Discount rate refers to the long-term market rate of return used to determine the present value of all future pension benefits and assets. It is assumed, as shown in the chart, that the discount rate will exceed inflation by approximately four percent.

Salary escalation and inflation rates It is assumed that, over the long term, increases in teachers' salaries will exceed inflation by one percent.

Even a seemingly small economic or demographic change can have a major impact on the plan's funding position. For example, a male teacher retiring at 57 years of age in 1995 had a life expectancy of 24.0 years, compared with 25.1 years for a similarly aged male teacher retiring in 2000. Changing the assumptions to reflect this improvement in the mortality experience of male retirees increases the plan's liability costs by $800 million.

PARTNERSHIP

As sole plan sponsor from 1917 until 1992, the Ontario government was responsible for all funding deficits and entitled to all funding surplus.

In 1992, the Ontario Teachers' Federation negotiated a partnership with the government. Teachers are now responsible for half of any surplus or deficit. As stated earlier, the partners negotiate the use of surplus and also have an equal say in the plan's design, including changes in benefits. The past use of actuarial surplus is discussed in note 9 to the financial statements.

NEED FOR A SURPLUS POLICY

Since 1990, whenever a funding surplus has existed, it has been used to eliminate special contributions or increase benefits.

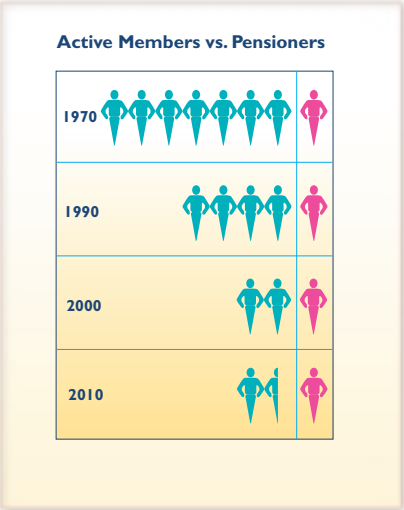
The partners know this level of yearly surplus creation is not sustainable. We are very concerned that current contribution rates will not be sufficient to cover the cost of future benefits, particularly if our current market forecasts for the next 10 years prove correct.

We encourage the partners to create a surplus policy, and we will commit resources to assist them. This policy would include the level above which the funding surplus would be used, and would be similar to the legislated capital reserve policies for banks and insurance companies. This would help to ensure some stability for contribution rates.

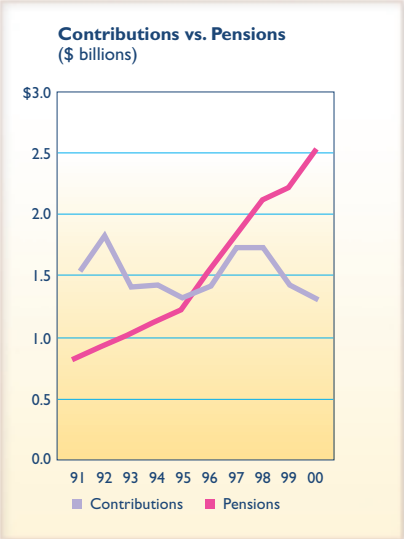
We believe it is essential to begin working today on a policy for the future because, if the plan is underfunded at a statutory valuation in the future, it will be the responsibility of the partners to make up the shortfall.

Small surplus The present value of all pensions is rising rapidly as the plan matures, totalling $76.4 billion at January 1, 2001. Sufficient assets were in place to meet these obligations with actuarially valued assets of $68.8 billion and future contributions valued at $14.4 billion, leaving a surplus of $6.8 billion. After these funds are assigned to plan improvements in April 2001, the plan will have only a small surplus of $600 million, less than one percent of liabilities.

Changing profile The profile of the plan has changed leaving fewer contributors while the number of teachers on pension continues to grow. Therefore, even an increase in contribution rates will have a reduced ability to compensate for a deficit. Ten years ago, future contributions were sufficient to cover about one-third of future benefits. Today, those contributions would only cover 19 percent.

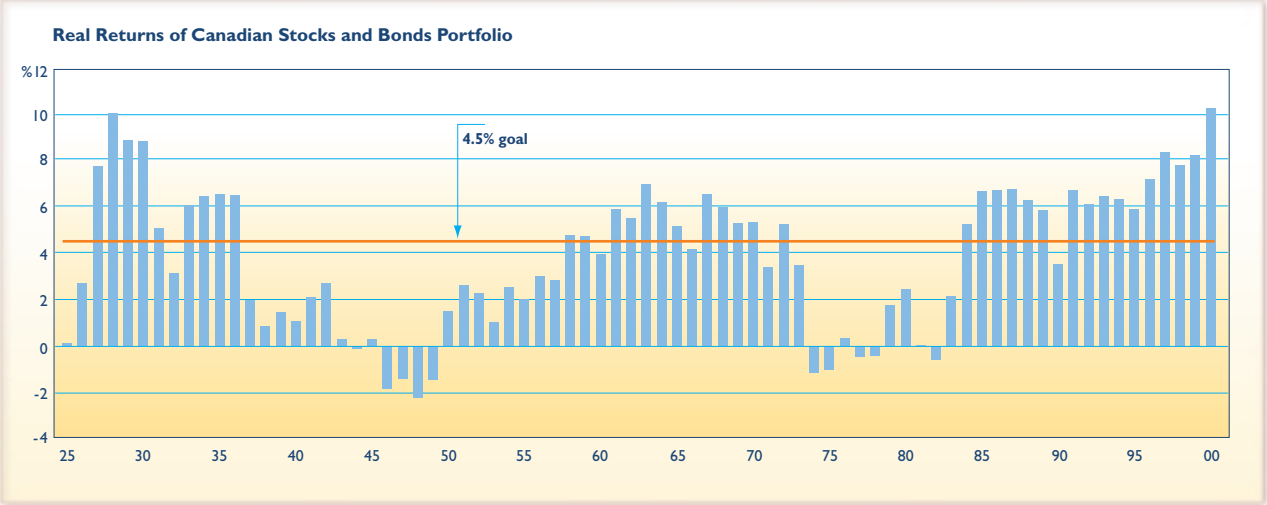


With only two active members for every pensioner today, there are half as many contributors per retiree as there were 10 years ago.



The gap between contributions and pension payments continues to widen. In 2000, 153,000 teachers and the government contributed $1.3 billion and we paid out $2.5 billion in benefits.

Increased risk In future, we expect modest real rates of return from stock and bond markets compared with the past 10 years. If history repeats itself, low or negative real-rate returns are possible over multiple years, as the accompanying chart illustrates. We are more concerned now about the impact of short-term market volatility on our ability to keep contributions stable than we were 10 years ago.



This chart tracks the rolling 10-year average real rate performance of an index-based portfolio consisting of two-thirds Canadian stocks and one-third Canadian bonds. The portfolio would reach our long-term investment target of 4.5% less than half the time.

WORKING WITH THE PARTNERS

Based on current valuation assumptions and the benefit improvements on April 1, the plan could require at least a 1.5 percent increase (matched by the government) in the contribution rates from the current average of 8 percent of salary. In the absence of such an increase in contribution rates, the plan must rely on investment returns above the actuarial assumption to make up the difference.

Our job as investment managers is to ensure that teachers receive the pensions they are promised. In the interest of prudent management, we will support the partners in developing a policy on surplus because we believe a large increase in the contribution rate would be unacceptable to plan members. Having a surplus policy in place would also help us plan our investment strategy, allowing us to build the most appropriate asset mix and investment programs around the policy.

In the meantime, we assure plan members that the pension board is committed to maximizing investment returns so that asset values have a better chance of keeping pace with the rising value of promised pensions.

STRIVING FOR EFFICIENCY

In seeking above-average investments, as well as providing timely and personalized member services, we strive to be an efficient organization. Last year, it cost $133 million to operate the pension board. Ongoing administrative costs were $106 per member. Investment expenses at 14 cents per $100 of net assets were low compared with many other institutional investors. These costs are tabulated in note 12 to the financial statements.

ACKNOWLEDGEMENTS

Our bi-annual employee survey showed that the pension board continues to be an attractive place to work. The positive attitudes and professionalism of staff are behind our standing as one of the consistent top investment performers in the pension fund industry as well as our highest-ever customer satisfaction rating from teachers and retirees. We remain committed to doing an even better job in the future.

CLAUDE LAMOUREUX

PRESIDENT AND CHIEF EXECUTIVE OFFICER

The challenge of faster, better and friendlier service

We are a customer-focused organization with a broad mandate that covers dozens of benefit entitlements and we serve more than 300,000 clients. Our services extend far beyond calculating and paying pensions; we respond to the ever-changing needs of our plan members and pensioners.

Member Services Volumes

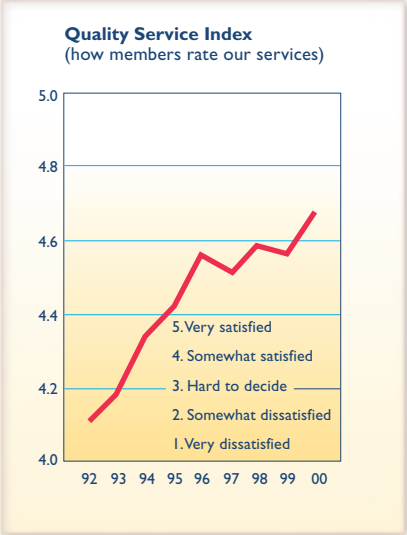
	2000	1999
Telephone calls	**94,296**	78,654
Purchase of credit	**12,541**	18,021
Pension inceptions	**7,034**	6,397
Pension estimates	**5,880**	6,331
Changes to survivor benefits	**3,358**	3,455
Termination estimates	**2,512**	2,736
Death benefits	**2,656**	2,713
Plan transfers	**2,019**	2,208
Marriage breakdown calculations	**806**	836
Commuted value payouts	**761**	612

Last year, we advised more than 2,800 teachers on their options at retirement planning workshops throughout Ontario, sent out 153,000 personalized annual benefit statements to active members, and collected $615 million in pension contributions from teachers through their employers. We paid out benefits of $2.5 billion to approximately 77,000 pensioners and members who left the plan.

HIGHEST-EVER CUSTOMER SATISFACTION

Our commitment to providing outstanding immediate and personalized service to all plan members and pensioners earned us the highest-ever customer satisfaction rating in 2000. The strongest improvements were in satisfaction with our services in providing pension inceptions, estimates, transfers, terminations and purchases of credit.

In 2001, we will replace the satisfaction survey, based on written member responses collated by staff, with an extensive random telephone survey conducted by an independent market research firm. The new approach

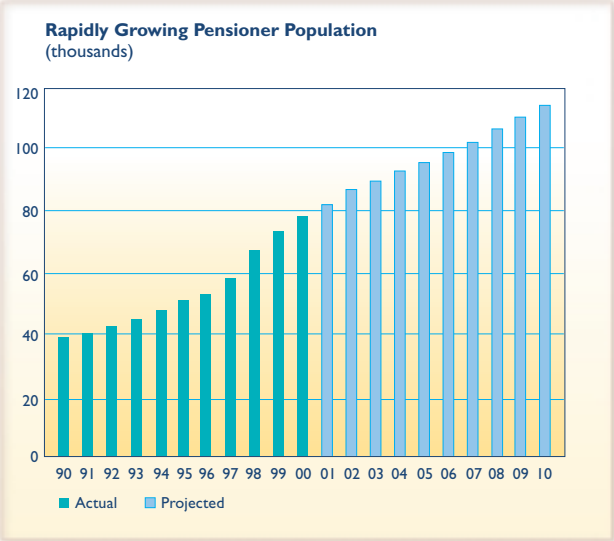


will measure a broader range of customer interactions, with the emphasis on services and service levels. This should provide a more informative evaluation of our personalized relationship with members.

EXPANDING PENSIONER POPULATION

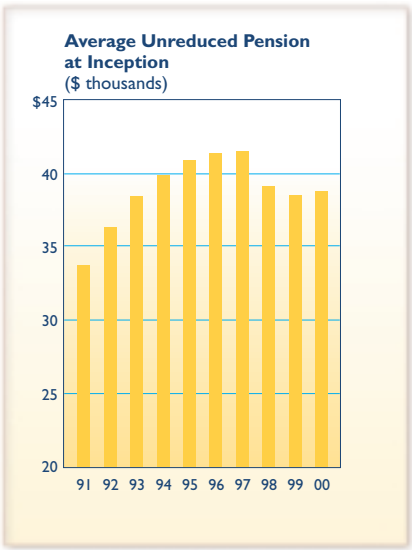
In the past three years, 21,800 teachers retired with two out of three taking advantage of the 85 factor. This increased the pensioner population to 77,000 at the end of 2000.

A large proportion of teachers is in the 45 to 55 age range and will retire in the current decade. As they consider their retirement options, these teachers will require frequent interaction with the pension board by telephone, e-mail, the Internet and one-on-one meetings.



The pension board is positioned to handle the influx of personal service needs from an expected 50,000 retirements over the current decade.

To provide better and faster customer service, we believe we have put in place some of the best technology and information management systems of any pension plan in North America. Personal service is delivered by 60 pension benefit specialists, who deal with situations ranging from members coping with the death of a spouse to requests for information on commuted value pay-outs. Staff are continuously retrained on best business practices, and we closely track our performance based on member feedback.

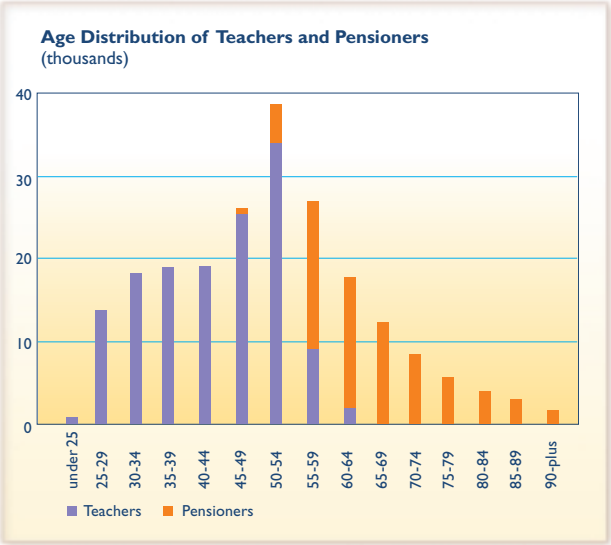


The average unreduced pension has declined from $42,000 in 1997 to $38,400 in 2000 due to early retirements under the 85 factor.

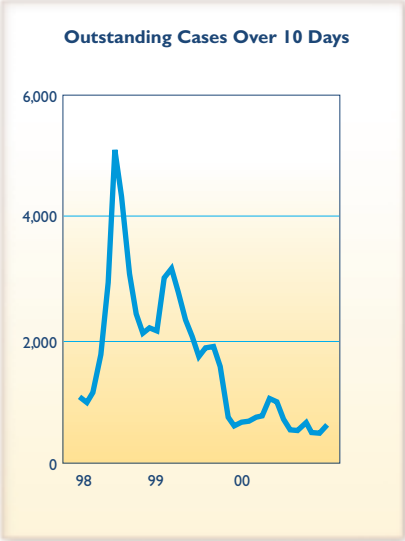
IMPROVED SERVICES

An example of how we use technology to improve service is our Computer Telephone Integration system that automatically recognizes a member's telephone number. By the time the member talks to a pension benefit specialist seconds later, the member's file is open on the specialist's computer.

The friendliness of our specialists is one reason why our customer satisfaction level is so high. Another reason for higher satisfaction is our new easier-to-read member's annual personal statement of benefits, including greater disclosure such as commuted value (the lump sum required to replace the individual's future entitlements).

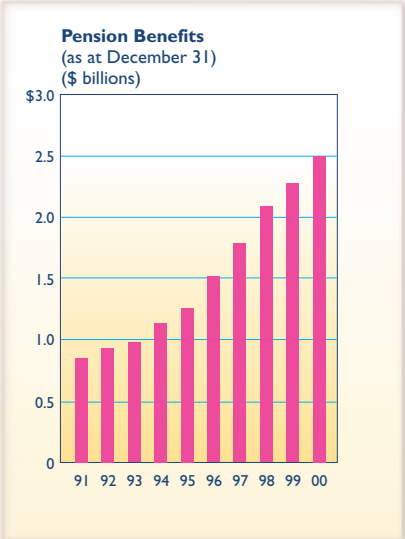


Over the past 10 years, retirees in their 50s have increased as a percentage of the pensioner population. The average pensioner age has decreased to 66.5 years.



Introduction of the 85 factor in 1998 caused a backlog in our workload. Our goal is to handle all member requests, no matter how complex, within 10 working days.

The commitment to outstanding service is evident in the time it takes to handle and complete requests from members. Outstanding requests more than 10 days old peaked at 5,000 in June 1998, following introduction of the 85 factor, and have remained well below 1,000 for most of the past year.

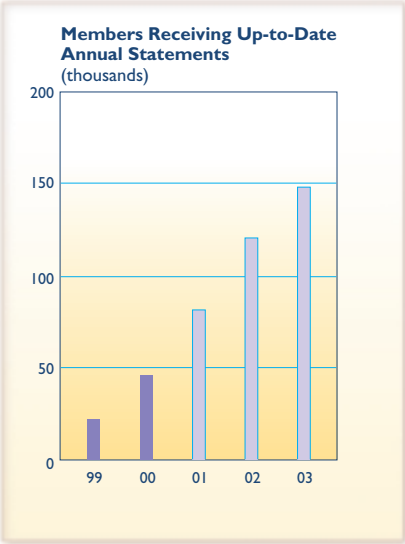


Benefits paid to retirees and their survivors continue to rise rapidly as a large number of teachers enter normal retirement or opt for early retirement.

We are also working with 218 employers to improve the quality and timeliness of member information we receive, including service credit and salary information on each active teacher.

By the end of 2000, 17 percent of employers, with more than 75,000 members, had been transferred from annual to payroll-based reporting. This also means that 75,000 members will now get annual statements that are one to two years more up to date than before.

With the continued cooperation of school boards, we expect to complete the transfer of all plan members to payroll-based reporting – and thus to up-to-date annual statements – by the end of 2003.

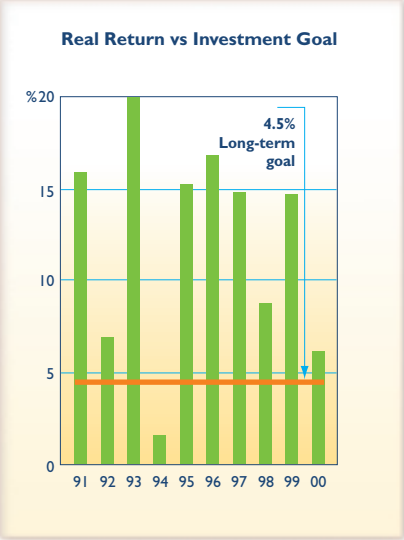


Typically, statements are only current as of August of the previous year, a situation we expect to correct for all members by the end of 2003.

The challenge of earning above-market returns

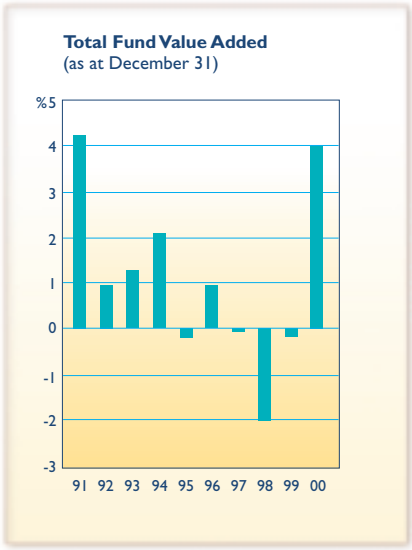
Our long-term goal is to create a surplus by growing assets faster than pension liabilities. To match average liability growth, assets must generate an annual real return of 4.5 percent (that is, 4.5 percent above the rate of inflation).

Over the long term, we believe that investing mostly in stocks will earn the level of real returns the plan needs. Consequently, our asset-mix policy has always been weighted much more to equities, a strategy that has paid off since 1990 with real returns substantially above the long-term goal. However, equity returns over the current decade could be below our target of 4.5 percent.



Because of exceptional investment markets, we exceeded the long-term investment objective in the 1990s, an achievement that will be more difficult over the next decade.

Because it will be more difficult to earn the required level of returns from passive investing alone – that is, by replicating market indices for stocks, bonds and commodities – we have reduced our index funds by shifting capital to active portfolios where we can add value. Over the past 10 years, active management and tactical asset allocation improved the returns we would otherwise have received from passive index investing by 1.1 percent.



Active management produces higher returns than the markets in which we invest can produce on their own. In 2000, this approach created $2.6 billion in value added.

INVESTMENT MANAGEMENT TEAM

We employ about 95 investment professionals, from portfolio managers, bond traders and stock analysts to foreign exchange managers, merchant bankers, and derivative traders. In addition, we employ a large staff at our wholly owned real estate subsidiary, The Cadillac Fairview Corporation Limited.

About 60 finance professionals support our investment effort. They ensure compliance with rigorous operational controls, policy guidelines and risk management limits. Every day, they settle transactions, forecast liquidity requirements, and report on investment positions, portfolio risk and returns.

Approximately 35 information technology professionals maintain and enhance our trading, risk management and reporting systems. They are developing a system that instantly routes orders from portfolio managers to various trading desks and allows for electronic execution and settlement of trades.

MAXIMIZING INVESTMENT RETURNS

To maximize returns, we actively manage 36 percent of invested assets. Even the indexed equity and fixed-income portfolios are partially actively managed through quantitative, arbitrage and other performance-enhancing strategies. We also use derivative products to manage risk and maximize returns. As a result, we are one of the largest international traders of equity-based swaps, futures and options. Many of our active strategies are independent of market direction.

We allocate a risk capital budget to each investment portfolio with the expectation of earning a minimum 10 percent return on this risk capital. The budget allocation varies among portfolios and is proportionately smaller, for example, for fixed-income securities than for merchant banking. In aggregate, the risk capital budgets are approximately 5 percent of invested assets.

We also macro-manage the total fund through "overlay" programs. For example, the asset-mix policy allows equity exposure to vary between 50 and 70 percent of net assets relative to a target of 60 percent. In 2000, we under-weighted equities and reallocated capital to fixed-income securities and real-rate bonds.

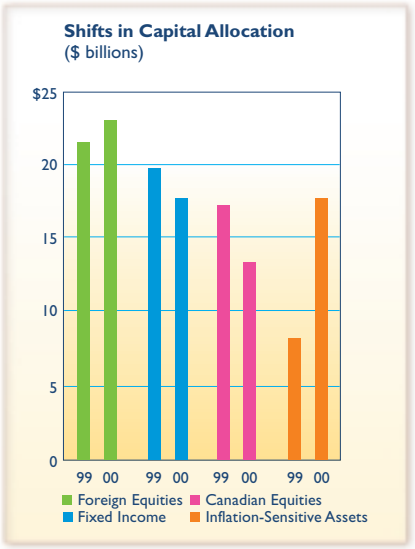
When we invest abroad, we earn a return on the investment and incur a gain or loss as a result of currency fluctuations. To reduce the volatility of returns from foreign currency fluctuations, we hedge 50 percent of investments in major foreign currencies that have a low correlation to the Canadian dollar.

Portfolio managers are rewarded for optimizing total assets and not just their own portfolios. An investment planning committee meets every two weeks to review the asset-mix policy and develop a tactical asset allocation response to current market conditions.

INDEX BANKING

We believe in being fully invested, and consider cash a drag on investment returns. Excess cash is normally invested in equity and fixed-income index funds until we identify opportunities that can earn above-market returns.

For example, to improve returns above the Canadian market benchmark, we have developed quantitative portfolios that invest in TSE 300 stocks based on models that attempt to identify strategies and stocks that should outperform the index. These portfolios have exceeded the TSE 300 returns for eight consecutive years. We account for about 4 percent of the value of trading volume in TSE 300 companies and have minimized transaction costs by trading large blocks of individual stocks or baskets of different stocks in a single transaction. Greater use of electronic trading is further reducing costs.



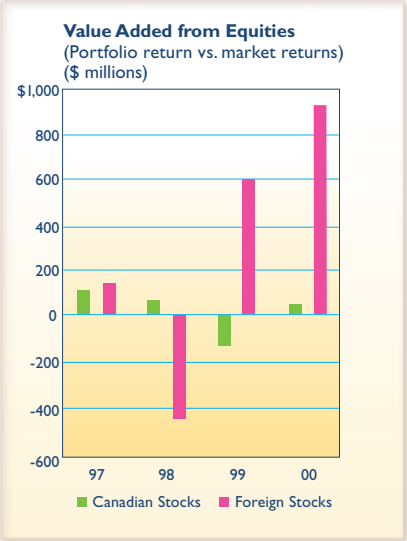
We reduced most asset classes as we transferred capital to inflation-sensitive assets such as real estate, real-rate bonds and commodities.

In the case of foreign equity index funds, our staff invest entirely in equity-based derivatives to earn market returns. Since the correlation of these investments to market performance is extremely high, these portfolios achieve market returns on a consistent basis.

ACTIVELY MANAGED EQUITY PORTFOLIOS

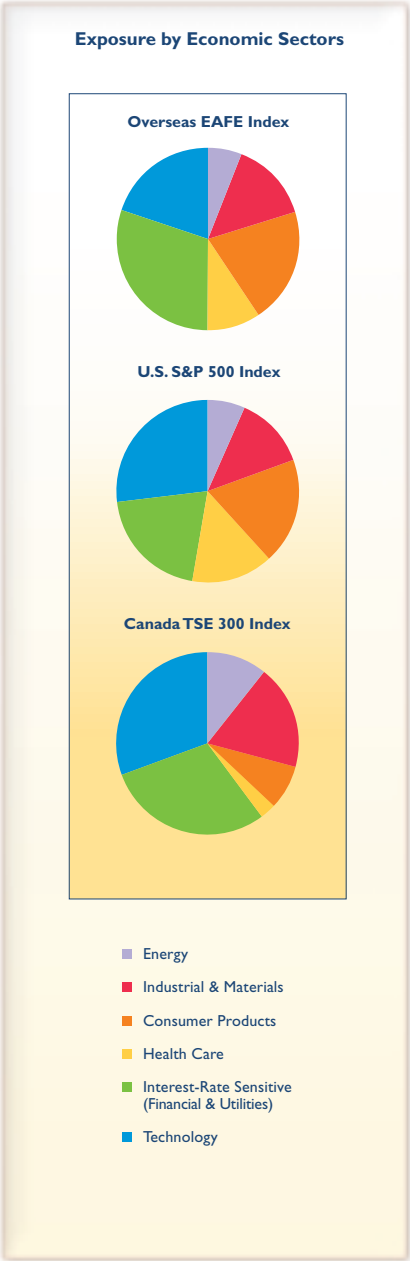
Stocks We have considerable experience as an active equity investor in Canada. In 2000, we began to expand this expertise to the global marketplace by transferring capital from foreign equity index funds to internally managed global equity programs. At the end of 2000, our staff managed more than $640 million of a total $8.3 billion in global equities.

At the same time, we remain committed to external foreign equity managers who have earned exceptional returns for the plan for many years. Building our skills in active global investing will strengthen our relationships with these managers and improve our understanding of their investment decisions.



In Canada, we have added value above equity benchmarks (indicated as zero). Outside Canada, the value-added has been more volatile and more spectacular.

Opportunities to invest in public companies in Canada are limited. The Canadian market is relatively small compared to the capital held by large institutional investors. For this and other reasons, it is important to look beyond Canada for additional investment opportunities. Focusing on global opportunities should reduce fund risks and enhance returns because global markets provide a greater diversity of economic sectors. A more global focus also allows us to select companies that are world competitors with strong performance prospects.



Greater economic diversification outside Canada offers investment opportunities that should reduce risk and improve long-term returns.

Corporate governance We attempt to improve shareholder value in public companies by voting our shares, encouraging boards of directors to practice good corporate governance, and being more involved in certain companies.

We now publish our proxy voting record on our web site **www.otpp.com**. Sharing our voting inten-

tions with management, shareholders and plan members in advance of shareholder meetings increases the transparency of our decisions and strengthens our corporate relationships with the companies in which we invest.

2000 Proxy-Voting Record

	For	Against
Employee Stock Options	46	89
Shareholder Rights Plans	1	36
Other	246	135

The most contentious issue is excessive stock options that dilute shareholders' value. In our view, the cost of options should be recorded in financial statements so that shareholders know the full financial impact of these awards.

The proxy voting record shown in the table has changed little over the past three years. We intend to be more active in working with other large investors to bring about change.

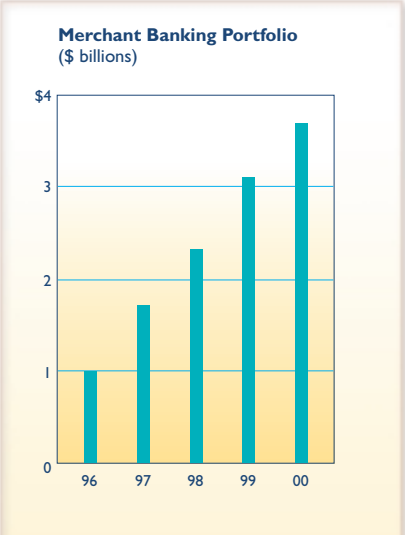
Our involvement with select companies is intended to support their boards of directors in requiring management to develop a value-added strategy with growth targets. In 2000, we made direct investments in four such companies in telecommunications, energy and industrial products. The investments are 10 to 20 percent of each firm's outstanding shares and totalled $810 million. These commitments doubled the value of our relationship investing portfolio to $1.5 billion with direct and indirect investments in eight U.S., seven Canadian and 21 U.K. companies.

Merchant banking We have developed expertise in all facets of merchant banking and ended 2000 with $3.9 billion in over 100 investments in the consumer products, communications, industrial products, entertainment & media, financial services, retail, and energy industries. We invest directly in Canadian firms, which represent 40 percent of the merchant banking portfolio. In the United States and Europe, we invest both directly and indirectly through limited partnerships.

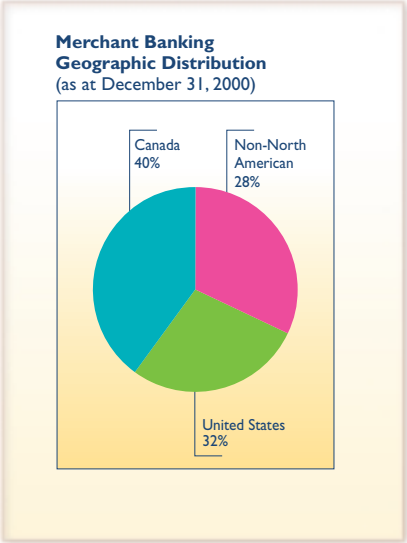
There are many opportunities to earn premium returns in the private market, where we are specialists in identifying value-added prospects. For example, we invested $14.8 million in a Canadian technology company in 1992 as part of a management buyout. In late 1993, the refinanced and refocused company was taken public. We divested our interest in stages and, by the time the last shares were sold in 2000, had realized $131 million in gains. In 2000, we sold positions in eight companies acquired for $201 million to realize net proceeds of $310 million.

Our equity and mezzanine debt investments facilitate management buyouts, business expansions, acquisitions, financial restructurings, ownership changes and taking companies private or public. In 2000, we participated with four U.S. funds in the management buyout of Shoppers Drug Mart and acquired a significant minority interest.

We first offered mezzanine debt in 1999 and had $244 million invested by the end of 2000. This product appeals to many companies as an alternative to equity and senior debt, filling the void in Canada served by the high-yield market in the U.S.



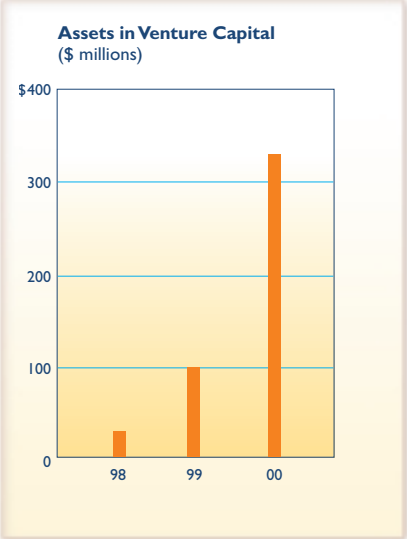
Our merchant bank has grown to be one of the largest in Canada, earning annual returns in excess of 23% since 1991.



We are increasingly adopting a global perspective in our search for premium investment returns from merchant banking.

Our merchant banking portfolio includes a venture capital fund launched three years ago that ranks among the top sources of early-stage capital in Canada. Investing in start-up enterprises carries higher risks in the expectation of higher rewards. Our size, long-term investment perspective and diverse asset base allow us to take risks in the most promising opportunities on the assumption that the successes will exceed the costs of failures.

At the end of 2000, we had $329 million invested in 24 companies and 12 venture capital funds, principally in life sciences and information technology. These investments typically involve multiple rounds of financing of $3 million to $20 million each. Approximately 54 percent of our venture capital investments are in Canada and 46 percent in the United States.

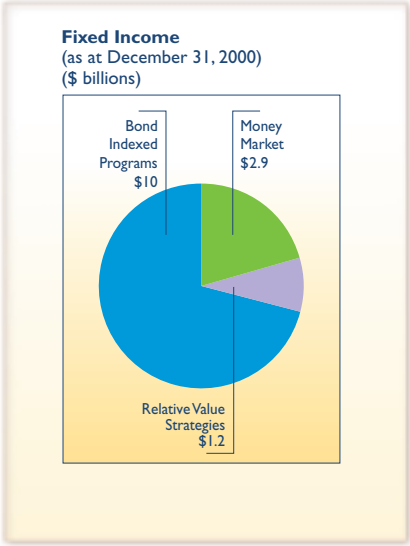


We are committed to Canadian venture capital investments where there are reasonable prospects of earning good returns for the risks involved.

FIXED-INCOME PORTFOLIOS

During the past two years, our consolidated bond portfolios have been among the top quartile of fixed-income performers.

Our basic approach is to invest the majority of fixed-income assets in bond indexed programs to replicate the Scotia Capital Canada Universe, which contains federal government bonds. Our portfolio contains substantial holdings in Government of Canada bonds, more than three percent of the Bank of Canada's domestic public debt. However, we use relative value strategies to attempt to earn returns 20 to 30 basis points above this benchmark.



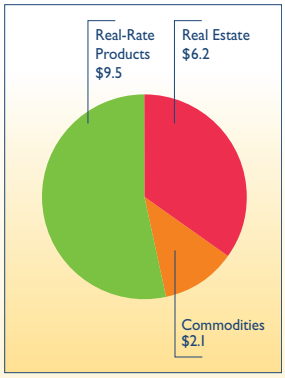
The fixed-income group manages $14.1 billion in assets.

Fixed income includes $2.9 billion allocated to the money-market portfolio and $1.2 billion in programs where we use relative value strategies to enhance returns. We have also expanded the relative value approach to include Canadian high-yield corporate securities that are well diversified by industry and economic segment. At year-end, this portfolio totalled $286 million. We are targeting the high-yield U.S. market for future expansion. We also continue to develop quantitative techniques to improve analytics, capture mispricing, and find other relative value opportunities in both bond and money markets. In this way we benefit from diversification by implementing strategies where expected returns have a low correlation to the fixed-income market overall.

INFLATION-SENSITIVE INVESTMENTS

The assets that best match the plan's liabilities have stable real returns and a high correlation with inflation. Nominal bonds are only a good fit during periods of stable inflation. Stocks have high average returns and a positive long-term correlation with inflation, but are highly volatile in the short run. Real estate, real-rate bonds and commodities are highly sensitive to inflation.

Inflation-Sensitive Investments
(as at December 31, 2000)
($ billions)



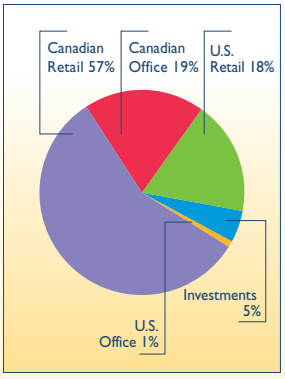
To better match inflation-indexed pensions, we are building up ownership of inflation-sensitive investments.

Since late 1998, we have managed these investments as a separate asset class. While we strive to maximize long-term real returns from these assets, their primary role is to shield the fund's surplus from the short-term risks we experienced in 2000 – a rapid rise in liabilities due to higher inflation from 2.6 to 3.2 percent and falling real interest rates from 4 to 3.4 percent.

Real estate We own a $10.4 billion real estate portfolio ($6.2 billion net of liabilities), managed by Cadillac Fairview, our wholly owned subsidiary. Approximately 95 percent of the portfolio consists of full or partial ownership of 69 shopping centres and 48 office buildings in Canada and the United States.

Our current strategy is to reposition the North American office and retail assets through a combination of redevelopment, acquisitions and dispositions with the goal of owning premier properties in key markets. This strategy is being implemented by Cadillac Fairview. We previously owned 22 percent of this company and acquired full ownership in March 2000 for $2.4 billion. As a result, we own Canada's best property portfolio and the industry's top property management company.

Real Estate Portfolio
(as at December 31, 2000)

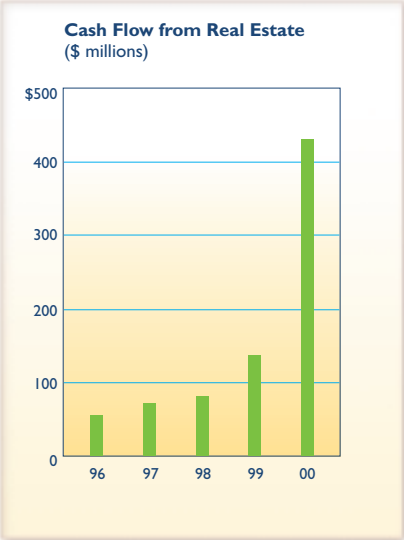


Our plan is to increase ownership of high-quality office buildings and large shopping centres in North America.

The Canadian portfolio includes premier properties, such as the Toronto Eaton Centre, Vancouver's Pacific Centre and the Toronto-Dominion Centre complex in Toronto. We recently purchased full ownership of these properties from the previous co-investor. We also strengthened our retail ownership in the Toronto area by acquiring Sherway Gardens. In the United States we own 23 shopping centres in the major markets of 10 states.

Owning Cadillac Fairview provides exclusive access to the expertise of 1,750 employees dedicated to maximizing the value of the plan's real estate assets. The Cadillac Fairview brand is internationally renowned and the company is the first call for major American and European retailers seeking a presence in the leading shopping centres. A testament to the market-draw of our shopping centres was the decision by Sears in 2000 to open five of its seven new Eatons stores in our properties.

The size and quality of our real estate portfolio provides large and predictable income. In 2000, the portfolio generated approximately $427 million in cash flow from operations.



The cash flow from real estate in 2000 was equivalent to paying close to 13,000 annual pensions.

Real-rate bonds Real-rate bonds are an excellent match against plan liabilities and, along with index-linked mortgages, are risk free with respect to inflation. As a result, we continue to be a keen buyer of these securities. In 2000, we increased our holdings of Canadian real-rate products from $4.2 billion to $5.8 billion and entered the U.S. market by acquiring $3.7 billion of U.S. Treasury Inflation-Protected Securities (TIPS). At year- end, our consolidated portfolio of real-rate securities totalled $9.5 billion.

Commodities Commodities generally have high real returns when there is unanticipated inflation and provide a hedge against short-term inflation risks in the value of the plan's liabilities. We invest through derivatives in the Goldman Sachs Commodity Index, which is heavily weighted to oil and gas, and doubled the plan's holdings to $2.1 billion in 2000.

This section of the annual report provides an overview of our operations and provides a more detailed explanation of the consolidated financial statements. It should be read in conjunction with the financial statements. Our objective is to present readers with a view of the pension board through the eyes of management by interpreting the material trends and uncertainties that affected the operating results, liquidity or financial condition of the pension plan in the last fiscal year. In addition to historical information, this section contains forward-looking statements that reflect management's objectives and expectations as at the date of this report, which involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements.

YEAR-END FINANCIAL POSITION

The plan's accrued pension liabilities increased from $52.1 billion to $58.6 billion during 2000. The actuarial assumptions used to determine these liabilities for financial statement purposes reflect management's best estimate of teachers' salaries, inflation, demographic factors, and market-based yields. These estimates at the end of 2000 were in line with the markets.

Valuation Assumptions

(as at December 31) (percent)	2000	1999
Discount rate	**6.25**	6.75
Salary escalation	**3.20**	3.25
Inflation rate	**2.20**	2.25

Both the financial statement and funding valuations now use the same assumptions.

Benefit payments In 2000, the plan paid $2.5 billion in benefits, an increase of $200 million over the previous year. The increase principally reflected 6,200 teachers retiring, bringing to 77,000 the number of retired members and their survivors receiving benefits.

Accrued Pension Benefits

($ Billions)	2000	1999
Accrued pension benefits, beginning of year	**$ 52.11**	$ 49.63
Interest on accrued pension benefits	**3.48**	3.49
Benefits earned	**1.36**	1.30
Benefits paid	**(2.54)**	(2.28)
	54.41	52.14
Changes in actuarial assumptions	**3.89**	0.77
Experience gains	**0.26**	(0.80)
Accrued pension benefits, end of year	**$ 58.56**	$ 52.11

The 2000 payments included $164 million in commuted value transfers (versus $108 million in 1999) and a 1.5 percent cost-of-living adjustment. To calculate the inflation adjustment rate, we average the annual change in inflation for 12 months ending in September each year. The inflation adjustment paid in January 2001 was 2.5 percent.

Change in net assets The plan began 2000 with $68.3 billion in net assets available for benefits. During the year, the plan gained $7.5 billion of income – $6.2 billion from investments, compared with $10.1 billion in 1999, and $1.3 billion from contributions, compared with $1.4 billion a year earlier.

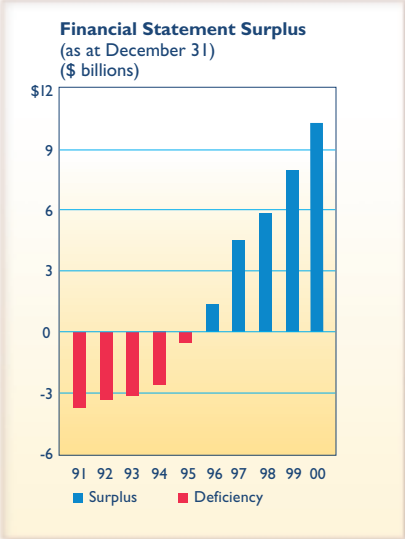
Changes in Net Assets

($ Billions)	2000	1999
Income		
Investment income	**$ 6.21**	$ 10.12
Contributions	**1.28**	1.41
	7.49	11.53
Expenditures		
Benefits	**2.54**	2.28
Operating expenses		
Member services	**0.03**	0.03
Investments	**0.10**	0.09
	2.67	2.40
Increase in net assets	**$ 4.82**	$ 9.13

Expenditures, including benefits paid to members and survivors, totalled $2.5 billion and $133 million to operate the pension board.

As a result of these changes, net assets available for benefits grew by $4.8 billion to $73.1 billion by the end of 2000.

Surplus The plan had a surplus for financial statement purposes of $10.2 billion at December 31, 2000. This compared with $7.9 billion a year earlier on a restated basis.



The year-end surplus, based on the financial statements, quantifies the plan's financial position from an accounting perspective.

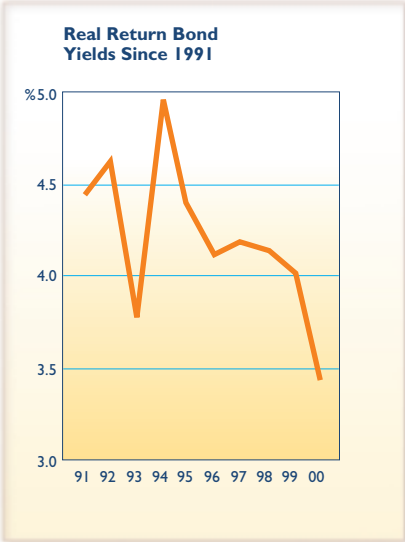
In the past, management used its best estimate of the long-term rate of return to determine the present value of all future pension benefits and assets. Net asset gains that exceed the actuarial assumptions were amortized over five years to smooth out the impact of market volatility from one year to the next.

Beginning in 2000, and as explained in note 2 to the financial statements, a market interest rate is now used to determine fair value for both fixed-income assets and accrued pension benefits. The value of equities (including real estate and commodities) continues to be adjusted for actuarial purposes to reflect the difference between the actual equity asset returns at year-end and management's best estimate of future equity returns. The difference in dollar terms (the actuarial asset value adjustment) is then amortized over five years. Strong performance by fixed-income assets increased our financial statement surplus.

MATCHING ASSETS AND LIABILITIES

To create a funding surplus we manage the relationship between investment assets and pension liabilities. Our goal is an asset mix that balances risks and rewards, avoids excessive volatility, and maintains stable contribution rates.

Because both assets and liabilities are sensitive to interest rate changes, one of our goals is to reduce the risk that liabilities will increase more than assets in response to lower real interest rates. Unfortunately,



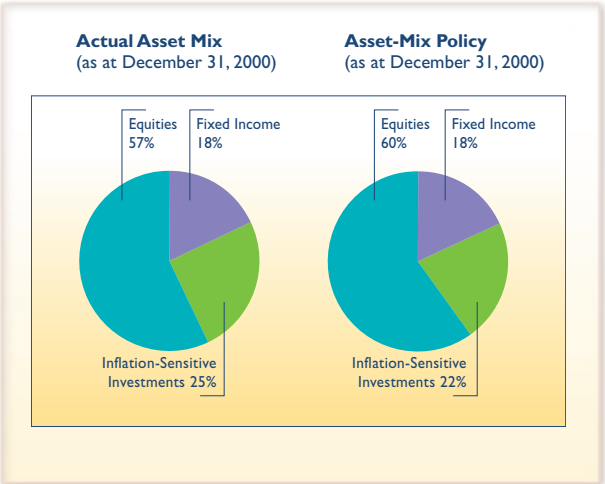
Real return yields declined by 59 basis points in 2000, after remaining within a 10 basis point range for the three previous years.

that is what happened in 2000. The sharp decline in real rates of return increased the value of total liabilities by $3 billion. During the year, we shifted assets from fixed-income and equity portfolios to real-rate products and real estate. Debt securities, along with inflation-sensitive assets, outperformed total equities to produce the healthy accounting surplus.

ASSET-MIX POLICY

The asset-mix policy is reviewed annually by management and the board of directors and changes are made as necessary to reflect changes in our asset/liability model. The asset mix is crucial to long-term performance. Studies show that approximately 90 percent of the variability of returns over time is driven by the asset-mix decision with the remaining 10 percent influenced by active management. In recent years, we have reduced our exposure to both stocks and fixed-income securities and created an asset class of inflation-sensitive assets that correlate well with the inflation-sensitive nature of our liabilities. The change in asset-mix policy also recognized that stock markets, especially in Canada, were overvalued on both a short-term and long-term basis.

Our current asset-mix policy, set in early 2000, is 60 percent equities, 22 percent inflation-sensitive assets (specifically real estate, real-rate products, and commodities), and 18 percent fixed-income securities. This asset-mix policy has a high probability of ensuring assets grow at least as fast as the liabilities over the long term. We estimate that the change in asset-mix policy contributed $600 million of value added during 2000 in addition to the $2.6 billion in benchmark outperformance.



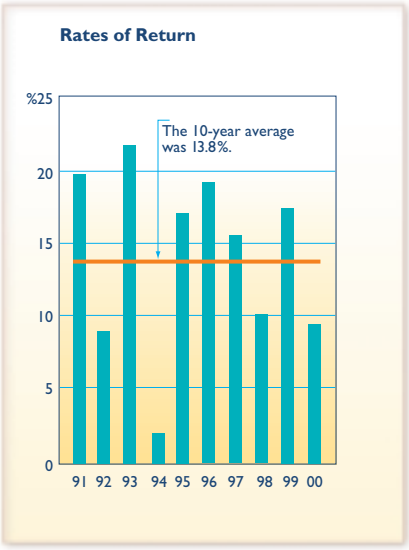
In 2000, we reduced equity investments below policy and ended the year overweight in inflation-sensitive investments compared with the new policy level.

INVESTMENT PERFORMANCE

Net investments increased to $72 billion in 2000, compared with $67.1 billion at the end of 1999.

2000 total fund performance During a year of volatile and generally negative stock markets, we achieved a 9.3 percent total fund rate of return in 2000, compared with 17.4 percent the prior year. After inflation of 3.2 percent, the real return was 6.1 percent, compared with 14.8 percent in 1999. The 2000 return generated $6.2 billion in investment income, compared with $10.1 billion a year earlier. Approximately one-third of equities are exposed to foreign markets, which had negative returns in 2000.

Four-year return We calculate average performance on a four-year cycle to produce a less volatile and more reliable measure than a single year's results. Our four-year average return was 13.0 percent, compared with 12.5 percent for the benchmark. The real rate of return (after inflation of 1.9 percent) was 11.1 percent – well in excess of the investment objective of 4.5 percent on average over the long term.



Over the current decade, returns are expected to revert to historical performance levels, which are closer to the long-term goal.

Rates of Return Compared to Benchmarks

(percent)	Investment returns	Benchmark return	Composite Benchmark
Fixed income and short-term securities	15.6	13.7	Scotia Capital Treasury Bills (91 days) Scotia Capital Canada Universe Scotia Capital Long Bond
Canadian equity	13.5	7.4	TSE 300
U.S. equity	(4.1)	(5.5)	S&P 500
Non-North American equity	(8.5)	(13.5)	Morgan Stanley EAFE, EMF National Index
Inflation-sensitive	19.9	18.0	Scotia Capital Real Return Bond Custom US Treasury Inflation-Protected Securities Goldman Sachs Commodities CPI plus 4%
Total Plan	9.3	5.3	Benchmark weighted by the policy asset mix

Ten-year return The average annual compounded rate of return for the past 10 years was 13.8 percent. The real return (after inflation of 1.9 percent) of 11.9 percent was substantially above the long-term goal.

PERFORMANCE VS. BENCHMARKS

The **total fund benchmark** aggregates the benchmark returns for each asset class, using our asset-mix policy weights. In 2000, the 9.3 percent total fund return compared with 5.3 percent for the benchmark. As a result, our portfolio managers created $2.6 billion of value above the returns that the markets in which we invested would have produced on their own. This was our largest one-year gain in value added. Included in our total fund return is our global tactical asset allocation program, which generated $519 million of value above the composite benchmark. (Performance incentives are based on the results achieved versus the benchmark, less 34 basis points for implementation and overhead costs).

Fixed income securities returned 15.6 percent, a dramatic turnaround from two percent a year earlier. These assets exceeded their benchmark of 13.7 percent to earn $229 million of value added.

Canadian equities (actively managed, enhanced index, and merchant banking) posted a 13.5 percent return versus 7.4 percent for the Canadian equity benchmark. Our enhanced quantitative index funds portfolio beat its benchmark for the eighth consecutive year to earn value added of $252 million. Our actively managed Canadian equity portfolios earned $21 million above their benchmark.

Merchant banking earned a 21.8 percent return – almost three times its benchmark to generate $427 million in value added. This $3.9 billion portfolio has contributed considerable value to total returns over the past 10 years.

Foreign equities (actively managed and enhanced index) returned a negative 4.1 percent in the U.S. and negative 8.5 percent for Non-North America (including $30 million in implementation costs) compared with negative 5.5 percent and 13.5 percent for their respective benchmarks. We increased our exposure to foreign stock markets during the year and ended 2000 with $23.1 billion in these assets. We also shifted capital from foreign equity index funds to actively managed programs. As a result, our actively managed programs produced $894 million above benchmark.

Inflation-sensitive investments of real-rate products, commodities and real estate earned 19.9 percent versus 18 percent for the composite benchmark. Real-rate bonds had a return of 17.3 percent, or $15 million better than the benchmark return. Commodities returned an exceptional 54.4 percent, though $15 million less than the benchmark due to unavoidable implementation costs. Our real estate portfolio had one of its best years, earning 13.0 percent, versus 7.2 percent for its benchmark to add $288 million in value.

RISKS AND RISK MANAGEMENT

We manage **surplus risk** using a Value at Risk (VaR) methodology. VaR has forced us to think of surplus risk as the aggregate of liability risk, asset-mix policy risk, and active management risk, taking into account correlation and diversification between the components.

The main source of **liability risk** is a drop in real interest rates, which increases the present value of future pensions accumulated up to that point. It makes new pension liabilities more difficult to finance, and puts upward pressure on contribution rates. Higher real interest rates have the opposite effect.

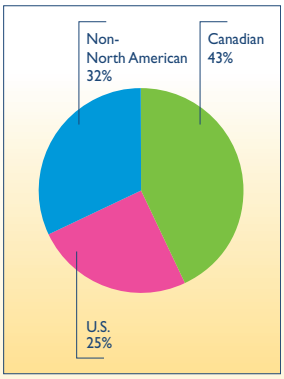
Asset-mix policy risk would be the mirror image of liability risk, and surplus risk would be zero, if investments perfectly matched the plan's long-term objective that asset growth will average a real rate of about 4.5 percent plus inflation. Real return bonds come close, but fall a bit short on yield.

The absence of a perfectly matching asset forces us to consider assets that individually do not always behave like our pension promise, but collectively give us the best trade-off between longer term expected surplus return and acceptable short-term surplus risk. Consequently, our asset mix is heavily weighted to equities because they meet our long-term goals, while our inflation-sensitive investments give more modest real returns but dampen surplus risk.

Active management risk is the potential risk of under-performing the benchmark by trying to improve on the return we get from passive implementation of asset-mix policy. The incremental surplus risk from active management is small. We control active risk through policy guidelines and procedures. Again using VaR, we assign each manager "risk capital" to go along with that manager's value added target with an expectation of a specific return on that risk capital. Risk from active positions is measured daily against the risk limits. One additional benefit from these risk measures has been an improvement in operational risk management.

Changes in the value of the Canadian dollar relative to foreign currencies can increase or decrease returns on our foreign investments, creating **foreign exchange risk**. We hedge 50 percent of our exposure to the main currencies in our asset-mix policy, and had $11.8 billion of foreign currency hedges in place at the end of 2000 to reduce volatility.

Equities
(as at December 31, 2000)



Through global diversification, we aim to reduce **excessive sensitivity to Canadian asset returns** by investing in foreign stocks and equity derivative contracts. Overall, Canada remains our primary equity market, where the plan had $17.7 billion invested in equities in 2000, followed by $10.1 billion in the United States, $2.8 billion in the United Kingdom, and $2.3 billion in Japan. However, we are concerned about the limited availability of stocks on the TSE 300. Many leading

Canadian corporations are closely owned, or listed in the U.S., further diminishing the investment pool in Canada.

With respect to **liquidity risk**, after payment of pension benefits and operating costs, the increase in net assets available for benefits totalled $4.8 billion in 2000. Cash flow came from $6.2 billion of investment income (dividends, interest income, rental income, and realized and unrealized gains) and $1.3 billion in contributions.

The cash needs for pension payments and operating expenses are predictable. On the investment side, our major liquidity risk is associated with our equity derivative contracts. A drop in foreign equity markets sustained for more than three months would require us to pay more cash to counterparties than we would otherwise expect.

We regularly assess the fund's ability to withstand the liquidity effects of a catastrophic 25 percent drop in all markets. Because the equity contracts have been profitable, we currently hold $493 million in net cash collateral from counterparties. This cash collateral, along with marketable short-term securities, annual cash flow, and other liquid assets, is more than sufficient to cover the fund's liquidity risk.

Every investment exposes us to the risk that a security issuer could default on payments or become insolvent. **Credit risk** exists with security issuers, such as governments and corporations, as well as with financial institutions and investment dealers with whom we have investment contracts. The largest credit exposure (note 3e) is to the Province of Ontario, which owes the plan $12.2 billion of non-marketable debentures valued at $15.7 billion, and $1.3 billion in contributions receivable. The next largest credit exposure is to the Government of Canada at $14.5 billion.

In the case of security issuers and derivative counterparties, we continuously monitor credit risk and, depending on the credit rating, restrict debt and equity investment in a single corporation or financial institution to between one and five percent of total fund assets.

In the case of swap counterparties, we deal primarily with 19 financial institutions rated Single A or better. Unrealized gains and losses on equity swaps are exchanged every three to six months. We exchange cash flows on interest rate swaps every six months, reducing the potential impact of a counterparty defaulting on its contractual obligations.

OUTLOOK

Our current expectation is that returns will not be as strong in the future as they have been in the past 10 years. We will continue to monitor financial markets and adjust our asset mix to achieve the best possible performance in the coming years. In the meantime, we assure all members that our first priority is to maximize returns without incurring undue risk.

Financials2000.pdf

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of the Ontario Teachers' Pension Plan have been prepared by management, which is responsible for the integrity and fairness of the data presented, including the many amounts which must, of necessity, be based on estimates and judgements. The accounting policies followed in the preparation of these consolidated financial statements conform with Canadian generally accepted accounting principles. Financial information presented throughout the annual report is consistent with the consolidated financial statements.

Systems of internal control and supporting procedures are maintained to provide assurance that transactions are authorized, assets are safeguarded and proper records maintained. These controls include quality standards in hiring and training of employees, a code of conduct, the establishment of an organizational structure that provides a well-defined division of responsibilities and accountability for performance, and the communication of policies and guidelines through the organization. Internal controls are reviewed and evaluated by internal audit programs which are subject to scrutiny by the external auditors.

Ultimate responsibility for the consolidated financial statements rests with the Board of Directors. The board is assisted in its responsibilities by the Audit and Actuarial Committee, consisting of five directors who are not officers or employees of the plan administrator. In addition, the committee reviews the recommendations of the internal and external auditors for improvements in internal control and the action of management to implement such recommendations. In carrying out its duties and responsibilities, the committee meets regularly with management and with both the external and internal auditors to review the scope and timing of their respective audits, to review their findings and to satisfy itself that their responsibilities have been properly discharged. This committee reviews the consolidated financial statements and recommends them for approval by the board.

The plan's external auditors, Deloitte & Touche LLP, have conducted an independent examination of the consolidated financial statements in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary to express the opinion in their Report to the Administrator. The external auditors have full and unrestricted access to the Audit and Actuarial Committee to discuss their audit and related findings as to the integrity of the plan's financial reporting and the adequacy of internal control systems.

CLAUDE LAMOUREUX
PRESIDENT AND CHIEF EXECUTIVE OFFICER

ANDREW JONES
VICE-PRESIDENT, FINANCE

FEBRUARY 14, 2001

AUDITORS' REPORT TO THE ADMINISTRATOR

We have audited the consolidated statement of net assets available for benefits and accrued pension benefits and surplus of the Ontario Teachers' Pension Plan as at December 31, 2000 and the consolidated statements of changes in net assets available for benefits, changes in accrued pension benefits and changes in surplus for the year then ended. These consolidated financial statements are the responsibility of the Plan's administrator. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the net assets available for benefits and accrued pension benefits and surplus of the Plan as at December 31, 2000 and the changes in its net assets available for benefits, changes in accrued pension benefits and changes in surplus for the year then ended in accordance with Canadian generally accepted accounting principles.

CHARTERED ACCOUNTANTS
TORONTO, CANADA

FEBRUARY 14, 2001

ACTUARIES' OPINION

William M. Mercer Limited was retained by the Ontario Teachers' Pension Plan Board (the "Board") to perform an actuarial valuation of the assets and the going concern liabilities of the Ontario Teachers' Pension Plan (the "Plan") as at December 31, 2000, for inclusion in the Plan's consolidated financial statements. As part of the valuation, we examined the Plan's recent experience with respect to the non-economic assumptions and presented our findings to the Board.

The valuation of the Plan's actuarial liabilities was based on:

- membership data provided by the Ontario Teachers' Pension Plan Board as at December 31, 1999;
- methods prescribed by the Canadian Institute of Chartered Accountants for pension plan financial statements;
- real and nominal interest rates on long term Canada bonds at the end of 2000;
- assumptions about future events (for example, future rates of inflation and future retirement rates) which have been communicated to us as the Board's best estimate of these events;
- information obtained from the Ontario Ministry of Labour and published reports on negotiated wage settlements in the 1999/2000 and 2000/01 school years; and
- an estimate of the salary grid increase for the 2000/01 school year based on the information above, along with input from the Partners.

The objective of the consolidated financial statements is to fairly present the financial position of the Plan on December 31, 2000 as a going concern. This is different from the statutory valuation [the actuarial valuation required by the *Teachers' Pension Act* and the *Pension Benefits Act [Ontario]*], which uses actuarial methods prescribed by the *Teachers' Pension Act* and cautious assumptions about future events to establish a prudent level for future contributions.

While the actuarial assumptions used to estimate liabilities for the Plan's consolidated financial statements represent the Board's best estimate of future events and market conditions at the end of 2000, and while in our opinion these assumptions are reasonable, the Plan's future experience will inevitably differ, perhaps significantly, from the actuarial assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations, and will affect the financial position of the Plan, and the contributions required to fund it, at that time.

We have tested the data for reasonableness and consistency, and we believe it to be sufficient and reliable for the purposes of the valuation. We also believe that the methods employed in the valuation and the assumptions are, in aggregate, appropriate for the purposes of the valuation. Our opinions have been given, and our valuation has been performed, in accordance with accepted actuarial practice.

LESTER J. WONG, F.C.I.A.

MALCOLM P. HAMILTON, F.C.I.A.

FEBRUARY 14, 2001

CONSOLIDATED STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED PENSION BENEFITS AND SURPLUS

AS AT DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
NET ASSETS AVAILABLE FOR BENEFITS		
Assets		
Investments (note 3)	**$85,117**	$73,872
Receivable from the Province of Ontario (note 4)	**1,251**	1,252
Receivable from brokers	**37**	210
Cash	**40**	42
Fixed assets	**8**	8
	86,453	75,384
Liabilities		
Investment-related liabilities (note 3a)	**13,074**	6,780
Due to brokers	**166**	230
Accounts payable and accrued liabilities	**92**	71
	13,332	7,081
Net assets available for benefits	**73,121**	68,303
Actuarial asset value adjustment (note 1e)	**(4,341)**	(8,316)
Actuarial value of net assets available for benefits	**$68,780**	$59,987
ACCRUED PENSION BENEFITS AND SURPLUS		
Accrued pension benefits (note 5)	**$58,556**	$52,105
Surplus	**10,224**	7,882
Accrued pension benefits and surplus	**$68,780**	$59,987

ON BEHALF OF THE BOARD

CHAIR

BOARD MEMBER

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999
Net assets available for benefits, beginning of year	**$68,303**	$59,171
Investment operations		
Investment income (note 7)	**6,211**	10,121
Investment expenses (note 12a)	**(100)**	(91)
Net investment operations	**6,111**	10,030
Member service operations		
Contributions (note 10)	**1,281**	1,413
Benefits (note 11)	**(2,541)**	(2,278)
Member service expenses (note 12b)	**(33)**	(33)
Net member service operations	**(1,293)**	(898)
Increase in net assets	**4,818**	9,132
Net assets available for benefits, end of year	**$73,121**	$68,303

CONSOLIDATED STATEMENT OF CHANGES IN ACCRUED PENSION BENEFITS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
Accrued pension benefits, beginning of year	**$52,105**	$49,626
Increase in accrued pension benefits		
Interest on accrued pension benefits	**3,478**	3,493
Benefits accrued	**1,359**	1,301
Changes in actuarial assumptions (note 5a)	**3,893**	766
	8,730	5,560
Decrease in accrued pension benefits		
Benefits paid (note 11)	**2,541**	2,278
Experience (losses) gains (note 5b)	**(262)**	803
	2,279	3,081
Net increase in accrued pension benefits	**6,451**	2,479
Accrued pension benefits, end of year	**$58,556**	$52,105

CONSOLIDATED STATEMENT OF CHANGES IN SURPLUS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
Surplus, beginning of year	**$7,882**	$4,381
Increase in net assets available for benefits	**4,818**	9,132
Change in actuarial asset value adjustment (note 1e)	**3,975**	(3,152)
Increase in actuarial value of net assets available for benefits	**8,793**	5,980
Net increase in accrued pension benefits	**(6,451)**	(2,479)
Surplus, end of year	**$10,224**	$7,882

FOR THE YEAR ENDED DECEMBER 31, 2000

DESCRIPTION OF PLAN

The following description of the Ontario Teachers' Pension Plan (the Plan) is a summary only. For more complete information, reference should be made to the *Teachers' Pension Act* (the TPA) as amended.

(a) General The Plan is governed by the TPA. It is a contributory defined benefit pension plan co-sponsored by the Partners who are the Province of Ontario (the Province) and Plan members, represented by the Ontario Teachers' Federation (the OTF). The terms of the Plan are set out in the *Partners' Agreement.*

The Plan is registered with the Financial Services Commission of Ontario and with the *Income Tax Act (Canada)* (registration number 0345785) as a Registered Pension Plan not subject to income taxes.

The Plan is administered and the investments are managed by the Ontario Teachers' Pension Plan Board (the Board). Under the TPA, the Board is constituted as a corporation without share capital to which the *Corporations Act (Ontario)* does not apply.

(b) Funding Plan benefits are funded by contributions and investment earnings. Contributions are made by active members of the Plan and matched by the Province and designated private schools and organizations. The determination of the value of the benefits and required contributions is made on the basis of periodic actuarial valuations (note 9).

(c) Retirement pensions A retirement pension is available based on the number of years of credited service, the average of the best five annual salaries and the age of the member at retirement. A member is eligible for a reduced retirement pension from age 55. An unreduced retirement pension is available at age 65 or at any age if the member has 35 years' credit or if the sum of a member's age and qualifying service equals 90. An early retirement window covering the period between June 1, 1998 and December 31, 2002 is currently provided, during which time a member can retire with an unreduced pension if the sum of the member's age and qualifying service equals 85 rather than 90.

(d) Disability pensions A disability pension is available at any age to a disabled member with a minimum of 10 years of credited service. The type of disability pension is determined by the extent of the disability.

(e) Death benefits Death benefits are available on the death of an active member and may be available on the death of a retired member. The benefit may take the form of a survivor pension, lump sum payment or both.

(f) Escalation of benefits Pension benefits are adjusted annually for inflation at 100 percent of the Consumer Price Index, subject to a limit of 8 percent in any one year with any excess carried forward.

(g) Retirement Compensation Arrangement The Retirement Compensation Arrangement (RCA) has been created by agreement between the Partners as a supplementary plan to provide the members of the Plan with benefits that, due to limitations imposed by the *Income Tax Act (Canada)* and its regulations, cannot be provided under the Registered Pension Plan. Because the RCA is a separate trust, the net assets available for benefits and accrued benefits of the RCA are not included in these financial statements (note 13).

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

These financial statements present the financial position and the results of operations of the Plan and are prepared in accordance with Canadian generally accepted accounting principles.

The financial statements of wholly-owned subsidiary companies are consolidated as part of the Plan's financial statements.

Certain comparative figures have been reclassified to conform with the current year's presentation.

(b) Investments and investment-related assets and liabilities

Fair Value Investments and investment-related assets and liabilities are stated at fair value. Fair value is an estimate of the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Where ascertainable, fair values are based on public market prices or quotations from investment dealers. Where public market prices or quotations are not ascertainable, fair values are derived using methods such as discounted cash flows, earnings multiples, appraisals, prevailing market rates for instruments with similar characteristics and other pricing models, as appropriate.

Trade date reporting Purchases and sales of investments and derivative contracts are recorded as of the trade date (the date upon which the substantial risks and rewards have been transferred).

Investment income Dividend income is recognized based on ex-dividend date and interest income and real estate operating income is recognized on the accrual basis as earned. Investment income also includes realized and unrealized gains and losses.

(c) Foreign currency translation

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rates prevailing on the year-end date. Income and expenses are translated into Canadian dollars at the exchange rates prevailing on the dates of the transactions. The realized and unrealized gains and losses arising from these translations are included in investment income.

(d) Accrued pension benefits

The value of accrued pension benefits and changes therein during the year are based on an actuarial valuation prepared by an independent firm of actuaries. The valuation is made as at the start of the year and then extrapolated to year-end. It uses the projected benefit method prorated on service and management's best estimate, as at valuation date, of various economic and non-economic assumptions (note 5).

(e) Actuarial asset value adjustment

The actuarial value of net assets available for benefits is determined by reference to market trends consistent with assumptions underlying the valuation of accrued pension benefits. The adjustment represents the difference between the actual and management's best estimate of return on the Plan's equity investments (including real estate and commodities) amortized over five years. Fixed income securities are valued at fair value on a basis consistent with the discount rate used to value the Plan's accrued pension benefits.

The year-over-year change in the actuarial asset value adjustment is reflected in the Consolidated Statement of Changes in Surplus.

(f) Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions that primarily affect the reported values of assets and liabilities, related income and expenses and related disclosures.

2. CHANGES IN ACCOUNTING POLICY– ACCRUED PENSION BENEFITS

Consistent with a new Canadian Institute of Chartered Accountants standard on Employee Future Benefits, the Board changed its method of determining the best estimate assumptions used in valuing the accrued pension benefits. The Board now uses a market interest rate to discount the accrued pension benefits, in order to arrive at the fair value of the Plan's liabilities. In prior years, the Board used a rate which reflected management's best estimate of the expected long-term asset rate of return.

With this change to the determination of the discount rate, the method for calculating the actuarial asset value adjustment has also been modified. In prior years, the adjustment represented the difference between the actual and management's best estimate of return on all Plan assets, amortized over five years. The actuarial asset value now values fixed income securities at fair value, consistent with the measurement of the Plan's liabilities at fair value. For the Plan's equity investments, an actuarial asset value adjustment is calculated as the difference between the actual and management's best estimate of return on the Plan's equity assets, amortized over five years.

The changes in accounting policy referred to above have been applied retroactively in the financial statements and have the following impact on 1999 figures previously reported:

($ Millions)	1999 Reported	1999 Restated
Net assets available for benefits	$68,303	$68,303
Actuarial asset value adjustment	(7,264)	(8,316)
Actuarial value of net assets available for benefits	$61,039	$59,987
Accrued pension benefits – opening	$48,636	$49,626
Changes during the year	3,469	2,479
Accrued pension benefits – closing	52,105	52,105
Surplus, beginning of year	5,747	4,381
Increase in net assets available for benefits	9,132	9,132
Change in actuarial asset value adjustment (note 1e)	(2,476)	(3,152)
Increase in actuarial value of assets available for benefits	6,656	5,980
Net increase in accrued pension benefits	(3,469)	(2,479)
Surplus, end of year	8,934	7,882
Accrued benefits and surplus	$61,039	$59,987

3. INVESTMENTS

The Plan invests directly or through derivatives in fixed income, equities and inflation-sensitive investments in accordance with its policy of asset diversification. The purpose of such diversification is to minimize the likelihood of an overall reduction in surplus and maximize the opportunity for gains across the investment portfolio.

(a) Investments[1] before allocating the effect of derivative contracts and investment-related receivables and liabilities

The schedule below summarizes the Plan's investments, including net accrued interest and dividends of $388 million (1999 – $454 million), before allocating the effect of derivative contracts and investment-related receivables and liabilities, as at December 31:

($ Millions)	2000		1999	
	Fair Value	**Cost**	Fair Value	Cost
Fixed income				
Debentures	**$15,715**	**$12,205**	$16,328	$12,991
Bonds	**13,218**	**12,696**	13,303	13,198
Money market securities	**4,273**	**4,238**	2,153	2,153
Alternative investments[2]	**2,162**	**1,720**	1,326	1,166
	35,368	**30,859**	33,110	29,508
Equities				
Publicly traded				
Canadian	**13,487**	**9,618**	17,125	11,195
United States	**1,885**	**1,565**	516	559
Non–North American	**6,415**	**5,455**	8,149	5,591
Non–Publicly traded				
Canadian	**1,110**	**856**	464	446
United States	**769**	**671**	699	510
Non–North American	**1,196**	**1,188**	984	852
	24,862	**19,353**	27,937	19,153
Inflation-sensitive investments				
Real estate (note 6)	**10,393**	**9,711**	3,508	3,220
Real rate products				
Canadian	**5,822**	**5,054**	4,656	4,349
United States	**4,424**	**4,190**	391	404
	20,639	**18,955**	8,555	7,973
	80,869	**69,167**	69,602	56,634
Investment-related receivables				
Securities purchased under agreements to resell	**1,948**	**1,946**	992	990
Derivative-related, net	**2,300**	**493**	3,278	409
Investments	**85,117**	**71,606**	73,872	58,033
Investment-related liabilities				
Securities sold under agreements to repurchase	**(3,578)**	**(3,572)**	(2,883)	(2,879)
Securities sold but not yet purchased	**(1,592)**	**(1,606)**	(973)	(992)
Real estate (note 6)	**(4,192)**	**(4,002)**	(693)	(710)
Derivative-related, net	**(3,712)**	**(1,199)**	(2,231)	(2,294)
Net investments (note 3c)	**$72,043**	**$61,227**	$67,092	$51,158

(1) For additional details, refer to the Schedule of Investments for our holdings over $50 million on page 45.

(2) Comprised of hedge funds, managed futures accounts and fund of funds programs.

(b) Derivative contracts

Derivative contracts are financial contracts, the value of which is derived from the value of underlying assets, indices, interest rates or currency rates. Derivative contracts are transacted either in the over-the-counter market or on regulated exchanges. The Plan utilizes derivatives to manage its asset mix, as well as its exposure to interest rates, foreign currencies, and credit. Derivatives are also utilized for trading purposes in a manner consistent with the Plan's investment objectives.

Notional amounts of derivative contracts serve as the basis upon which the returns from, and the fair value of, the contracts are determined.

The following schedule summarizes the Plan's derivative contracts as at December 31:

($ Millions)	**2000**		1999	
	Notional	**Fair Value**	Notional	Fair Value
Asset conversion				
Interest rate swaps	**$6,353**	**$(933)**	$ 6,091	$(763)
Equity and commodity swaps	**17,436**	**(215)**	13,719	3,257
		(1,148)		2,494
Interest rate management				
Interest rate swaps	**1,330**	**4**	1,104	1
Futures	**6,962**	**(1)**	4,238	(1)
Exchange traded options				
Purchased	**2,509**	**5**	3,041	4
Written	**2,644**	**(4)**	3,771	(4)
Over-the-counter options				
Purchased	**40**	**1**	97	3
Written	**100**	**(1)**	169	(4)
		4		(1)
Foreign currency management				
Currency swaps	**499**	**(10)**	553	10
Forwards	**13,347**	**24**	13,567	343
Futures	**708**	**1**	—	—
		15		353
Trading				
Interest rate swaps	**2,427**	**(7)**	2,836	28
Volatility swaps	**967**	**34**	66	1
Futures	**18,484**	**(17)**	13,715	(161)
Forwards	**5,899**	**175**	3,791	53
Exchange traded options				
Purchased	**454**	**14**	313	22
Written	**816**	**(5)**	441	(32)
Over-the-counter options				
Purchased	**1,964**	**38**	2,062	43
Written	**1,153**	**(22)**	1,042	(19)
		210		(65)
		(919)		2,781
Less: Net cash collateral received under derivative contracts		**(493)**		(1,734)
Net fair value of derivative contracts		**$(1,412)**		$1,047

The net fair value of derivative contracts as at December 31 on page 33 are represented by:

($ Millions)	**2000**	1999
Derivative-related receivables	**$2,562**	$4,755
Cash collateral paid under derivative contracts	**428**	324
Derivative-related liabilities	**(3,481)**	(1,974)
Cash collateral received under derivative contracts	**(921)**	(2,058)
	$(1,412)	$1,047

Securities with a fair value of $320 million (1999 – $246 million) have been deposited with various financial institutions as margin to effect derivatives transactions.

The derivative contracts on page 33 mature within one year except for the following, which have a weighted average maturity (in years) of:

	2000		1999	
	Notional *($ millions)*	**Maturity *(years)***	Notional *($ millions)*	Maturity *(years)*
Asset conversion				
Interest rate swaps	**$6,119**	**8.4**	$5,487	6.6
Equity and commodity swaps	**2,468**	**1.4**	5,155	1.6
Interest rate management				
Interest rate swaps	**1,004**	**8.2**	993	4.4
Over-the-counter options	**140**	**1.9**	—	—
Foreign currency management				
Currency swaps	**493**	**5.7**	553	7.1
Forwards	**182**	**1.5**	57	2.2
Trading				
Interest rate swaps	**2,155**	**5.1**	2,536	5.1
Volatility swaps	**221**	**3.2**	66	3.1
Over-the-counter options	**83**	**1.6**	102	2.1
Forwards	**23**	**1.4**	—	—

(c) Investment asset mix

The Plan has established a long-term asset-mix policy of approximately 60 percent equities, 18 percent fixed income and 22 percent inflation-sensitive investments.

The Plan's investments, after allocating the effect of derivative contracts and investment-related receivables and liabilities, as at December 31 are summarized below:

	2000		1999	
	Effective Net Investments at Fair Value *($ millions)*	**Asset Mix *%***	Effective Net Investments at Fair Value *($ millions)*	Asset Mix *%*
Fixed income				
Bonds	**$10,771**	**15%**	$14,926	22%
Money market and equivalents	**2,548**	**3**	2,378	4
	13,319	**18**	17,304	26
Equities				
Canadian	**17,739**	**25**	19,885	30
United States	**10,119**	**14**	8,191	12
Non–North American	**13,022**	**18**	13,568	20
	40,880	**57**	41,644	62
Inflation-sensitive investments				
Commodities	**2,098**	**3**	1,090	2
Real estate (note 6)	**6,201**	**9**	2,815	4
Real rate products	**9,545**	**13**	4,239	6
	17,844	**25**	8,144	12
Total net investments	**$72,043**	**100%**	$67,092	100%

(d) Interest rate risk

The value of the Plan's assets is affected by short-term changes in nominal interest rates and equity markets. Pension liabilities are exposed to long-term market interest rates as well as expectations for salary escalation.

The Plan's primary exposure is to a decline in the long-term real rate of return which may result in higher contribution rates required to meet pension obligations. As at December 31, 2000, holding the inflation and salary escalation assumptions constant, a 1 percent decrease in the assumed real long-term rates of return would result in an increase in the pension liabilities of approximately 13 percent (1999 – 16 percent).

After giving effect to the derivative contracts and investment-related receivables and liabilities discussed in note 3b, a 1 percent increase in nominal interest rates would result in a decline in the value of the fixed income securities of 6.6 percent (1999 – 7.7 percent).

(e) Credit risk

At December 31, 2000, the Plan's most significant concentration of credit risk is with the Government of Canada and the Province of Ontario. This concentration relates primarily to the holding of $14.5 billion of Government of Canada-issued securities and $15.7 billion of non-marketable Province of Ontario Debentures, a receivable from the Province of $1.3 billion and future provincial funding requirements of the Plan.

The Plan limits derivative contract credit risk by dealing principally with counterparties that have a credit rating of A or higher, and by utilizing an internal credit limit monitoring process, as well as through the use of credit mitigation techniques such as master netting arrangements and obtaining collateral where appropriate.

(f) Foreign currency risk

Foreign currency exposure arises from the Plan's holdings of foreign currency-denominated investments and related derivative contracts.

The Plan uses a currency overlay program to hedge a portion of its asset-mix policy allocation to U.S. and Non-North American equities. The Plan also takes trading positions in foreign currencies with the objective of adding incremental returns. The Plan's net foreign currency exposure in Canadian dollars after giving effect to the related policy hedge, as at December 31, is as follows:

($ Millions)	**2000**			1999
	Foreign Currency Exposure	**Net Foreign Currency Hedge**	**Net Foreign Currency Exposure**	Net Foreign Currency Exposure
United States Dollar	**$12,021**	**$5,389**	**$6,632**	$4,854
Euro	**5,920**	**2,528**	**3,392**	2,245
British Pound Sterling	**3,370**	**1,405**	**1,965**	1,537
Swiss Franc	**1,561**	**483**	**1,078**	252
Japanese Yen	**2,489**	**1,774**	**715**	1,280
Other	**2,165**	**187**	**1,978**	1,532
	$27,526	**$11,766**	**$15,760**	$11,700

(g) Securities lending

The Plan lends securities as a means of generating incremental income or supporting other investment strategies. As at December 31, 2000, the Plan's investments included loaned securities with a fair value of $3,402 million (1999 – $3,280 million). The fair value of collateral in respect of these loans was $3,590 million (1999 – $3,444 million).

4. RECEIVABLE FROM THE PROVINCE OF ONTARIO

The receivable from the Province consists of required matching contributions and interest thereon.

($ Millions)	**2000**	1999
Contributions receivable	**$1,194**	$1,194
Accrued interest receivable	**57**	58
	$1,251	$1,252

The receivable from the Province consists of $636 million to be received in 2001 and $615 million to be received in 2002.

5. ACCRUED PENSION BENEFITS

(a) Actuarial assumptions

The actuarial assumptions used in determining the value of accrued pension benefits of $58.6 billion (1999 – $52.1 billion), reflect management's best estimate of future economic events and involve both economic and non-economic assumptions. The non-economic assumptions include considerations such as mortality, withdrawal rates and retirement rates. The primary economic assumptions include the discount rate, salary escalation rate and the inflation rate. As discussed in note 2, the discount rate is now set at the market rate, as at the valuation date, of debt obligations with characteristics similar to the Plan's liabilities. The inflation rate is the difference between the yield on federal long-term nominal bonds and federal real return bonds. The salary escalation rate incorporates the inflation rate assumption and long-term expectation of growth in real wages. A summary of the primary economic assumptions, as at December 31, is as follows:

	2000	1999
Discount rate	**6.25%**	6.75%
Salary escalation rate	**3.20%**	3.25%
Inflation rate	**2.20%**	2.25%

The main economic assumptions were changed as a result of changes in capital markets during 2000. These changes resulted in a net increase in the value of accrued pension benefits of $3,297 million. In addition, a change was made to the assumed post-retirement mortality rates to better reflect the Plan's experience. This change increased the value of accrued pension benefits by a further $596 million. In 1999, changes to the actuarial assumptions resulted in a net increase in the value of accrued pension benefits of $766 million.

(b) Experience gains and losses

An experience loss of $262 million (1999 – gain of $803 million), arising from differences between the actuarial method and assumptions and actual results, relates primarily to current experience for members' salary and inflation rates.

6. INVESTMENT IN REAL ESTATE

(a) Acquisition of Cadillac Fairview Corporation ("CFC")

On March 17, 2000, pursuant to a plan of arrangement, the Plan acquired the remaining 78.2 percent of the common shares that it did not previously own of CFC, a fully integrated commercial real estate operating company, and $100 million of CFC convertible debentures for total consideration of $2,355 million.

The fair value of CFC's net assets acquired is summarized below:

($ Millions)	
Real estate properties	$5,730
Other assets	403
	6,133
Debt on real estate properties	(2,892)
Other liabilities	(324)
Net assets of CFC	2,917
Less: Investment in CFC previously held	(562)
Total consideration	**$2,355**

(b) Investment in Real Estate

The Plan's investment in real estate, which is comprised of real estate–related investments that are either owned or managed on behalf of the Plan by The Cadillac Fairview Corporation Limited, as at December 31, is as follows:

($ Millions)	**2000**		1999	
	Fair Value	**Cost**	Fair Value	Cost
Assets				
Real estate properties	**$9,635**	**$8,901**	$2,454	$2,411
Investments	**526**	**577**	485	498
Other assets	**232**	**233**	7	7
Investment in CFC	**—**	**—**	562	304
Total assets	**10,393**	**9,711**	3,508	3,220
Liabilities				
Debt on real estate properties	**3,833**	**3,694**	693	710
Other liabilities	**359**	**308**	—	—
Total liabilities	**4,192**	**4,002**	693	710
Net investment in real estate	**$6,201**	**$5,709**	$2,815	$2,510

(c) Real Estate Income[1]

The Plan's real estate income for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Revenue		
Rental	**$1,140**	$263
Investment	**41**	24
	1,181	287
Expenses		
Property operating	**447**	101
Interest	**242**	41
Management	**42**	7
Other	**23**	—
	754	149
Operating income	**427**	138
Realized gain (loss)	**14**	(16)
Unrealized gain	**187**	190
Net income	**$628**	$312

(1) Operating income, on a fair value basis, excludes a charge for depreciation and amortization.

7. INVESTMENT INCOME

(a) Investment income, before allocating the effect of derivative contracts

Investment income, before allocating the effect of derivative contracts and before allocating the realized and unrealized net gains/losses, for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Fixed income interest		
Debentures (net of interest incurred on swap contracts of $1,039 million; 1999 – $753 million)	**$386**	$762
Money market securities	**197**	104
Bonds	**720**	633
	1,303	1,499
Equity dividend income		
Canadian equity	**222**	271
United States equity	**13**	13
Non–North American equity	**234**	241
	469	525
Inflation-sensitive investments		
Real estate operating income (note 6c)	**427**	138
Real rate products interest income		
Canadian	**189**	152
United States	**92**	14
	708	304
	2,480	2,328
Net gain on investments [1]	**3,731**	7,793
	$6,211	$10,121

(1) Includes net unrealized gains (losses) of $(4,145) million (1999 – $1,075 million).

(b) Investment income

Investment income by asset class, after allocating the effect of the derivative contracts and net gains, including foreign currency losses of $71 million (1999 – $1,106 million gain), for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Fixed income	**$1,689**	$(347)
Canadian equity	**2,523**	4,475
United States equity	**316**	1,559
Non–North American equity	**(694)**	3,697
Inflation-sensitive investments	**2,377**	737
	$6,211	$10,121

8. INVESTMENT RETURNS AND RELATED BENCHMARK RETURNS

Investment returns and related benchmark returns by investment asset class for the year ended December 31 are as follows:

	2000		1999	
	Investment Returns	**Investment Benchmark Returns**	Investment Returns	Investment Benchmark Returns
Fixed income	**15.6%**	**13.7%**	2.0%	2.8%
Canadian equity	**13.5**	**7.4**	30.4	32.0
United States equity	**(4.1)**	**(5.5)**	12.7	14.1
Non–North American equity	**(8.5)**	**(13.5)**	27.7	21.6
Inflation-sensitive investments	**19.9**	**18.0**	12.0	9.8
Total Plan	**9.3%**	**5.3%**	17.4%	17.6%

Investment returns have been calculated in accordance with the acceptable methods set forth by the Association for Investment Management and Research and the Pension Investment Association of Canada.

The Plan identifies benchmarks to evaluate the performance of the investment management process. The performance of each asset class is measured against a benchmark that simulates the results of the markets in which the managers invest, except that the inflation-sensitive investments composite benchmark includes real estate which is measured against an inflation-related benchmark.

The total return of the Plan is measured against a Canadian dollar denominated composite benchmark produced by aggregating Canadian dollar equivalent returns from each of the policy asset class benchmarks, using the Plan's asset mix policy weights. The total return incorporates the Plan's tactical asset allocation decisions.

9. FUNDING POLICY

Statutory actuarial valuations are prepared periodically in accordance with the *Teachers' Pension Act* to determine the funding requirements of the Plan. Active members are currently required to contribute 7.3 percent of the portion of their salaries covered by the Canada Pension Plan and 8.9 percent of salaries above this level. Aggregate member contributions are matched by the Province and other employers.

The actuarial assumptions and methods used to determine statutory pension liabilities are different than those used to calculate the amounts disclosed in these financial statements. The statutory valuations use a more conservative approach than the valuations used in these financial statements (note 5) and also take into account benefits to be earned and contributions to be made after the valuation date.

The initial statutory valuation of the Plan, prepared by William M. Mercer Limited as at January 1, 1990 disclosed an unfunded liability of $7.8 billion which was the amount by which the Plan's liabilities exceeded its assets. This liability was the responsibility of the Province and was to be paid off with interest by a series of special payments over a 40 year period, which began January 1, 1990. Subsequent statutory valuations have treated the present value of the remaining special payments as an asset.

The statutory valuation as at January 1, 1998 disclosed the present value of special payments to be $8.45 billion, with an actuarial gain of $6.78 billion. Pursuant to the *Partners' Agreement* between the Ontario Teachers' Federation (OTF) and the Province, the Partners entered into negotiations to decide how to utilize the gain. Pursuant to the agreement reached on April 18, 1998, the Partners agreed to share the 1998 actuarial gain of $6.78 billion and future gains in the following sequence:

(i) $2.24 billion would be spent on improving benefits;
(ii) special payments on the pre-1990 unfunded liability would be eliminated at an estimated cost of $8.45 billion; and
(iii) a further $8.45 billion less the $2.24 billion would be spent on improved benefits or member contribution rate reductions, subject to the Province's consent prior to April 1, 2001; or held in a contingency reserve as determined by the OTF.

As a result, $2.24 billion of the gain was used to improve benefits under the Plan, and the remaining $4.54 billion of the gain was used to eliminate the obligation of the Province to make special payments after November 30, 2008. These changes consumed the actuarial gain. The present value of the remaining special payments after application of gains was $3.91 billion as at January 1, 1998.

The statutory valuation as at January 1, 1999 disclosed the present value of the remaining special payments to be $3.65 billion with an actuarial gain of $3.52 billion. Pursuant to the 1998 agreement noted above, all of this gain was used to eliminate the obligation of the Province to make special payments after April 1999.

The statutory valuation as at January 1, 2001 disclosed an actuarial gain of $6.78 billion (2000 – $4.54 billion).

10. CONTRIBUTIONS

($ Millions)	**2000**	1999
Members		
Current service	**$604**	$612
Optional credit	**11**	8
	615	620
Province of Ontario		
Current service	**601**	592
Interest	**42**	43
Optional credit	**5**	11
Special payments (note 9)	**—**	128
	648	774
Other employers	**9**	9
Transfer from other pension plans	**9**	10
	18	19
	$1,281	$1,413

11. BENEFITS

($ Millions)	**2000**	1999
Retirement pensions	**$2,215**	$2,016
Disability pensions	**31**	30
Death benefits	**102**	93
Refunds	**18**	16
Commuted value transfers	**164**	108
Transfers to other plans	**11**	15
	$2,541	$2,278

12. ADMINISTRATIVE EXPENSES

(a) Investment expenses

($ Millions)	**2000**	1999
Salaries and benefits	**$40.5**	$31.8
External investment management fees	**34.3**	34.8
Custodial fees	**6.6**	6.4
Premises and equipment	**6.6**	6.5
Professional consulting services	**5.0**	4.3
Information services	**3.7**	3.6
Communication and travel	**2.1**	1.8
Statutory audit fees	**0.3**	0.3
Other	**1.0**	1.1
	$100.1	**$90.6**

(b) Member service expenses

($ Millions)	**2000**	1999
Salaries and benefits	**$20.9**	$21.2
Premises and equipment	**6.2**	6.1
Professional and consulting services	**2.4**	2.2
Communication and travel	**2.1**	1.9
Board and committee remuneration	**0.2**	0.2
Statutory audit fees	**0.2**	0.2
Other	**0.7**	0.8
	$32.7	$32.6

(c) Executive compensation

The compensation table represents full disclosure of base salary, annual bonus, long-term incentives and other compensation earned in 1998, 1999 and 2000 by the Chief Executive Officer and the four other most highly compensated executives.

Name and Principal Position	Year	Base Salary	Annual Bonus[1]	Long-term Incentive Plan[3]	Group Term Life Insurance	Other Compensation
Claude Lamoureux	2000	$389,169	$504,500	$790,100	$1,119	$9,600[4]
President & CEO	1999	357,637	196,100	131,900	1,033	9,600
	1998	349,077	177,600	0	964	9,600
Robert Bertram	2000	$302,800	$404,000	$627,000	$ 870	$13,962[5]
Executive V.P. Investments	1999	276,309	102,600	101,800	798	13,343
	1998	269,053	63,200	0	777	13,209
Neil Petroff	2000	$196,130	$338,500	$451,900	$ 561	$ 0
Sr. V.P. International Equity Indexes, Fixed Income & Foreign Exchange	1999	175,444	202,800	51,400	507	0
	1998	170,606	124,700	0	490	0
Morgan McCague	2000	$186,384	$323,800	$460,000	$ 533	$ 0[6]
Sr. V.P. Quantitative Investments	1999	164,863	188,000	53,200	476	3,218
	1998	155,037	162,900	0	448	3,009
Allan Reesor	2000	$237,976	$319,200[2]	$280,100	$ 682	$ 4,808[6]
Executive V.P., Member Services and C.I.O.	1999	195,619	100,900	40,797	564	3,792
	1998	188,736	94,400	59,600	545	3,654

[1] Bonuses for investment professionals are based on a combination of total fund, asset class, and individual performance, measured in dollars of value added. Performance versus benchmark is measured over four annual performance periods.

Bonuses for other executive staff are based on achievement of annual corporate and divisional objectives.

[2] Includes deferred annual incentive for 1999.

[3] The investment long-term incentive program was restructured in 1999 following a review of competitive market practices. The new program continues to be based on four-year performance periods. Initial grants are adjusted by the four-year total fund rate of return and by a performance modifier, based on total fund dollar value-added over a composite benchmark.

[4] Automobile allowance.

[5] Includes an automobile allowance of $8,000 per annum plus unused vacation cashout.

[6] Unused vacation cashout.

13. RETIREMENT COMPENSATION ARRANGEMENT

The Retirement Compensation Arrangement (RCA) is established pursuant to an agreement between the Province of Ontario and the Ontario Teachers' Federation (the Partners), to provide to the members of the Plan certain benefits that would have been provided under the Registered Pension Plan, but for amendments made to the *Income Tax Act (Canada)* and its Regulations that restrict benefits that may be provided under a registered plan for periods of service after 1991 and for certain periods before 1992 that are credited after 1991.

The RCA is administered under a trust separate from the assets of the Registered Pension Plan. The Board has been appointed by the Partners to act as the trustee of the RCA.

Because the RCA is a separate trust, the net assets available for benefits and the value of accrued benefits and deficiency, referred to below, have not been included in the accompanying financial statements of the Registered Pension Plan on pages 26 to 28.

The RCA is funded on a pay-as-you-go basis from a portion of the contributions made to the Board by teachers, the Province of Ontario and designated private schools and organizations. The portion is based on a rate determined periodically by the Board's independent actuary in a manner that is expected to be sufficient to pay the benefits over the next 12 months. Due to the funding policy adopted by the Partners, the assets will continue to be substantially less than the liabilities.

In addition, since it is difficult to predict the benefits expected to be paid over the next 12 months, it is possible that the assets may be insufficient to pay the benefits. In such a case, the payment of benefits will be temporarily suspended and the contributions raised in order to fund the payments that are due under the RCA.

A summary of the balance sheet for the RCA as at December 31 is as follows:

($ Thousands)	**2000**	1999
Net assets available for benefits		
Assets	**$2,200**	$1,799
Liabilities	**(408)**	(655)
	$1,792	$1,144
Accrued benefits and deficiency		
Accrued benefits	**$305,900**	$238,768
Deficiency	**(304,108)**	(237,624)
	$1,792	$1,144

The actuarial assumptions used in determining the value of accrued benefits are consistent with the assumptions used in the Plan except that the assumed discount rate has been adjusted to reflect the impact of the 50 percent refundable tax under the RCA.

The estimate of the value of accrued benefits is highly sensitive to salary increases, both actual and assumed. Any changes to the salary assumptions will have a significant impact on the liabilities for future benefits. In addition, significant uncertainty exists in projecting the liabilities of the RCA due to changes in the number of future participants as well as changes to the income tax regulations relating to pensions.

14. COMMITMENTS

The Plan has committed to enter into investment transactions, which will be funded over the next several years in accordance with the terms and conditions agreed to. As at December 31, 2000, these commitments totalled $2,824 million (1999 – $1,634 million).

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

FIXED INCOME

($ Millions)

Type	Year of Maturity	Coupon (%)	Fair Value	Cost
Government of Canada bonds	2001–2029	4.50–13.00	$9,516	$9,467
Canadian corporate bonds	2001–2049	0.00–16.00	1,988	1,997
Canadian treasury bills	2001–2002	5.41–5.97	1,839	1,819
Commercial paper	2001	5.71–5.93	549	548
International corporate bonds	2003–2012	5.74–10.00	317	305
Provincial bonds	2002–2016	5.50–9.75	267	270
Foreign denominated Canadian bonds	2001–2085	4.40–13.00	213	220
Term deposits	2001	5.50–5.70	133	133
Discount instruments	2001	5.47–5.80	113	111
Securities purchased under agreements to resell	2001	2.00–6.30	1,948	1,946
Securities sold under agreements to repurchase	2001	5.75–6.45	(3,578)	(3,572)

PROVINCE OF ONTARIO DEBENTURES

($ Millions)

Maturity Date	Coupon (%)	Fair Value	Cost
2001 to 2006	9.00–15.00	$6,186	$5,170
2007 to 2012	10.00–16.00	9,155	6,661
Total debentures net of accrued interest		15,341	11,831
Accrued interest		374	374
Total		$15,715	$12,205

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

CORPORATE SHARES

(Millions)

Security Name	Shares	Fair Value $
Nortel Networks Corporation	37.8	1,823.9
Nexen Inc.	21.4	791.4
Royal Bank of Canada	9.4	476.7
Toronto-Dominion Bank, The	8.4	366.4
Encal Energy Ltd.	31.1	331.6
Bank of Montreal	4.2	328.4
BCE Inc.	7.6	328.1
Bank of Nova Scotia, The	7.5	326.1
Manulife Financial Corporation	6.8	317.8
AT&T Canada Inc.	6.9	299.7
Maple Leaf Foods Inc.	37.9	299.2
Enron Corp.	2.2	279.1
Canadian Imperial Bank of Commerce	5.7	263.3
Sun Life Financial Services of Canada Inc.	6.2	248.7
Alcan Aluminium Limited	4.7	242.4
Canadian Pacific Limited	5.5	234.5
Petro-Canada	5.1	194.1
WestJet Airlines Ltd.	8.3	192.8
Alberta Energy Company Ltd.	2.6	184.9
Celestica Inc.	2.2	177.3
Talisman Energy Inc.	2.8	155.6
Bombardier Inc.	6.3	146.7
Barrick Gold Corporation	5.9	145.3
Thomson Corporation, The	2.5	144.8
Suncor Energy Inc.	3.6	136.1
Gulf Canada Resources Limited	17.8	135.9
Canadian National Railway Company	3.1	135.5
TELUS Corporation	2.9	117.9
TransCanada PipeLines Limited	6.6	112.9
HSBC Holdings	5.0	110.2
Total Fina SA	0.6	109.3
Ballard Power Systems Inc.	1.1	103.3
Canadian Natural Resources Limited	2.4	101.6
Enbridge Inc.	2.3	101.2
Shaw Communications Inc.	2.9	99.0
Potash Corporation of Saskatchewan Inc.	0.8	97.1
Abitibi-Consolidated Inc.	7.0	95.9
ENI SpA	9.7	93.2
United Dominion Industries Limited	5.1	91.0
Imperial Oil Limited	2.3	89.6
Power Corporation of Canada	2.4	89.1
Akzo Nobel NV	1.1	86.7
Inco Limited	3.2	86.4
ING Groep NV	0.7	86.4
Research In Motion Limited	0.7	85.5
BAE Systems PLC	9.9	84.8
NewPower Holdings, Inc. (Warrants)	5.7	83.2

CORPORATE SHARES

(Millions)

Security Name	Shares	Fair Value $
XTRA Corporation	1.1	81.7
Veba AG	0.9	80.8
Placer Dome Inc.	5.5	79.2
Clarica Life Insurance Company	1.9	78.4
C-MAC Industries Inc.	1.2	77.4
Anderson Exploration Ltd.	2.3	77.4
BioChem Pharma Inc.	1.6	76.7
Hitachi Ltd.	5.6	75.2
Kirby Corporation	2.3	73.6
Bayer AG	0.9	73.5
Telefonos de Mexico SA	1.1	73.3
Westcoast Energy Inc.	2.0	73.2
Magna International Inc.	1.2	72.6
Loblaw Companies Limited	1.4	70.4
Seagram Company Ltd., The	0.9	70.3
Zurich Financial Services Group, The	0.1	69.8
National Bank of Canada	2.6	69.5
Power Financial Corporation	2.0	69.1
Telecom Italia SpA	5.8	68.4
Matsushita Electric Works, Ltd.	1.9	67.6
Telefonica, SA	1.5	65.5
NOVA Chemicals Corporation	2.3	65.0
Shell Transport & Trading Company	5.1	63.3
Novartis AG	0.02	61.9
Portugal Telecom SA	4.5	61.5
Unilever PLC	4.8	61.4
Aventis SA	0.5	59.4
TransAlta Corporation	2.7	59.3
Lindsay Manufacturing Co.	1.7	58.9
Nokia OYJ	0.9	58.1
Mackenzie Financial Corporation	2.1	57.3
George Weston Limited	0.7	56.2
Daiichi Pharmaceutical Co., Ltd.	1.2	55.7
Rogers Communications Inc.	2.2	55.2
Deutsche Bank AG	0.4	54.6
Australia & New Zealand Banking Group Limited	4.5	54.1
Trizec Hahn Corporation	2.3	53.4
Allied Irish Banks plc	3.1	53.3
Jardine Strategic Holdings PLC	12.2	53.2
Wolters Kluwer	1.3	52.4
Cheung Kong (Holding) Ltd.	2.7	52.3
Quebecor World Inc.	1.4	51.3
Shell Canada Limited	1.3	50.4
Royal Bank of Scotland Group	1.4	50.1
Alcatel	0.6	50.1

Note: For a complete list of companies, please see our website at **www.otpp.com.**

CONVERTIBLE AND EXCHANGEABLE DEBENTURES

(Millions)

Security Name	Par Value ($)	Fair Value ($)
Power Financial Corporation 8.0% Due April 30, 2014	85.5	529.8
PDFB Investments Inc. 3.25% Due March 12, 2018	89.1	254.6

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

REAL ESTATE PORTFOLIO

Property	Total Square Footage	Effective % Ownership
	(in thousands)	
Canadian Regional Shopping Centres		
Cataraqui Town Centre, Kingston	580	50%
Champlain Place, Dieppe	729	100%
Chinook Centre, Calgary	1,056	100%
Don Mills Shopping Centre, Toronto	420	100%
Eastgate Square, Hamilton	578	100%
Erin Mills Town Centre, Mississauga	759	50%
Fairview Mall, Toronto	883	50%
Fairview Park Mall, Kitchener	746	100%
Fairview Pointe Claire, Montreal	1,044	50%
Georgian Mall, Barrie	533	100%
Hillcrest Mall, Richmond Hill	558	100%
Intercity Shopping Centre, Thunder Bay	455	100%
Le Carrefour Laval, Montreal	1,183	100%
Les Galeries D'Anjou, Montreal	1,011	50%
Les Promenades St. Bruno, Montreal	1,036	100%
Lime Ridge Mall, Hamilton	827	100%
Market Mall, Calgary	754	50%
Markville Shopping Centre, Markham	954	100%
Masonville Place, London	684	100%
McAllister Place, St. John	471	100%
Midtown Plaza/Village, Saskatoon	687	100%
New Sudbury Centre, Sudbury	496	100%
Pacific Centre, Vancouver	1,348	50%*
Polo Park Mall, Winnipeg	1,197	100%
Regent Mall, Fredericton	446	100%
Richmond Centre, Vancouver	488	100%
Rideau Centre, Ottawa	692	31%
Sherway Gardens, Toronto	979	100%
Southland Mall, Regina	423	100%
The Promenade, Toronto	693	50%
Toronto Eaton Centre, Toronto	1,559	100%
Victoria Eaton Centre, Victoria	406	100%
Woodbine Centre, Toronto	682	60%

Property	Total Square Footage	Effective % Ownership
	(in thousands)	
Canadian Office Properties		
1 Queen Street East and 20 Richmond Street East, Toronto	503	50%
Granville Square, Vancouver	398	100%
Pacific Centre Office Complex, Vancouver	1,537	50%*
Shell Centre, Calgary	681	50%
Toronto Dominion Centre Office Complex, Toronto	4,437	50%*
Toronto Eaton Centre Office Complex, Toronto	1,899	100%
Waterfront Centre, Vancouver	395	100%
Yonge Corporate Centre, Toronto	661	50%
US Regional Shopping Centers		
Broward Mall, Fort Lauderdale, Florida	1,000	100%
Dover Mall, Dover, Delaware	834	100%
Galleria at White Plains, White Plains, New York	885	100%
Golden East Crossing, Rocky Mount, North Carolina	584	100%
Gwinnett Place, Duluth, Georgia	1,249	33%
Kitsap Mall, Silverdale, Washington	715	49%
Lakewood Center, Lakewood, California	2,044	49%
Los Cerritos Center, Cerritos, California	1,302	49%
Northpark Mall, Ridgeland, Mississippi	958	100%
Redmond Town Center, Redmond, Washington	1,119	49%
Stonewood Mall, Downey, California	929	49%
The Esplanade, Kenner, Louisiana	911	100%
Town Centre at Cobb, Kennesaw, Georgia	1,273	33%
Washington Square, Tigard, Oregon	1,239	49%

* Ownership increased to 100% subsequent to year end

PRIVATE COMPANIES AND PARTNERSHIPS

Absolute Return Fund Ltd.
Apaquogue Limited
ARC Canadian Energy Venture Fund
BC European Capital V
BC European Capital VI
BC European Capital VII
CACF Limited
DLJ Merchant Banking Partners II, L.P.
Exxel Capital Partners V, L.P.
Friedrich Grohe AG
Hicks, Muse, Tate & Furst Latin America Fund, L.P.
Magnatrax Corp.
Maple Leaf Sports & Entertainment
Maple Partners Financial Group
Morgan Stanley Real Estate Fund III International L.P.
Newcastle Capital Management Inc.
Providence Equity Partners Fund II, L.P.
Providence Equity Partners Fund III, L.P.
Schroder Asian Properties L.P.
Shoppers Drug Mart Inc.
The Macerich Company
The Third Hermes UK Focus Fund
Trimac Corporation

ELEVEN-YEAR REVIEW

FOR THE YEAR ENDED DECEMBER 31

($ Millions)	**2000**	1999	1998	1997	1996	1995	1994	1993	1992	1991	1990
CHANGE IN NET ASSETS											
Income											
Investment income	**6,211**	10,121	5,137	7,246	7,436	5,656	528	5,907	2,145	3,843	1,031
Contributions											
Members/transfers	**624**	630	612	591	620	636	732	689	711	651	559
Province of Ontario	**657**	655	653	649	673	669	704	712	740	663	587
– special payments	**—**	128	492	456	152	—	—	—	438	270	187
Total Income	**7,492**	11,534	6,894	8,942	8,881	6,961	1,964	7,308	4,034	5,427	2,364
Expenditures											
Benefits paid	**2,541**	2,278	2,103	1,802	1,520	1,261	1,130	1,001	921	829	760
Investment expenses	**100**	91	67	59	40	30	25	20	14	7	1
Member service expenses	**33**	33	32	31	29	27	26	24	23	18	19
Distribution of gain	**—**	—	—	—	—	—	—	325	—	—	—
Total Expenditures	**2,674**	2,402	2,202	1,892	1,589	1,318	1,181	1,370	958	854	780
INCREASE IN NET ASSETS	**4,818**	9,132	4,692	7,050	7,292	5,643	783	5,938	3,076	4,573	1,584
NET ASSETS											
Fixed income	**13,319**	17,304	11,476	10,276	10,622	12,509	11,409	17,569	19,007	19,199	18,129
Equities – Canadian	**17,739**	19,885	17,613	19,433	17,367	12,218	9,943	7,510	3,217	2,618	520
– Foreign	**23,141**	21,759	24,015	19,955	16,005	12,287	10,714	7,035	3,253	1,796	807
Inflation-sensitive investments											
– Commodities	**2,098**	1,090	401	126	—	—	—	—	—	—	—
– Real Estate	**6,201**	2,815	1,582	1,561	1,272	925	694	608	451	180	—
– Real Rate Products	**9,545**	4,239	3,019	1,597	1,066	1,064	653	548	457	16	—
Net Investments	**72,043**	67,092	58,106	52,948	46,332	39,003	33,413	33,270	26,385	23,809	19,456
Receivable from											
Province of Ontario	**1,251**	1,252	1,233	1,262	1,286	1,308	1,338	1,362	1,323	1,190	945
Other assets	**13,159**	7,040	5,391	8,537	3,293	1,586	622	36	72	10	—
Total assets	**86,453**	75,384	64,730	62,747	50,911	41,897	35,373	34,668	27,780	25,009	20,401
Liabilities	**(13,332)**	(7,081)	(5,559)	(8,268)	(3,482)	(1,760)	(879)	(957)	(7)	(312)	(277)
Net Assets	**73,121**	68,303	59,171	54,479	47,429	40,137	34,494	33,711	27,773	24,697	20,124
Smoothing reserve	**(4,341)**	(8,316)	(4,788)	(5,578)	(4,416)	(1,907)	(252)	(2,947)	(414)	(883)	709
Actuarial value of net assets	**68,780**	59,987	54,383	48,901	43,013	38,230	34,242	30,764	27,359	23,814	20,833
Accrued pension benefits	**58,556**	52,105	48,636	44,457	41,833	38,744	36,848	33,998	30,781	27,479	24,391
Surplus (Deficiency)	**10,224**	7,882	5,747	4,444	1,180	(514)	(2,606)	(3,234)	(3,422)	(3,665)	(3,558)
PERFORMANCE (%)											
Rate of return	**9.3**	17.4	9.9	15.6	19.0	16.9	1.7	21.7	8.9	19.6	5.6
Benchmark	**5.3**	17.6	11.9	15.6	18.1	17.2	(0.3)	20.5	8.0	15.4	(7.8)
Long-term goal	**7.7**	7.1	5.5	5.2	6.7	6.2	4.7	6.2	6.6	8.3	9.5

CORPORATE DIRECTORY

President & Chief Executive Officer
Claude Lamoureux

Investments
Robert Bertram, Executive Vice-President

Active Equities
Brian Gibson, Senior Vice-President

Relationship Investing
Roy Graydon, Vice-President

International Equity Indexes, Fixed Income & Foreign Exchange
Neil Petroff, Senior Vice-President

Fixed Income
Sean Rogister, Vice-President

International Equity Indexes
Barbara Trott, Vice-President

Quantitative Investments
Morgan McCague, Senior Vice-President

Canadian Core Portfolios
Marcus Dancer, Vice-President

Research & Economics
Leo de Bever, Senior Vice-President

New Business Development
Russ Bruch, Vice-President

Merchant Banking
Dean Metcalf, Vice-President

Member Services
Allan J. Reesor, Executive Vice-President & Chief Information Officer

Client Services
Rosemarie McClean, Vice-President

MIS Member Services
Phil Nichols, Vice-President

Finance
Andrew Jones, Vice-President

Human Resources & Public Affairs
John Brennan, Vice-President

Internal Audit
Peter Maher, Vice-President

Law
Roger Barton, Vice-President, General Counsel & Secretary

THE CADILLAC FAIRVIEW CORPORATION LIMITED
Real Estate Portfolio

President & Chief Executive Officer
Peter Sharpe

Portfolio Operations
Brian Muzyk, Executive Vice-President & Chief Operating Officer

Eastern Canada Portfolio
Normand Blouin, Senior Vice-President

Greater Toronto Area Portfolio
Tony Grossi, Senior Vice-President

Ontario Portfolio
Linda Gray, Senior Vice-President

U.S. Portfolio
Alan Carlisle, Senior Vice-President

Western Portfolio
Ron Wratschko, Senior Vice-President

E-business
Ronald Peddicord, Executive Vice-President

Technology
Scot Adams, Senior Vice-President and Technology Officer

Finance and Taxation
Ian MacKellar, Executive Vice-President and Chief Financial Officer

Law
Peter Barbetta, Executive Vice-President, General Counsel and Secretary

Office and Retail Development
Michael Kitt, Executive Vice-President

Architecture and Design
Rudy Adlaf, Senior Vice-President

Office Development
John Sullivan, Senior Vice-President

Project Management and Environmental Services
David Handley, Senior Vice-President

Investments
Andrea Stephen, Senior Vice-President

We welcome your comments and suggestions for this annual report, as well as other aspects of our communications program. Please call Lee Fullerton, Communications Manager, at 416-730-5347. e-mail: communications@otpp.com

Communications Department
Ontario Teachers' Pension Plan Board
5650 Yonge Street Toronto, Ontario M2M 4H5
Toll-free: 1-877-812-7989 Local: 416-228-5900
www.otpp.com

OTPP (impt).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: OTPP (impt)
Date: Saturday, September 17, 2016 09:10:49
Attachment 1: MOF letter.pdf

Hopefully the last attachment (but an important one that was just received late yesterday).

Nadine

MOF letter.pdf

ONTARIO TEACHERS' PENSION PLAN

5650 Yonge Street
Toronto, Ontario, Canada
M2M 4H5

tel: 416-228-5900 or 1 877-812-7989
fax: 416-730-5349
www.otpp.com

September 15, 2016

Alex Killoch, Director
BPS Pensions Branch
Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto, Ontario
M7A 1Y7

Dear Alex:

As requested, we are outlining the annual process for providing actuarial and financial information about the Ontario Teachers' Pension Plan (Plan) to the Ministry of Finance. We are also providing information related to the funding valuation of the Plan and in particular, the discount rate setting process. Copies of various documents, correspondence and memos have been attached for reference purposes with applicable dates noted below.

Annual Process Related to the Province of Ontario Budget

Each December, the Ministry of Finance provides a request for information to the President and CEO of the Plan to assist in the preparation of the Ontario Budget. Specific assumptions to be used in the analysis are provided including return on investment, inflation, real rate of return and anticipated salary growth. The Province selects the best estimate assumptions in accordance with the Chartered Professional Accountants of Canada Public Sector Accounting Board Handbook. (December 11, 2015 request from the Province attached).

The external Plan actuary – Mercer – prepares the liability and current service cost calculations using the "projected benefit method, pro-rated on services" and economic assumptions are requested by the Province. Supporting information including contribution and benefit information is provided by the Plan. (January 26, 2016 correspondence from Mercer and the Plan attached).

Supplemental information was prepared by Mercer at the request of the Province in June of 2016 to assist in addressing inquiries from the Office of the Auditor General of Ontario. (June 17, 2016 Memo attached).

Annual Funding Valuation Process

On an annual basis, Mercer prepares a preliminary valuation for review by the Ontario Teachers' Pension Plan Board (Board). It is the Board's responsibility to decide key actuarial assumptions in close collaboration with the Plan actuary. The independent actuary must confirm that the

assumptions are independently reasonable and are appropriate in aggregate in accordance with the Canadian Institute of Actuaries Standards of Practice.

The annual assumption setting exercise is robust. The determination of the discount rate is informed by the Funding Management Policy (described below) and the Discount Rate Review process which reflects what the Plan's assets can reasonably be expected to earn over the long run less expenses and less provisions for adverse deviation (PFAD). The Plan takes into consideration two key PFADs: plan maturity and insufficient return. PFADs are set with reference to the demographic profile of the Plan, the risk tolerance and intergenerational fairness between members. A key challenge is the maturity of the Plan with the ratio of active members to pensioners being 1.4 to 1 with the ratio projected to decrease in the future. Longevity compounds this challenge as Teachers in Ontario live longer than the general Canadian population and their life expectancy continues to increase.

For the January 1, 2016 funding valuation (which will be filed with the regulatory authorities by September 30th), the nominal discount rate is 4.8% with an underlying real return of 2.75%. This real return takes into account PFADs of approximately 150 basis points.

Funding versus Accounting Valuations

The funding valuation assesses the Plan's long-term financial health to facilitate determination of future contribution rates and benefit levels. For the Plan, the cost method used is the aggregate method which allows the Plan to address funding surpluses and deficits through future benefits changes (eg. Conditional Inflation Protection (CIP)) and enables the Plan to factor in cash flows from future service. This differs from accounting standards which requires use of the projected benefit method prorated on services.

There are also differences in the assumption setting process. The Plan's assumption setting process for the annual funding valuation is noted above. Please refer to the attached Memo prepared by Mercer dated September 15, 2016, which outlines key methods and assumptions to be used to value pension plans per Canadian Public Sector Accounting Standards (PS3250).

Funding Management Policy

The Plan Sponsors (the Province of Ontario and Ontario Teachers' Federation) are jointly-responsible for two key decisions: a) what pension benefits the Plan will provide, and b) the contribution rate needed to ensure the Plan's benefits are fully funded over the long term. In doing so, the Sponsors negotiate the use of surplus funds and, when there is a funding shortfall, both share responsibility for eliminating it.

In March 2003, the Sponsors adopted a Funding Management Policy (FMP) as a supplement to the Partners' Agreement, with the objective to provide a guidance framework for decision making when there is a funding surplus or shortfall. A key component in the creation of the FMP was the concept of 'funding zones', each defined by a range. The funding zones provide a point of reference for whether action is required by the Sponsors, and if so, guidance is provided on how to use any surplus funds or resolve any shortfall – specifically, answering the question of when is it prudent to increase or decrease benefits, raise or lower contribution rates, or simply conserve assets for an uncertain time. While the FMP outlines preferred mechanisms

associated with its various funding zones, it is ultimately the Sponsors' responsibility to decide what actions to take.

In March 2015, a zone for Temporary Plan Improvements was added to the FMP, to allow for temporary contribution decreases, surplus distribution and/or benefit improvements (so long as they do not increase the long-term cost of the Plan) when assets exceed the projected cost of future benefits when valued using the Temporary Basis. Uses of surplus in this zone are paced, amortized over a period between three and 10 years, with an annual spending limit applied to amortization terms shorter than 10 years. The zone includes a provision that temporary improvements cease if a significant market event occurs. (FMP Framework and Summary attached).

As noted in Mercer's June 17th Memo, "should the plan earn future returns that are equal to the valuation discount rate adopted by the Province for financial statement reporting purposes, it is possible that some of the future contribution requirements could be reduced by agreement of the Sponsors as experience gains would be recognized in the funding valuation based on the assumptions currently used for funding purposes".

*****

We trust that the above information and various attachments provide a helpful overview of the annual process for providing financial information to the Ministry of Finance as well as the process in place for the annual funding valuation. Please do not hesitate to call if you have any questions or require further information.

Sincerely,

Barbara Zvan, FSA, FCIA, CERA
SVP, Strategy & Risk and Chief Investment Risk Officer
(416) 730-6364
Barbara_zvan@otpp.com

Cc: Ross Peebles
Joshua Paul
Rob Pomykacz
Allan Shapira
Mary Cover

Ministry of Finance

Income Security and Pension Policy Division

Office of the Assistant Deputy Minister
Frost Building South, 5th floor
7 Queen's Park Crescent East
Toronto ON M7A 1Y7
Tel.: 416 212-8073
Fax: 416 327-0760

Ministère des Finances

Division des politiques en matière de sécurité du revenu et de régimes de retraite

Bureau du sous-ministre adjoint
Édifice Frost Sud, 5e étage
7 Queen's Park Crescent East
Toronto ON M7A 1Y7
Tél.: 416 212-8073
Téléc.: 416 327-0160

Ontario

December 11, 2015

Mr. Ron Mock
President and Chief Executive Officer
Ontario Teachers' Pension Plan Board
5650 Yonge Street, Suite 400
Toronto, Ontario
M2M 4H5

Dear Mr. Mock:

In preparation for the 2016 Ontario Budget, I am writing to request actuarial and financial information, as at December 31, 2015, on the Teachers' Pension Plan (TPP) and the Teachers' Retirement Compensation Arrangement (TRCA). This information is required for calculating the Province's 2015-16 pension expense and pension liability.

To ensure that the information requested in this letter is consistent with the Province's best estimates (as required by the Public Sector Accounting Board [PSAB]), please use the following economic assumptions in your actuarial calculations for the requested TPP information.

Economic Assumption (annual rates)	Basis 1	Basis 2	Basis 3	Basis 4
Return on Investment	6.50%	6.25%	6.25%	6.00%
Inflation	2.25%	2.25%	2.00%	2.00%
Real Rate of Return	4.25%	4.00%	4.25%	4.00%
Salary Growth	2.25% for 2016 to 2019 and 3.25% thereafter	2.25% for 2016 to 2019 and 3.25% thereafter	2.00% for 2016 to 2019 and 3.00% thereafter	2.00% for 2016 to 2019, 3.00% thereafter

Despite the salary growth assumption above, please reflect in the valuation a 1% lump sum increase for the school year 2015-16, a 1% increase for the school year 2016-17 and additional 0.5% increase half-way through the school year 2016-17.

...2

We understand the Board may be preparing its financial statements based on International Financial Reporting Standards and Canadian Institute of Chartered Accountant Standard Section 4600. There has not been any change in reporting requirements under the Public Sector Accounting Board. Therefore, the actuarial and financial information we are requesting in this letter should be prepared in the same manner as has been provided to us in prior years.

Please provide the following actuarial and financial information with one set of calculations for each set of assumptions outlined in the table above. In these calculations for the TPP, please use the projected benefit method, prorated on services:

1. Actuarial present value (APV) of accrued benefit obligations, as at December 31, 2015. ***Basis 4 in last year's letter was used by the Province for 2015. Please include an APV reconciliation on that basis from December 31, 2014 to December 31, 2015 for all four bases.***

2. Actuarial value and market value of pension fund assets, as at December 31, 2015. The actuarial value of assets should be determined on the same basis as in prior years.

3. Interest on accrued benefits, cost of benefits accrued (separating out current period benefit cost, cost related to any plan amendments, transfers and other costs), actuarial adjustments, and the benefits paid (separate retirement pensions from other benefit payments) for the year ended December 31, 2015.

4. Contributions broken down by employee contribution, Province of Ontario contribution and other transfers for the year ended December 31, 2015 and the additional payments from the Province of Ontario with respect to "payments re foregone inflation adjustment" under subsection 5(2.1) of the *Teachers' Pension Act* for the year ended December 31, 2015. Please provide the same level of detail as would be disclosed in the "Contributions" note to the TPP's 2015 financial statements.

5. Return on investment, inflation and salary escalation assumptions that will be used in the TPP's 2015 financial statements.

6. Expected average remaining service life of active employees, as at December 31, 2015.

7. Net gain and loss for the year ended December 31, 2015 that would be subject to smoothing on the same basis as in prior years. Please also provide the same level of detail as in prior years.

...3

8. The "Schedule of Contributions and Interest Receivable from the Province of Ontario" (due in early January, 2016).

9. Number of pensioners and active members, as at December 31, 2015.

10. Please provide a brief, high level explanation of the source(s) of the actuarial gains and losses for 2015.

11. Please provide the 2016 service cost for all requested bases.

12. 2015 financial statements of the TPP and the TRCA as soon as they are available.

Please provide items 1 to 5 above for the TRCA based on what will be reported in the TRCA's 2015 financial statements. Note that we do not require that the information on the TRCA be based on the Province's economic assumptions.

Although the TPP has been amended to provide conditional inflation protection for service after December 31, 2009, the intention of the Partners is to provide 100% inflation protection to the extent possible. As such, please provide us with the actuarial calculation for #1 and #3 above assuming that inflation protection for post 2009 service will be provided at 100% and at 50% of the annual increase in the Consumer Price Index.

We require these estimates by **January 29, 2016.** Should you have any questions, please contact Mr. Rob Pomykacz at robert.pomykacz@ontario.ca, or by telephone at (416) 327-0156.

To expedite the preparation of Ontario's 2015-16 *Public Accounts*, I would also ask that you communicate by letter by April 30, 2016 whether, to the best of your knowledge, there were any events between December 31, 2015 and March 31, 2016, which would in your opinion, affect these valuation results in a material way.

Please forward all the information requested in this letter to:

Mark Rozic, Manager (Acting)
External Reporting Branch
Office of the Provincial Controller Division
Treasury Board Secretariat
2nd Floor, Office 260, Frost Building South
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel: (416) 325-8293
Fax: (416) 325-2029
E-mail: mark.rozic@ontario.ca

And to:

Alex Killoch, Director
BPS Pensions Branch
Ministry of Finance
1st Floor, Frost Building South
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel: (416) 325-5724
Fax: (416) 212-8293
E-mail: alex.killoch@ontario.ca

Thank you for your cooperation in this matter.

Yours sincerely,

Leah Myers

c: Alex Killoch
Sanjeev Batra
Mark Rozic
Pauline Fong
Joshua Paul
Mary Cover
Rob Pomykacz
Bill Pelow

ONTARIO TEACHERS'
PENSION PLAN / RÉGIME DE RETRAITE DES ENSEIGNANTES ET DES ENSEIGNANTS

5650 Yonge Street
Toronto, Ontario, Canada
M2M 4H5

tel. 416-226-2700 or 1-800-668-0105
fax. 416-730-7807 or 1-800-949-8208
www.otpp.com

January 26, 2016

Mark Rozic, Manager (Acting)
External Reporting Branch
Office of the Provincial Controller Division
Treasury Board Secretariat
2nd Floor, Office 260, Frost Building South
7 Queen's Park Crescent
Toronto, Ontario M7A 1Y7

Dear Mr. Rozic:

I am responding to a letter dated December 11, 2015 from Ms. Leah Myers that requested actuarial and financial information about the Ontario Teachers' Pension Plan (registered pension plan - RPP) and the Retirement Compensation Arrangement (RCA) at December 31, 2015.

Items 1, 3 (except the benefit payment breakdown), 6, 10 and 11 are included in the enclosed letter from Mercer (Canada) Limited.

Item 2 - Market Value of Pension Fund Assets ($ millions)

Please note that we no longer use an asset smoothing method for our financial statements. As such, there is no separate "actuarial" value of assets.

Market value of assets at December 31, 2015	Not yet available

Item – 3(a) RPP Benefits Paid ($ millions)

Retirement Pensions	$ 5,056
Survivor Pensions	273
Disability Pensions	27
Lump Sum Death Benefits	71
Refunds	1
Commuted Value Transfers	74
Transfers to Other Plans	8
Family Law Value Transfers	27
Total	$ 5,537

Item – 3(b) RCA Benefits Paid

The RCA pension payments made in 2015 were $7.40 million and the RCA lump sum payments in 2015 were $4.87 million.

Item - 4(a) RPP Contributions ($ millions)

Members		
Current Service	$	1,580
Optional Credit		35
Total	$	1,615
Province of Ontario		
Current Service	$	1,568
Interest		37
Optional Credit		32
Total	$	1,637
Other Employers	$	33
Transfers from Other Plans		14
Total	$	47
Grand Total	$	3,299

Item 4(b) - RCA Contributions ($ millions)

Members	$	5.6
Province of Ontario		3.3
Other Employers		2.4
Total	$	11.3

Item 4(c) - Payments re: Foregone Inflation Adjustments

The foregone inflation amounts for 2014 payments which are part of the government billing for payment in January 2016 are as follows:

		Total		**Province of Ontario**
RPP	$	1,130,253	$	1,106,279
RCA		12,205		11,946
Total	$	1,142,458	$	1,118,225

Item 5 - Economic Assumptions	**RPP**	**RCA**
Discount Rate	3.25%	1.625%
Salary Escalation Rate	2.50%	2.50%
Inflation Rate	1.50%	1.50%
Real Rate	1.70%	0.125%

Item 7 - Net Gain and Loss on Actuarial Value of Assets

Not applicable. Please note that we no longer use an asset smoothing method for our financial statements. As such, there is no separate "actuarial" value of assets.

Item 8 - Schedule of Contributions and Interest Receivable ($ millions)

Contributions	$	3,157
Interest		51
Total	$	3,208

Item 9 - Number of Pensioners and Active Members as at December 31, 2015

Pensioners	133,000
Active Members	183,000

Item 12 – Financial Statements

Not yet available.

We will provide any outstanding information as soon as it is available. In addition, we will send an updated version of this letter if any of the information contained herein is subsequently changed.

Please do not hesitate to call if you have any questions.

Sincerely,

Mary Cover, FSA, FCIA
Director, Pension Strategy and Enterprise Risk
(416) 730-2976
mary_cover@otpp.com

cc: Alex Killoch – Ministry of Finance

Lise Houle
Principal

120 Bremner Boulevard, Suite 800
Toronto ON M5J 0A8
416 868 2039 Fax 416 868 7695
lise.houle@mercer.com
www.mercer.ca

MERCER

26 January 2016

Ms. Mary Cover
Director, Pension Strategy & Enterprise Risk
Ontario Teachers' Pension Plan Board
5650 Yonge Street
Toronto, ON M2M 4H5

Private & Confidential

Subject: December 31, 2015 Valuation Results Using the Province's Assumptions

Dear Mary,

As requested, we have provided you with information for the Ontario Teachers' Pension Plan (OTPP) on points 1, 3, 6, 10 and 11 in the December 11, 2015 letter from the Ministry of Finance to Mr. Ron Mock. As instructed in the Ministry letter, the following sets of assumptions have been used in calculating the liabilities as at December 31, 2015:

	Basis 1	**Basis 2**	**Basis 3**	**Basis 4**
Valuation discount rate	6.50%	6.25%	6.25%	6.00%
Inflation rate	2.25%	2.25%	2.00%	2.00%
Real valuation discount rate	4.25%	4.00%	4.25%	4.00%
Salary escalation rate	2.25% for the years 2016 to 2019, 3.25% thereafter	2.25% for the years 2016 to 2019, 3.25% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter

For each basis, all the other assumptions and the valuation methods are those used by the Ontario Teachers' Pension Plan Board in the December 31, 2015 valuation for financial statement purposes. This includes proposed demographic assumption changes as well as negotiated salary increases providing a 1% lump sum increase at September 1, 2015, a 1% increase at September 1, 2016 and a 0.5% increase half-way through the school year commencing September 1, 2016. The demographic assumptions were updated to reflect recent experience of Plan members related to retirement, termination of plan membership, re-

instatement of inactive members and increases in salaries related to experience. The changes to the demographic assumptions are described in the presentation material from our meeting with the Technical Committee on January 13, 2016. The remaining demographic assumptions are provided in our Report on the Actuarial Valuation for Financial Statement Purposes as at December 31, 2014. We expect that our report on the December 31, 2015 actuarial valuation will be finalized in March, 2016.

For the sake of clarity, we note that the assumed increases in the YMPE and maximum pension limits under the Income Tax Act are the same rates as the long-term salary growth rates noted for each of the four bases.

The Province has requested that we prepare the results assuming that inflation protection for post 2009 service will be provided at 100% and at 50% of the assumed inflation rate. In this letter we have included results using both of these alternative inflation protection levels. We note that at the time of preparing this letter, the Plan provides for 70% of conditional inflation protection for post 2009 service.

At the Province's request, the liabilities have been calculated using the "projected benefit method, pro-rated on services". In the calculations presented in this letter, we have used the projected benefit method, pro-rated on service with three attribution periods to reflect the different indexing provisions for service accrued to December 31, 2009, service accrued from January 1, 2010 to December 31, 2013 and service accrued from January 1, 2014. However, we note that the same level of indexing was applied to all service from January 1, 2010 to December 31, 2015 for purposes of calculating the liabilities provided in this letter (whether the results are based on 100% or 50% conditional indexing).

We have included information regarding the experience gain/loss incurred relative to salary growth during the year as well as the impact on the December 31, 2015 liabilities due to changing the rate of inflation and salary growth assumption in Bases 3 and 4 in our tables relative to the assumptions from Bases 1 and 2. We note that since the assumed increases in salaries determined by the Province are set equal to the assumed inflation rate plus 1%, we have not separately identified the changes in salary only without the corresponding changes in inflation.

The results as at December 31, 2015 are summarized in the following tables.

Results using 100% conditional indexing for post 2009 service (results in $ millions)

	Basis 1	Basis 2	Basis 3	Basis 4
Valuation discount rate:	**6.50%**	**6.25%**	**6.25%**	**6.00%**
Inflation rate:	**2.25%**	**2.25%**	**2.00%**	**2.00%**
Salary escalation rate:	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**
1. Actuarial present value (APV) of accrued pension benefits at December 31, 2014 using **Last Year's Basis 4**	$113,801	$113,801	$113,801	$113,801
2. Increase in the APV of accrued pension benefits				
Interest on the APV of accrued pension benefits	$7,310	$7,310	$7,310	$7,310
Current Service Cost (mid-year)	2,868	2,868	2,868	2,868
Contributions for optional credit	34	34	34	34
Repayment of refunds	0	0	0	0
Transfers from other plans	14	14	14	14
Change in valuation assumptions and methods:				
Change in demographic assumptions	350	350	350	350
Change in interest rate from Basis 1	0	4,142	4,142	8,309
	$10,576	$14,718	$14,718	$18,885
3. Decrease in the APV of accrued pension benefits				
Pensions paid	$5,356	$5,356	$5,356	$5,356
Refund of contributions	0	0	0	0
Lump sum payments and transfers	180	180	180	180
Salary experience gains	1,028	1,028	1,028	1,028
All other experience gains	552	552	552	552
Negotiated Salary Increases	1,161	1,161	1,161	1,161
Change in inflation rate and salary growth rates from Basis 1	0	0	3,829	3,829
Change in other actuarial assumptions and methods	46[1]	46	46	46
	$8,323	$8,323	$12,152	$12,152
4. Net increase in the APV of accrued pension benefits	$2,253	$6,395	$2,566	$6,733
5. APV of accrued pension benefits at December 31, 2015	$116,054	$120,196	$116,367	$120,534
6. Annual current service cost at January 1, 2016 (BOY)	$2,880	$3,058	$2,899	$3,079

[1] Change to commuted value assumption to value benefits payable upon termination

Results using 50% conditional indexing for post 2009 service (results in $ millions)

	Basis 1	Basis 2	Basis 3	Basis 4
Valuation discount rate:	**6.50%**	**6.25%**	**6.25%**	**6.00%**
Inflation rate:	**2.25%**	**2.25%**	**2.00%**	**2.00%**
Salary escalation rate:	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.25% for the years 2016 to 2019, 3.25% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**	**2.00% for the years 2016 to 2019, 3.00% thereafter**
1. Actuarial present value (APV) of accrued pension benefits at December 31, 2014 using **Last Year's Basis 4**	$112,004	$112,004	$112,004	$112,004
2. Increase in the APV of accrued pension benefits				
Interest on the APV of accrued pension benefits	$7,182	$7,182	$7,182	$7,182
Current Service Cost (mid-year)	2,508	2,508	2,508	2,508
Contributions for optional credit	34	34	34	34
Repayment of refunds	0	0	0	0
Transfers from other plans	14	14	14	14
Change in valuation assumptions and methods:				
Change in demographic assumptions	322	322	322	322
Change in interest rate from Basis 1	0	3,975	3,975	7,990
	$10,060	$14,035	$14,035	$18,050
3. Decrease in the APV of accrued pension benefits				
Pensions paid	$5,356	$5,356	$5,356	$5,356
Refund of contributions	0	0	0	0
Lump sum payments and transfers	180	180	180	180
Salary experience gains	979	979	979	979
All other experience gains	545	545	545	545
Negotiated Salary Increases	1,104	1,104	1,104	1,104
Change in inflation rate and salary growth rates from Basis 1	0	0	3,461	3,461
Change in other actuarial assumptions and methods	36[2]	36	36	36
	$8,200	$8,200	$11,661	$11,661
4. Net increase in the APV of accrued pension benefits	$1,860	$5,835	$2,374	$6,389
5. APV of accrued pension benefits at December 31, 2015	$113,864	$117,839	$114,378	$118,393
6. Annual current service cost at January 1, 2016 (BOY)	$2,523	$2,671	$2,574	$2,727

[2] Change to commuted value assumption to value benefits payable upon termination

We have the following comments on the results:

- Our valuation of the actuarial present value of the accrued pension benefits as at December 31, 2015 and the 2016 current service costs are based on membership data as at August 31, 2015. The actuarial present value of accrued pension benefits as at August 31, 2015 is then extrapolated forward to December 31, 2015, reflecting expected cashflows and the actual inflation adjustment as at January 1, 2016 of 1.30% for pre-2010 service and 0.91% for post-2009 service. The 2015 mid-year current service is based on membership data as at August 31, 2014. A summary of the membership data as at August 31, 2015 was included with our email of October 23rd, 2015 to Glen Tunney.

- We understand that the Province adopted Last Year's Basis 4 in establishing the actuarial present value of accrued pension benefits as at December 31, 2014. This is the same as Basis 1 for the current year.

- We have assumed that any change in the Province's assumptions (i.e. nominal and real discount rates, inflation rate, and salary escalation rate would occur at December 31, 2015).

The Expected Average Remaining Service Lifetime (EARSL) of active employees at August 31, 2015 and estimated for December 31, 2015, is 15.3 years. The increase in the EARSL from the prior year is primarily attributable to the change in assumed termination and retirement rates.

The net experience gain incurred on the plan liability since the prior year was primarily attributable to the lower than expected level of inflation for the January 1, 2016 indexing. Other experience gains and losses were relatively small.

The figures presented in this letter exclude the Ontario Teachers' Retirement Compensation Arrangement ("OTRCA"), which provides benefits to members that are in excess of those permitted to be provided from the registered pension plan. The Province has requested information on the OTRCA based on what will be reported in the OTRCA's 2015 financial statements, and does not require calculations on any other basis.

While the actuarial demographic assumptions used to estimate liabilities for the Plan represent the Ontario Teachers' Pension Plan Board's best estimate of future events and the economic assumptions are as provided by the Province, and while in our opinion the assumptions used for the valuation are appropriate provided the Province selected the economic assumptions in accordance with the Chartered Professional Accountants of Canada Public Sector Accounting Board Handbook ("PSAB Handbook"), the Plan's future experience will inevitably differ, perhaps significantly, from the actuarial assumptions. Any differences between the actuarial

assumptions and future experience will emerge as gains or losses in future valuations, and will affect the financial position of the Plan at that time.

We have tested the data for reasonableness and consistency, and in my opinion, the membership data on which the valuation is based are sufficient and reliable for the purpose of the valuation. In my opinion, the calculations have been made in accordance with my understanding of the reporting requirements under the PSAB Handbook and this report has been prepared, and, my opinions given, in accordance with accepted actuarial practice in Canada.

If you have any questions, please do not hesitate to call.

Sincerely,

Lise Houle

Copy:
Scott Clausen, Mercer
Jason Lipping, Mercer
\\mercer.com\ca_data\shared\tor\ru1\client\ontr-tch\2015\funding\programs\ministry of finance work\cover jan 25 2016 ministry info ltr.doc

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120 Bremner Boulevard, Suite 800
Toronto, Ontario M5J 0A8
Fax +1 416 868 7555
Lise.houle@mercer.com
www.mercer.ca

MEMO

TO: Mary Cover, Ontario Teachers' Pension Plan
DATE: 17 June 2016
FROM: Lise Houle
SUBJECT: Ministry of Finance Request for Supplemental Accounting Results
COPY: Scott Clausen, Jason Lipping, Mercer

As a follow-up to the accounting results we provided to you with our letter of January 26th, 2016, determined using the actuarial assumptions provided by the Ministry of Finance, we understand that the Ministry has requested supplemental information from the Ontario Teachers' Pension Plan as the Ministry addresses inquiries from the Office of the Auditor General of Ontario.

In particular, the Ministry has requested the following information relating to the Ontario Teachers' Pension Plan, using Bases 3 and 4 described in our January 26th letter:

- Present value of future current service accruals,
- Present value of future basic contributions, and
- Present value of future supplemental contributions

The requested information, calculated as at August 31, 2015 and rolled forward to December 31, 2015 is as follows:

	Basis 3	**Basis 4**
Valuation Discount Rate	6.25%	6.00%
Inflation Rate	2.00%	2.00%
Real Valuation Discount Rate	4.25%	4.00%
Salary Escalation Rate	2.00% for the years 2016 to 2019, 3.00% thereafter	2.00% for the years 2016 to 2019, 3.00% thereafter
PV of future service accruals	$36,767 million	$39,563 million
PV of future basic contributions	$36,073 million	$36,826 million
PV of future supplemental contributions	$2,888 million	$2,924 million

The present value of future service accruals is calculated as the difference between the actuarial present value of total projected pension benefits (ie aggregate liabilities) less the actuarial present value of accrued pension benefits as at December 31, 2015. The benefits used in our calculations reflect 100% conditional indexing for both pre-2010 and post-2009 service. The actuarial present

value of accrued pension benefits as at December 31, 2015 are those provided in our January 26th letter while the actuarial present value of total projected pension benefits are calculated using the same approach, but captures all projected service to date of expected decrement.

The actuarial present value of basic contribution reflects both expected basic employee and employer contributions to be paid to date of assumed decrement.

The actuarial present value of future service accruals and of basic contributions only considers current active and inactive members of the Ontario Teachers' Pension Plan. In keeping with the approach used for the funding valuation, the present value of future supplemental contributions is determined on an open-group basis and reflects scheduled contributions to December 31, 2026.

It is our understanding that the province intends to use these figures to perform a high level test to consider if there should be a limit applied to the asset/surplus held as at December 31, 2015. We note that, should the plan earn future returns that are equal to the valuation discount rate adopted by the Province for financial statement reporting purposes, it is possible that some of the future contribution requirements could be reduced by agreement of the Sponsors as experience gains would be recognized in the funding valuation based on the assumptions currently used for funding purposes.

For more details on the actuarial assumptions, methods and data used in our calculations, please refer to our January 26th letter. The demographic assumptions are summarized in our Report on the Actuarial Valuation for Financial Statement Purposes as at December 31, 2015.

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120 Bremner Boulevard, Suite 800
Toronto, Ontario M5J 0A8
Fax +1 416 868 7555
scott.clausen@mercer.com
www.mercer.ca

MEMO

TO: Mary Cover, Ontario Teachers' Pension Plan
DATE: 15 September 2016
FROM: Scott Clausen, Mercer
SUBJECT: Canadian Public Sector Accounting Standards (PS3250)

As discussed, the purpose of this memo is to provide section references from Canadian Public Sector Accounting Standards (PS 3250) that refer to the selection of methods and assumptions to be used to value pension plans for the purpose of the province's financial reporting. All Section references shown in this memo refer to Sections from PS3250.

Actuarial Cost Method:

.029
The projected benefit method prorated on services should be used to attribute the cost of retirement benefits to the periods of employee service.

.030
When a retirement plan provides benefits that accrue in a non-uniform manner, the projected benefit method prorated on services may need to be adjusted to reflect the manner in which retirement benefits are earned by employees. For example, a pension plan formula may state that the pension benefit accrues at one percent of salary for the first 15 years and at two percent of salary for the final 20 years. In this circumstance, the prorating of the total estimated benefit to each accounting period would be adjusted to reflect the rates at which pension benefits are earned in that 35-year period.

.032
In other retirement plans, regular benefit increases for inflation protection may be provided even when such protection is not promised in a contractual agreement or in legislation. For those plans, careful analysis and professional judgment are needed to determine the substance of a government's obligation. If a regular pattern of benefit increases can be established over a reasonable period, it may be appropriate to incorporate the cost of such inflation protection in the cost of retirement benefits earned to the accounting date and reported as an accrued benefit obligation.

Asset Valuation:

.035

When determining a government's retirement benefit liability and expenditure / expense, plan assets would be valued at market-related values. Under this method, plan assets are recorded at market value or they are adjusted to market value over a period not to exceed five years. Values adjusted to market closely approximate current economic value in a manner that can minimize short-term fluctuations. Market-related values would be used because they are objective and verifiable. Once a basis of valuation is chosen it would be applied consistently.

Actuarial Assumptions:

.042

Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts.

.044

The actuarial assumptions underlying the valuation of the retirement benefit liability and expenditure / expense would be internally consistent. For example, when a government determines its discount rates by reference to its plan asset earnings, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the short-term forecast of rates of return on assets currently held in the fund. When a government determines its discount rates by reference to its cost of borrowing, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the specific rates of interest and the periods committed to by the government on the amounts borrowed.

Limit on Accrued Benefit Asset:

.050

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

.053

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

.054

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

.055

The objective of the Recommendation in paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

.056

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

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

Actuarial Gains and Losses:

.061

Actuarial gains and losses would be amortized over a reasonable future period because of their tentative nature and because further adjustments will likely be required in the future. A reasonable future period is the **expected average remaining service life of the related employee group**. Amortization may commence in the period following the determination of the adjustment. Actuarial gains and losses would be determined on a market value basis or a basis adjusted to market value, consistent with paragraph .035.

Past Service Costs:

.066

The cost of plan amendments related to prior period employee services should be accounted for in the period of the plan amendment.

Joint Defined Benefit Plans:

.079

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

.081

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

FUNDING MANAGEMENT POLICY (FMP) FRAMEWORK DESCRIPTION

Valuation Basis

Assets = 110% of Liabilities valued at interest rates + 0.5%

Zone:	**Permanent Plan Improvements**
Mechanism:	**Improve benefits as negotiated**
Funding Risk:	Plan is essentially fully funded at Government of Canada long bond rates. Funding security is desired to ensure the Plan can support these benefits continually in the future. The impact of new teachers is important as they will create losses.

That is, Assets ~ 133% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.25%

Zone:	**Temporary Plan Improvements**
Mechanism:	**Improve benefits or lower contributions as negotiated[1]**
Funding Risk:	Plan is well funded and can afford changes that temporarily provide a benefit enhancement (as long as it does not create a long term cost) and/or lower the contributions being paid into the Plan.

[1] Amortization period used to determine temporary benefit

That is, Assets ~ 107% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.55%

Zone:	**Fully Funded (Do Nothing)**
Mechanism:	**Maintain Base Benefits and Contributions**
Funding Risk:	Plan is adequately funded to provide base benefits supported by the base contributions. Given the volatility of market factors and the numerous assumptions in the funding valuation, "fully funded" is considered a range.

Zone:	**Additional Support Required From Current FMP Levers**
Mechanism:	**Raise Contribution Rates and/or Invoke Conditional Inflation Protection as negotiated**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions. An increase to the contribution rate (within FMP maximum) and/or a decrease to the level of indexing being provided are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Zone:	**Additional Support Required From New/Additional Changes**
Mechanism:	**Negotiate other plan changes**
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions and CIP is fully invoked and contribution rates are increased to maximum outlined in FMP. Plan changes are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
Application (Article I):	**Section 1.01 and 1.02** ▪ Requires the Board to use Board's "best estimates assumptions," including a margin for adverse deviation in the case of the discount rate. ▪ Sets out what best estimates economic assumptions may be based on. ▪ Requires the Board to maintain indices to record inflation adjustments for post-2009 service. **Sections 1.03 and 1.04** ▪ If the Board uses a discount rate different from that outlined in the FMP and this discount rate is more penalizing (that is, produces a larger deficit or a smaller surplus), the FMP becomes void in 12 months unless both Partners notify the Board otherwise. These sections serve as an "exit" provision for the Partners. **Section 1.05** sets out under what circumstances each section of the FMP applies. **Section 1.06** limits surplus distributions or contribution decreases to those permitted by law. **Section 1.07** makes temporary improvements conditional on not having a restoration basis deficit.
Definitions (Article II):	**Section 2.01** Defines key terms, including: ▪ Basic contributions (contributions as per Sch.1 on January 1, 2012), which is used throughout the FMP as the target contribution rate (10.4% on earnings up to the YMPE/12% above the YMPE). ▪ Run-rate benefits (benefits as per Sch.1 on January 1, 2009), which include 100% inflation protection and assume basic contributions. ▪ Reference Rate (rate chosen by the Board representing Government of Canada nominal and real return bonds, which may be based on market or smoothed data; has recently been 3 year smoothed nominal and real return bonds). ▪ Remaining amortization value (difference between the temporary improvement value and the commitment value). ▪ Temporary improvement value (present value of a temporary improvement amortized over 3-10 years; if amortized over fewer than 10 years, improvement for a year is limited to the amount of basic contributions paid during a year).
Restore basic contributions and benefits (Article III):	**Section 3.01** ▪ Restoration basis is used (*reference rate* + 1.55%). ▪ Defines assets (refers to PBA Regulations) and current and revised liabilities. **Section 3.02** ▪ Sets out that current and revised liabilities are calculated using the restoration basis, plus an adjustment. The phrase "plus an adjustment" is used throughout the FMP and reflects the fact that the Board often files using a basis that is higher than required under the FMP. **Section 3.03** ▪ Outlines how indexing is accounted for in the valuation (that is, level of indexing provided in current filing zone continues).
Restoration Basis: *Surplus* (Article III continued)	*Sections 3.04 to 3.08 apply when surplus exists using the restoration basis and current contributions are higher than target, partial indexing (for previous years or go forward) exists or other benefits have been reduced.* **Section 3.04** Sets conditions under which sections 3.05-3.08 apply: ▪ If Assets > Liabilities (surplus reported); and ▪ Current contributions > Basic contributions (i.e., contributions are above long-term target level); or ▪ Current Benefits < Run-Rate Benefits (i.e. contributions are above long-term target level or benefits are below the long-term target level). **Section 3.06** Sets out the order of how to restore past benefit reductions or contribution increases: ▪ Actions can consist of increasing benefits to run-rate (long-term target) including prospective restoration or lowering contributions to basic (target) or a combination. ▪ First, increase go-forward indexing to 50% for post-2013 service period, then to 100% on all post-2009 service periods. Second, restore current pension amounts to run rate level, as much as possible, starting with the years where indexing was less than 50% until all years of partial indexation are restored to the same level and then restore to 100% for all service periods. ▪ Partners reserve the right to reconsider order in the future. **Section 3.07** A number of conditions apply after a decision: ▪ Assets equal to or greater than revised liabilities (i.e. no deficit created); ▪ Inflation indexing restored to no more than if 100% of inflation was provided;

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	▪ Inflation indexing restored to no less than current level (i.e. can't lower prior inflation indexing given); ▪ The value of revised benefits needs to be between current and run-rate benefits (similarly, contributions must be between current and target). **Section 3.08** (Expires December 30, 2017) Sets out the limits from the 2013 Term Sheet (commonly known as the JSPP Agreement) with respect to escalated adjustments and benefit improvements: ▪ Escalated adjustments if assets are greater than 100% of the current liabilities (and not below 100% after). ▪ Benefit improvement or restoration if net assets available for benefits are greater than 105% of the current (unsmoothed) liabilities (and not below 105% after).
Restoration Basis: *Deficit* (Article III continued)	*Sections 3.09 to 3.14 apply when the liabilities are greater than the assets using the restoration basis; thus the Partners must raise contribution rates, lower the amount of indexing and/or decrease other benefits.* **Section 3.09** Sets conditions under which Sections 3.10 to 3.14 apply: ▪ If Current liabilities > Assets (i.e., deficit reported). **Section 3.11** Sets out that deficit can be eliminated by changing contributions or benefits provided that: ▪ Assets are equal to or greater than revised liabilities; and ▪ Revised member contributions are no more than 15% (above YMPE). **Section 3.12** The Partners can agree to change benefits or contribution level as long as: ▪ Partners have entered into a written agreement governing the manner in which contributions by the Minister and the Employers will be adjusted to offset any reduction in benefits; and ▪ No indexing granted gets taken away. **Section 3.13** Outlines the current intention that member contributions will be increased up to 15% (above YMPE) before benefits are reduced or less than full indexing is provided. **Section 3.14** Sets out the limits with respect to the 2013 Term Sheet regarding employer contribution increases.
Funding Zone: Temporary (Article IV):	**Section 4.01** ▪ Temporary basis is used (*reference rate* + 1.25%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent). - Current liabilities (liabilities including the greater of current and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Revised liabilities (liabilities including the greater of revised and run-rate benefits and any remaining amortization value from a previous temporary commitment). - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus). **Section 4.02** Sets out that the liabilities are calculated using the temporary basis, plus an adjustment. *Sections 4.03 to 4.06 apply when the plan has a surplus using the temporary basis; that is, there is surplus available for improving benefits, decreasing contributions or distributing surplus, all on a temporary basis. The surplus spend is amortized over a period of three to ten years, at the partners' choice. If amortization period is less than ten years, the annual spend limit is the amount of basic contributions for a year.* **Section 4.03** Sets out conditions under which Sections 4.04 and 4.05 apply: - If assets > liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided. **Section 4.04**

APPENDIX I. FUNDING MANAGEMENT POLICY SUMMARY

Subject	Summary of Provisions
	The Board reports the commitment value (the amount of surplus that can be used to provide a temporary improvement). **Section 4.05** The Partners can agree to temporary improvements so long as after the change, assets over revised liabilities are equal to or greater than zero. **Section 4.06** provides a requirement for a side agreement setting out how Minister contributions are adjusted if there is a surplus distribution or temporary improvement of benefits.
"Do Nothing" Zone (Article IV continued):	*Sections 4.07 to 4.09 apply if assets are equal to or less than current liabilities using the temporary basis; that is, if there is a deficit using the temporary basis.* **Section 4.09** States that the Partners will not provide new improvements if there is a temporary basis deficit. That is, the Partners will do nothing, and Article III (restoration basis) will apply. However, no actions result from move to restoration because contributions and indexing are already at run-rate in order to be in temporary zone. The Partners could, however, have to file a valuation (using the restoration basis) if the filing schedule required a filing.
Funding Zone: Distributions (Article V):	**Section 5.01** ▪ Distribution basis is used (*reference rate* + 0.5%). ▪ Defines: - Assets (either market value of net assets or assets defined in PBA Regulations; that is, if smoothing creates surplus that otherwise would not exist, it cannot be spent) - Liabilities (includes remaining amortization value) - Current targeted funding amount - Revised targeted funding amount - Reference rate (ensures that smoothed data is not used to get a surplus if there otherwise would not be surplus) **Section 5.02** Sets out that the liabilities are calculated using the distribution basis, plus an adjustment. *Sections 5.03 to 5.05 apply when the plan has a surplus using the distribution basis; that is, there is usable surplus for improving benefits above run-rate permanently or decreasing contributions below target level permanently.* **Section 5.03** Sets out conditions under which Sections 5.04 and 5.05 apply: - If Assets > 110% of Liabilities; and - Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and - Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and - Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.05** The Partners can agree to change benefits or contributions so long as after the change assets remain greater than 110% of the liabilities and a side agreement has been entered into to set out how Minister contributions are adjusted if there is a surplus distribution or temporary improvement of benefits. *Sections 5.06 to 5.08 apply when the plan has a funding ratio that is at least 100% but less than 110% and valued using contribution rates at the basic or target level, full indexing provided prospectively and benefits fully restored.* **Section 5.06** Sets out the conditions under which Sections 5.07 and 5.08 apply: ▪ If Assets ≤ 110% of Liabilities; and ▪ Current Contributions ≤ Basic Contributions (current contributions are equal to or lower than long-term target); and ▪ Current Benefits ≥ Run-Rate Benefits (current benefits are equal to or higher than long-term target); and ▪ Full inflation indexing has been provided prospectively and benefits are fully restored. **Section 5.08** If the conditions in Section 5.06 are satisfied, there is not sufficient surplus to provide a permanent improvement; therefore, Article IV will apply to determine whether there is surplus using the temporary basis.

Subject	Summary of Provisions
Post-December 30, 2017 Valuations (Article VI):	*This section articulates at a high level the use of the surplus credits (earned pre-January 1, 2018) after December 30, 2017. OTF earns surplus credit for any unmatched forgone inflation (i.e., inflation indexing less than 50%) prior to January 1, 2018 or via other benefit reductions made before January 1, 2018. See the JSPP Agreement for more detail.* **Section 6.01** ▪ Restoration basis is used (reference rate + 1.55%). ▪ Defines: - Assets (PBA regulations) - Current Liabilities - Revised Liabilities **Section 6.02** Provides overriding provision for post-December 30, 2017: for valuations where assets are greater than current liabilities, Section 6.03 applies (with reference to the 2013 Term Sheet). **Section 6.03** Sets out the use of surplus credits: ▪ OTF has first call on surplus up to a limit;
Valuation frequency and filing (Article	*This section reinforces an earlier section of the Partners' Agreement that specifies that it is the Partners' joint decision whether to file (other than in a required filing year).* ▪ Partners' decision when to file. ▪ Partners will notify the Board within 7 months of valuation date.
Arbitration (Article VIII):	Refers to Arbitration already in prior section of the Partners' Agreement.
Limitations (Article IX):	FMP does not apply for changes required by law or for changes that increase the liabilities by less than 0.5% or for changes that use the $76m in section 60 *(Note $76m was utilized with January 1, 2008 filing).*

OTPP (recent announcement on indexation increase).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: OTPP (recent announcement on indexation increase)
Date: Sunday, September 18, 2016 18:08:30
Attachment 1: 2016 Valuation - DM Approved Filing Letter.pdf
Attachment 2: 2016 Valuation - Minister Approval DN 2016-08-04.pdf

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Hi Lucy,

I'm attaching some info on the decision announced this week regarding the increase in indexation from 70 to 90%. As you were asking about the share the pain payments, I thought that these docs might provide additional background. n

From: Paul, Joshua (EDU)
Sent: September-13-16 11:40 AM
Subject: AG-OTPP Follow Up
Importance: High

Hello,

This email attempts to follow up in two ways:

1. Provide the documentation the AG requested on the upcoming filing; and

2. Provide the responses to Cindy's questions below.

1. Documentation

Attached are two documents. The first is a Minister's decision note package on the move from 70 to 90. The second is a letter from both partners to the plan providing the direction. Again, this is a decision that has yet to be announced so is highly confidential. The announcement is planned for tomorrow.

The decision note does not highlight how the 8.6 breaks down, but does flag the share the pain issue. If the AG wanted more detail on the 8.6 breakdown, they could go directly to the OTPP.

2. Answers to questions

See below. I would suggest that the current decision is the easiest one to highlight as the 2015 was a bit more complex.

2016 Valuation and Filing

$13.2 billion preliminary funding valuation (as of January 1, 2016).

The $8.6 billion cost of moving to 90% conditional inflation protection is made up primarily of two parts:

1. Approximately $4.3 billion increase in future payments to members, to provide inflation protection at 90% instead of 70%

2. Approximately $4.3 billion reduction in future “share the pain” payments by the Province to the Plan

2015 Valuation and Filing

$6.8 billion preliminary funding valuation (as of January 1, 2015). A $3.7 billion cost of moving to 70% conditional inflation protection made up primarily of two parts:

1. Approximately $1.85 billion increase in future payments to members, to provide inflation protection at 70% instead of 60%

2. Approximately $1.85 billion reduction in future “share the pain” payments by the Province to the Plan

Hope this helps and happy to discuss.

2016 Valuation - DM Approved Filing Letter.pdf

Ministry of Education
Mowat Block
Queen's Park
Toronto, ON M7A 1L2

Ministère de l'Éducation
Édifice Mowat
Queen's Park
Toronto ON M7A 1L2

Ontario Teachers' Federation
Suite 200
1300 Yonge Street
Toronto, ON M4T 1X3

Federation des enseignantes
et des enseignants de l'Ontario
Suite 200, 1300 rue Yonge
Toronto ON M4T 1X3

August 8, 2016

Ron Mock
President and CEO
Ontario Teachers' Pension Plan
5650 Yonge Street
Toronto, ON M2M 4H5

Dear Ron Mock:

Re: Filing of the January 2016 Plan Valuation

The preliminary valuation of the Ontario Teachers' Pension Plan ("the Plan") as at January 1, 2016 indicates that the Plan has a going concern surplus of approximately $13 Billion. Although this valuation is not required to be filed with the Financial Services Commission of Ontario, the Partners have decided that it would be to our mutual advantage to do so.

On account of the surplus and in keeping with the commitment made to Plan members when conditional inflation protection was introduced, we propose that for post-2009 service, inflation protection should be raised to 90 percent starting with the January 1, 2017 adjustment. Further, we propose to restore pensions to the level that would have been payable if full inflation protection had been provided since retirement, also effective January 1, 2017. It is our understanding that both of these measures can be taken within the framework of the available surplus funds.

We request that you instruct the Plan Actuary to prepare a revised valuation based on the Plan amendments outlined above so that this valuation may be filed with the regulator in accordance with the relevant regulations.

We are most grateful to you and your staff for your assistance in filing this valuation.

Yours sincerely,

Francine LeBlanc-Lebel
President
Ontario Teachers' Federation

Nancy Matthews
Deputy Minister
Ministry of Education

FLL/NM/am

2016 Valuation - Minister Approval DN 2016-08-04.pdf

Ontario

Submissions and Documents Review/Approvals Form

Ministry of Education

Title: OTPP 2016 Funding Valuation	Log # 2016 064576	Date Prepared: July 12, 2016	Date Due:
Originated by: Stephen Di Renzo	Tel No. 6-9922	Lead Branch: Education Finance	
Once signed return to: Wendy Samuel	Tel No. 2-1818	Division: FPBD	

Submission Type:	New	Revised	Final
( ) Cabinet Specify Committee: _____	❑	❑	❑
( ) MB20	❑	❑	❑
( ) Legislation/Regulation	❑	❑	❑
(✓) Decision Note	✓	❑	❑
( ) Briefing/Info Note	❑	❑	❑

Document Type:	New	Revised
( ) Letter - Minister's Signature	❑	❑
( ) Letter - Deputy's Signature	❑	❑
( ) Deputy Information Item	❑	❑
( ) Other: _____	❑	❑

Note:

This note seeks approval to file the 2016 funding valuation of the OTPP with the Financial Services Commission of Ontario.

MO Staff were consulted on this item? X Yes No	If yes, who? Sam Andrey and Christopher Humphries
Briefing scheduled? Date: _____ ❑ Minister ❑ Deputy	To be posted on website? ❑ Yes X No

Review/Approval requirements

	R ✓	A ✓	Approving Official	Name	Signature	Date In	Date Out
As Required		✓	Lead Author	S. Di Renzo	S Di Renzo	07-12-16	07-12-16
		✓	Lead Manager	N. Roberto	N. Roberto	07-12-16	07-12-16
			Lead Director	A. Bright	N. Roberto for A. Bright w.d.t	"	"
		✓	Executive Director	J. Paul		July 15	July 15
			CMSD				
			CSIIT				
			ELRD				
			EYD				
			FLALRD				
			FPBD				
			LCD				
			LLED				
			SAD				
Corporate sign-off as required			Director – Comms	M. Leaning			
			Director – Legal	P. Rajan			
			Director – HR	S. Henderson			
Req'd		✓	Lead ADM	G. Sékaly	D. Stewart for G. Sékaly	July 17/16	
		✓	Deputy Minister	N. Matthews	D. Stewart July 17 NM	July 17/16	
As required		✓	Minister's Office Staff	C. Humphries			
		✓	Minister	M. Hunter	MH		

EDU-DMO

Ministry of Education

Mowat Block
Queen's Park
Toronto ON M7A 1L2

Ministère de l'Éducation

Édifice Mowat
Queen's Park
Toronto ON M7A 1L2

Ontario

MEMORANDUM TO: The Honourable Mitzie Hunter
Minister of Education

THROUGH: Nancy Matthews
Deputy Minister

FROM: Gabriel F. Sékaly
Assistant Deputy Minister
Financial Policy and Business

DATE: July 14, 2016

SUBJECT: Funding Valuation of the Ontario Teachers' Pension Plan

---

Attached is a decision note seeking direction to file the 2016 funding valuation of the Ontario Teachers' Pension Plan (OTPP) with the Financial Services Commission of Ontario (FSCO), the Provincial pension plan regulator.

The funding valuation is an assessment of the long-term financial health of the pension plan. The valuation uses a number of assumptions to compare the value of pension plan assets (such as stocks and bonds, as well as future contributions) to the value of pension plan liabilities (the amount required to pay accrued and future pension benefits). Pension plans in Ontario are required under the *Pension Benefits Act* to undertake a valuation annually and file a balanced valuation with FSCO once every three years. A balanced valuation must show that the plan has enough assets to pay out the projected cost of future pension benefits.

It is the responsibility of the OTPP sponsors, the Ontario Teachers' Federation and the Ontario government, to determine when to file the annual valuation with FSCO. The sponsors are also responsible for negotiating the use of any surplus funds and, when there is a funding shortfall, implementing a strategy to eliminate it.

The preliminary valuation of the OTPP as of January 1, 2016 indicates a surplus of about $13.2 billion. This means the pension plan has 107% of the assets it needs to pay future pensions to all members, based on current contribution and benefit levels. The surplus is primarily the result of strong returns on plan investments in 2015. Because the Plan is financially balanced, it is recommended that this valuation be filed with FSCO and that a portion of the surplus be used to continue to restore member benefits. This is consistent with the past two valuation filings, where the sponsors agreed to use surplus to partially restore inflation protection for members in accordance with the Plan's Funding Management Policy.

My staff and I are available to provide you or your staff with further information as required.

Gabriel F. Sékaly,
Assistant Deputy Minister

Attachments (1): Minister's Decision Note

Ministry of Education
MINISTER'S DECISION NOTE

2016 Preliminary Funding Valuation of the
Ontario Teachers' Pension Plan (OTPP)

Confidential Advice to Minister

PURPOSE:

To provide an overview of the OTPP's preliminary valuation as at January 1, 2016 and seek direction to pursue the filing of the valuation, with partially restored inflation protection measures.

KEY INFORMATION:

Valuation of the OTPP

- Each year, the OTPP is required to undergo a funding valuation to determine the status of the plan. The OTPP retains Mercer, a third party actuary, to perform the valuation.
- The funding valuation looks ahead 70+ years to assess the actuarial value of the OTPP's assets and liabilities. Assets are what the pension plan owns (stocks, bonds, real estate, future contributions) while liabilities are the present value of members' and retirees' pension benefits.
    - If the assets are equal to or exceed the liabilities, the plan is financially balanced. An excess of assets represents a surplus, while an excess of liabilities represents a deficit.
- According to the OTPP's preliminary funding valuation (as at January 1, 2016) the Plan has a surplus of about $13.2B with a discount rate of 2.75%. This surplus means the Plan has about 107% of the funds required to meet its long-term pension obligations.
    - The surplus is primarily due to steps the sponsors previously took to adjust plan provisions (i.e. introducing inflation protection conditional on the health of the Plan and special contributions). Without these measures the Plan's funded status would be in deficit.
- The discount rate plays a key role in projecting whether the pension plan has enough assets to meet its future pension obligations by assessing how much the plan's assets can reasonably be expected to earn over the long term. The higher the discount rate, the lower the projected cost of future pensions and vice versa (eg. a 0.25% decrease in the discount rate would increase the projected future pension obligation by about $7B).
    - For the 2014 valuation, the discount rate was increased from 2.75% to 2.85% in acknowledgement of the aforementioned steps taken by the sponsors, which improved the sustainability of the Plan. This discount rate was maintained in 2015.
    - For the 2016 valuation, the Plan has reduced the discount rate back to 2.75% given the volatile global investment outlook and the plan's demographic profile.

Restoring Inflation Protection

- Conditional Inflation Protection (CIP) was first introduced in 2008 as a lever to give the sponsors the ability to manage deficits by decreasing inflation protection on pension payments for future service. Under these provisions:

    - Service accrued prior to 2010 fully inflation protected; and
    - Service accrued after 2009 is subject to conditional inflation protection:
        - Inflation protection for service accrued during 2010-2013 is guaranteed at 50% and can be adjusted upwards to 100% depending on the financial status of the plan; and
        - Inflation protection for service accrued after 2013 is not guaranteed. CIP can be adjusted upwards to 100% or downwards to 0% depending on the financial status of the plan.
- It is the stated intention of the sponsors that inflation protection will be reinstated as the funded status of the OTPP improves. Consistent with this commitment, last year's preliminary surplus was used to restore inflation protection from 60% to 70% beginning in 2016.
    - The sponsors also decided to restore the level of base pensions, for the purposes of future CIP calculations, to what would have been payable if full inflation protection had been provided since retirement (known as restoring the run-rate).
- The sponsors propose to use a portion of this year's surplus to partially restore inflation protection to 90% and restore the run rate. This change would begin in 2017 and would remain in place until the next funding valuation is filed.
    - The OTF have indicated that they are not willing to file the valuation with CIP at 85% or lower. The OTPP is supportive of filing the valuation with the CIP increase to 90%, but cautioned the sponsors that should the plan experience future deficits, they would be forced to make changes (invoke further CIP again and/or increase contributions).

<u>Filing the January 1, 2016 Valuation</u>

- The *Pension Benefits Act* (PBA) requires a valuation to be filed with the Financial Services Commission of Ontario (FSCO), the government regulator responsible for overseeing the insurance and pension industries, at least once every 3 years.
- The OTPP last filed a valuation with the FSCO as of January 1, 2015. This means that the OTPP could either:
    - voluntarily file the valuation as of January 1, 2016 or 2017; or
    - file a mandatory valuation as of January 1, 2018.
- As co-sponsors of the OTPP, the government and the Ontario Teachers' Federation (OTF) must jointly decide on whether or not to file.
    - The OTF have indicated that they support filing the January 1, 2016 valuation and using part of the surplus to provide inflation protection at 90% for the period starting January 1, 2017 until the next valuation is filed.
    - Should the decision be made to file this year, the sponsors have until September 30, 2016 to officially file the valuation. To meet that legislated deadline, OTPP would need a decision in writing by September 1, 2016 to give Mercer sufficient time to prepare the formal valuation report.
- Filing this year's valuation would ensure that there is adequate time to continue to monitor the funded status of the OTPP, develop plans to address any potential shortfalls that arise over the next three years, and consult with OTPP members about their preferences before changes to pension benefits are made.

RISK SUMMARY:

- **Medium.** Filing the January 1, 2016 valuation and partially restoring inflation protection will likely be positively received by teachers and federations. However, should 2016 and beyond result in lower investment returns, the CIP lever could be reduced again to maintain the Plan's financial health and may be met with objection from teachers and federations.

RISK ANALYSIS:

Risk Factor	Context	Level of Risk	Mitigating Factor
Increase in benefits may have to be clawed back if there is a shortfall in the next filing.	When filed with FSCO, the valuation must show that the pension plan is balanced. If there is a deficit, the filing must outline actions that will be taken to address the shortfall and balance the plan, through increasing contribution rates or adjusting the accrual of pension benefits for future years. If there is a shortfall in the next filing, OTPP may have to reduce CIP again to balance the plan.	Medium	CIP is an established Plan provision that has been consistently invoked by the sponsors to keep the plan viable and affordable in the long-term. The sponsors have also honoured their commitment to restore inflation protection as the funded status of the Plan has improved.

FINANCIAL IMPLICATIONS:

- Providing inflation protection at 90% from 70% would cost approximately $8.6B of the Plan's identified surplus.
- OTPP contributions will continue to be frozen at the current rate until December 30, 2017, the end of the contribution freeze period in the Jointly Sponsored Pension Plans (JSPP) agreement.
- Providing inflation protection at 90% will mean the government will continue to make "sharing the pain" payments to OTPP.
    - As part of the 2008 agreement to introduce CIP, the government agreed to a "sharing the pain" provision. The provision states that for years where members receive less than 100% inflation protection, the government is required to make additional contributions to the Plan equal to the amount forgone by members. Contributions are made up to 50% for CIP on service accrued after 2013 (e.g. if CIP for this period was 40% the government is required to make additional contributions at 50%, not 60%).

COMMUNICATIONS STRATEGY:

- An OTPP Communications Working Group (CWG) made up of members of OTF, the Government and the OTPP is responsible for drafting the joint announcement of the valuation results.
- Once developed, the announcement will go through the appropriate approvals.
- The approach will follow the practices used for most filing announcements since the formation of CWG in 2009.

NEXT STEPS:

- Sponsors meet to confirm agreement on valuation terms as detailed above.
- If the sponsors decide to file the 2016 valuation, they will send a joint letter to the OTPP directing them to have the actuaries prepare a revised valuation based on the terms detailed above (i.e. partially restore inflation protection measures, and restore the run rate). The Plan would then file the revised valuation with FSCO.
    - Ministry staff will seek Ministerial approval of this letter once the valuation terms have been confirmed.

OPTIONS:

- Option 1: Direct the OTPP to file the January 1, 2016 valuation and restore inflation protection measures as described above. **(Recommended)**
- Option 2: Do not file the January 1, 2016 valuation of the OTPP.

PREPARED BY: Stephen Di Renzo
Senior Policy Coordinator
Education Finance Branch
(416) 326-9922

APPROVED BY: Joshua Paul
Executive Director
Fiscal & Financial Planning
(416) 327-9060

OPTION 1: Direct the OTPP to file the January 1, 2016 valuation and restore inflation protection measures as described above. (Recommended)

☑ Agree/Approve ☐ Do Not Agree/Approve

OPTION 2: Do not file the January 1, 2016 valuation of the OTPP.

☐ Agree/Approve ☐ Do Not Agree/Approve

The Honourable Mitzie Hunter

Aug. 2, 2016
Date

OTPP - accrued benefit asset recognition.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Uros Karadzic [uros.karadzic@ca.ey.com]; Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: OTPP - accrued benefit asset recognition
Date: Thursday, March 30, 2017 15:18:32
Attachment 1: image002.jpg
Attachment 2: OTPP Recognition of accrued benefit asset (EY 30 March 2017).pdf

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Hi Nadine,

Attached is a draft version of our letter related to the accrued benefit asset recognition (i.e. asset ceiling analysis) for OTPP for your review. Let us know if you have any comments or concerns. We welcome a meeting/call to discuss.

Upon confirming the letter is satisfactory, we will follow up with a similar letter for OPSEU.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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Any tax advice in this e-mail should be considered in the context of the tax services we are providing to you. Preliminary tax advice should not be relied upon and may be insufficient for US penalty protection. Tout conseil de fiscalité contenu dans le présent courriel doit être pris dans le contexte des services de fiscalité que nous vous offrons. Aucune décision ou position ne doit être prise à la lumière de conseils de fiscalité préliminaires, lesquels pourraient ne pas permettre d'éviter des pénalités aux États-Unis.

image002.pdf

EY

OTPP Recognition of accrued benefit asset (EY 30 March 2017).pdf

Ernst & Young LLP
Ernst & Young Tower
222 Bay Street, PO Box 251
Toronto, ON M5K 1J7

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Nadine Petsche
Director, Accounting Policy and Financial Reporting
Office of the Provincial Controller Division
7 Queen's Park Crescent, 2nd Floor
Toronto ON M7A 1Y7

30 March 2017

Ontario Teacher's Pension Plan - DRAFT
Accrued benefit asset recognition

The Office of the Provincial Controller Division ("OPCD") has asked EY to provide pension accounting support with the preparation of financial statements for the Province of Ontario (the "Province"). This document has been prepared to determine the extent to which an accrued benefit asset may be recognized as at 31 March 2017 in respect of the Province's share of the Ontario Teachers' Pension Plan ("OTPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").

As at 31 March 2017, prior to any valuation allowance (if any), OPCD determined the followings:

- Plan's accrued benefit asset is $26.9B (obligation of $123.8, market related-value of asset of $169.8B, unamortized actuarial gain of $19.1B)
- The Province's portion (50%) of the accrued benefit asset is $12.3B[1]

Our analysis determined that a valuation allowance is not required at 31 March 2017 and the Province's portion of the accrued benefit asset of $12.3B in respect of the Plan may be recognized as an asset without any impairment.

1 Background Information

1.1 Key characteristics of the Plan

Following key characteristics of the Plan are most relevant to our analysis:

- The Plan a Joint Defined Benefit Plan ("JDBP") under PSAS. The Plan is jointly sponsored by the Province, through the Minister of Education, and the Ontario Teachers' Federation ("OTF"), representing the employees.
- The Province's portion of the Plan is 50% of the overall Plan, reflecting the sharing principle between the sponsors under the Teacher's Pension Act ("Act").
- Funding valuations must be filed at least once every three years. If there is a surplus/deficiency on a funding valuation basis, the joint sponsors must negotiate and agree to changes in future contribution levels or benefit levels to result in an actuarially balanced valuation.

[1] reflects specific downward net adjustment of $1.2B by OPCD to the Province's portion of the Plan for the Province's financial statements

- Changes to contribution levels and benefit levels must reflect the sharing principle in that each joint sponsor is responsible for their share of deficit or entitled to their share of surplus.
- The Act or the Plan documents do not prohibit contribution holidays (i.e. surpluses belonging to the joint sponsors may be applied to reduce contributions).

1.2 Assumptions for financial reporting

The following highlights key assumptions applied for the valuation of the obligation and costs at 31 March 2017 for the purpose of Province's financial statements. The assumptions represent best estimate assumptions, selected by the Province:

- The Province's financial statement year-end reporting is as at 31 March 2017 (the "measurement date")
- The measurement of assets and obligations are as at 31 December 2016 (this earlier measurement date is permitted under PSAS 3250.039)
- Assumed inflation protection for post-2009 service will be provided at 100% of the assumed inflation rate
- Valuation discount rate: 6.00%
- Inflation rate: 2.00%
- Salary escalation rate: 2.00% per annum to 2019 and 2.75% thereafter

2 Considerations for the accrued benefit asset recognition

PSAS contains relevant guidance for recognition of an accrued benefit asset in respect of the Province's share of the Plan at 31 March 2017. We have considered the guidance under PS 3250 relating to recognition the recognition of an accrued benefit asset based on an expected future benefit available to the Province, in the context of JDBP.

Joint Defined Benefit Plans

PS 3250.081 states "*when a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.*"

The Province has an equal share (50%) in the costs and risks of the OTPP. Both entitlement to any surplus and responsibility for any deficiency are shared equally between the Province and employee sponsor. The determination of a net asset or liability (and valuation allowance, if applicable) is therefore performed on an aggregate Plan basis, and the Province's portion of that asset/liability is determined subsequently by applying 50% portion to the Province.

Province's ability to benefit from an accrued benefit asset

PS 3250.050 states "*an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the*

expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs".

PS 3250.052 states "*a government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. The accrued benefit asset may become impaired when there is a plan surplus for accounting purposes that the government is not entitled to benefit from fully. For example, there may be a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus*".

The Province is only able to recognize an accrued benefit asset to the extent that they are able to derive an expected future benefit from such asset. As per PS 3250.052, an expected future benefit may arise from (i) withdrawal of surplus or (ii) by taking a contribution holiday or receiving a refund of contributions. Based on Ontario case law and the Ontario Pension Benefits Act ("PBA"), it is difficult to establish the right of a plan sponsor to withdraw surplus. For purposes of determining the expected future benefit, our assumption is that the Province does not have a right to surplus withdrawal. However, contribution holidays are permitted by the Ontario PBA and the Plan documents. As such, the Province has access to an expected future benefit through future contribution reductions. The Funding Management Policy sets out an agreed upon framework of priorities for the sponsors in jointly determining how any funding surpluses can be utilized. The sponsors may negotiate lower contributions or an increase in benefits. There is no minimum level of contribution requirements set out by the Plan and contributions levels are negotiated. Therefore, the joint sponsors can each benefit from their respective portion of plan surplus for accounting purposes.

3 Determination of the accrued benefit asset recognition

This section provides details on the determination of the accrued benefit asset in respect of the Plan. Based on PS 3250.50 to 3250.059 (Limit on the carrying amount on accrued benefit asset), we have estimated the adjusted benefit asset, the expected future benefit, the valuation allowance, and the accrued benefit asset (net of valuation allowance) to be recognized by the Province under PSAS as at 31 March 2017.

3.1 Adjusted benefit asset

PS 3250.053 states "*To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset. The adjusted benefit asset is the accrued benefit asset less net unamortized actuarial losses (determined on a basis using market value of assets)*".

Based on the financial information for the Plan as at the measurement date provided by OPCD, we have determined the unamortized actuarial gains/losses for the Plan on a basis using the market value of assets as follows:

Market value of assets ("MVA")	$175.6B
Market-related value of assets ("MVRA")	$(169.8)B
Actuarial gains/losses not recognized due to smoothing	$5.8B
Unamortized actuarial gains/(losses), on MRVA basis	$19.1B
Unamortized actuarial gains/(losses), on MVA basis	$24.9B

As there is an unamortized actuarial gain (determined on a basis using market value of assets), the adjusted benefit asset is equal to the Plan's surplus position on a market basis:

Market value of assets	$175.6B
Obligation	$(123.8)B
Plan surplus	$51.8B
Unamortized losses	$0.0B
Adjusted benefit asset (PS 3250.053)	$51.8B

The adjusted benefit asset for the Plan is $51.8B.

3.2 Expected future benefit

PS 3250.56 states **"***a government determines its expected future benefit the sum of:*

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

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

Present value of the Plan's expected future accruals

PS 3250.57 further states "*A government's expected future accruals for service for the current number of active employees are determined on a basis consistent with that used to determine its accrued benefit obligation…"*

Mercer's accounting results letter determined the following using the Province's assumptions for financial reporting under PSAB:

- The 2017 total service cost is $3.1B
- The total present value of expected future accruals is $100.1B as at 31 December 2016

Mercer also noted the present value of expected future accruals has been calculated on an open group basis using a perpetuity approach (i.e. the current number of active employees), by projecting the current service cost with the assumed salary scale and discounting with interest. This is in line with PSAS requirements.

We have validated Mercer's calculation of the total present value of expected future accruals of $100.1B. We have estimated the present value of the Plan's expected future accruals to be approximately $95B, based on the current number of active employees and the province's assumptions for financial reporting under PSAB as at the measurement date:

- Annual salary increase of 2.75% (ultimate rate)

- Discount rate of 6.00%

Our estimate of the present value of expected future accrual has been determined as follows: 2017 current service cost / (discount rate – ultimate rate of salary increase) = $3.1B / (0.06-0.0275) = $95B.

We note that our estimate is approximately $5B lower than the amount determined by the actuary. The actuary's result is likely more refined; however, the use of either figure will result in a valuation allowance of nil as the expected benefit exceeds the adjusted benefit asset. Therefore, we have not followed up with the actuaries to reconcile this difference.

Minimum contributions the Province is required to make regardless of any surplus

As there is no fixed contribution (as a percentage or dollar amount) requirement which is independent of the Plan's funding status, our interpretation is that there are no contributions that the Province is required to make, regardless of any surplus. The sponsors of the Plan can agree to any level of contribution through negotiation that leads to an actuarially balanced funding valuation. The Plan's funding level has an impact on the contribution rates, i.e. they are made with consideration for the Plan's funding surplus. Further, there is no minimum level of contribution required "regardless of any surplus". This interpretation is consistent with the interpretation we see applied in practice for other Canadian plan sponsors reporting under PSAS.

Present value of the required employee contributions

We note that PS 3250.056 is written in the context of a single sponsor Plan while the OTPP is a joint-sponsored Plan. As such, the present value of the required employee contributions for OTPP is nil (i.e. the employee contributions being referenced by PS 3250.056 is in respect to contributions made by employees who are not sponsor of the Plan).

Plan surplus that can be withdrawn

As discussed in Section 2, we have assumed no Plan surplus can be withdrawn by the joint sponsors.

Expected future benefit

Using the actuary's estimate of the present value of the Plan's expected future accruals, the expected future benefit for the Plan is the present value of the Plan's expected future accruals:

Present value of the Plan's expected future accruals (PS 3250.57)	$100.1B
Present value of the required employee contributions (PS 3250.056a)	(0.0)B
Minimum required contributions regardless of any surplus (PS 3250.056a)	(0.0)B
Plan surplus that can be withdrawn (PS 3250.056b)	(0.0)B
Expected future benefit (PS 3250.056)	$100.1B

The Plan's expected future benefit is $100.1B.

3.3 Valuation allowance

PS 3250.054 states "*the adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required*".

Per 3.1 and 3.2 of this letter, we have determined that the Plan's expected future benefit exceeds the Plan's adjusted benefit asset:

Plan's adjusted benefit asset (PS 3250.053)	$51.8B
Plan's expected future benefit (PS 3250.056)	$100.1B
Valuation allowance (PS 3250.054) [max (0, $51.8B – 100.1B)]	$0.0B

The Plan's accrued benefit asset is not impaired, and accordingly, no valuation allowance is required.

3.4 Accrued benefit asset recognition

The Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Accrued benefit asset	$26.9B
Valuation allowance (PS3250.054)	0.0B
Accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B

Accordingly, the Province's portion of the Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Plan's accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B
Province's portion of the accrued benefit asset (50%) [PS3250.050 x 50%]	13.5B
Other Province specific adjustment made by OPCD	(1.2)B
Accrued benefit asset to be recognized by the Province (PS3250.050)	$12.3B

The accrued benefit asset of $12.3B without any asset impairment should be recognized for the Province's financial reporting under PSAB.

Appendix
Information Provided

Our analysis is based on the following information we received:

- Actuarial valuation report for OTPP as at 1 January 2016 prepared by Mercer for funding purposes
- Analysis of Pension Asset ceiling Accounting Considerations for the Office of the Provincial Controller Division re; Ontario Teachers' Pension Plan prepared by Deloitte for 31 March 2015 financial reporting
- Teachers' Pension Act
- OTPP Funding Management Policy
- Letter Re: Accounting results as at 31 March 2017 prepared by Mercer

Appendix
Applicable guidance under PS 3250

Measurement date

.39 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Limit on the carrying amount on accrued benefit asset

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

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

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

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

.54 The adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required.

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

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

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

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

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

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

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

Joint defined benefit plans

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

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

accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.

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

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

Glossary

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

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

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

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

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

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

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

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

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

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

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

benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.

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From: []
To:
Subject: OTPP Recognition of accrued benefit asset
Date:

Subject:	OTPP Recognition of accrued benefit asset
Location:	teleconference 416 246 7171 passcode 1474532#
Start:	Wed 05/10/2017 3:00 PM
End:	Wed 05/10/2017 3:30 PM
Recurrence:	(none)
Meeting Status:	Meeting organizer
Organizer:	Virani, Shyrose (TBS)
Required Attendees:	Virani, Shyrose (TBS); Petsche, Nadine (TBS); Patel, Bharat (TBS); Fong, Pauline (TBS); Li, Wendy (TBS); Sun, Alicia (TBS); Ma, Patricia (TBS); Shayan Jafrani; christina.chan@ca.ey.com
Optional Attendees:	Uros Karadzic; Veinot, Cindy (TBS) (Cindy.Veinot@ontario.ca)

Nadine to moderate

OTPP Recognition of accrued benefit asset .rtf

From: Petsche, Nadine (TBS) []
To: Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]; shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: OTPP Recognition of accrued benefit asset
Date: Monday, April 03, 2017 12:01:07
Attachment 1: OTPP Recognition of accrued benefit asset (EY 30 March 2017)np.docx

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Hi Christina and Shayan.

Thanks for sharing the draft analysis on OTPP. I was hoping you might be available for a 15 minute call later today or tomorrow to discuss my comments (attached) and next steps.

Shyrose can help to set up a time to chat.

Thanks.

Nadine

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Ernst & Young LLP
Ernst & Young Tower
222 Bay Street, PO Box 251
Toronto, ON M5K 1J7

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Nadine Petsche
Director, Accounting Policy and Financial Reporting
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Toronto ON M7A 1Y7

April XX, 2017

Ontario Teacher's Pension Plan - DRAFT
Accrued benefit asset recognition

The Office of the Provincial Controller Division ("OPCD") has asked EY to undertake an asset ceiling test to inform OPCD's decision as to whether a valuation allowance is required in relation to the Province's share of the Ontario Teachers' Pension Plan ("OTPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").
~~provide pension accounting support with the preparation of financial statements for the Province of Ontario (the "Province").~~ This document provides the results of our analysis and recommendations to OPCD management regardgin the ~~has been prepared to determine the~~recognition of ~~extent to which~~ an accrued benefit asset for OTPP ~~may be recognized~~ as at 31 March 2017. ~~in respect of the Province's share of the Ontario Teachers' Pension Plan ("OTPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").~~

As at 31 March 2017, prior to considering the possible need for a~~any~~ valuation allowance ~~(if any)~~, OPCD determined the followings:

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- The Province's portion (50%) of the accrued benefit asset is $12.3B[1]

Since o~~O~~ur analysis determined that a valuation allowance is not required at 31 March 2017, ~~and~~it would appear appropriate to report the Province's portion of the accrued benefit asset of $12.3B for it's respective potion of the plan ~~in respect of the Plan may be recognized as an asset without any impairment~~.

1 Background Information

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Following key characteristics of the Plan are most relevant to our analysis:

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Commented [npp1]: May wish to highlight the relevance of this requirement w.r.t. negating possibility of minimum contributions

[1] reflects specific downward net adjustment of $1.2B by OPCD to the Province's portion of the Plan for the Province's financial statements

- Changes to contribution levels and benefit levels must reflect the sharing principle in that each joint sponsor is responsible for their share of deficit or entitled to their share of surplus.
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The following highlights key assumptions applied for the valuation of the obligation and costs at 31 March 2017 for the purpose of Province's financial statements. The assumptions represent best estimate assumptions, selected by the Province:

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- The measurement of assets and obligations are as at 31 December 2016 (this earlier measurement date is permitted under PSAS 3250.039)
- Assumed inflation protection for post-2009 service will be provided at 100% of the assumed inflation rate
- Valuation discount rate: 6.00%
- Inflation rate: 2.00%
- Salary escalation rate: 2.00% per annum to 2019 and 2.75% thereafter

Commented [npp2]: Does EY wish to include reference/comments regarding stub period considerations by OPCD? See Pauline/Bharat for history of OAG comments.

2 Considerations for the accrued benefit asset recognition

PSAS contains relevant guidance for recognition of an accrued benefit asset in respect of the Province's share of the Plan at 31 March 2017. We have considered the guidance under PS 3250 relating to recognition ~~the recognition~~ of an accrued benefit asset based on an expected future benefit available to the Province, in the context of accounting for a JDBP under PS3250.

Joint Defined Benefit Plans

PS 3250.081 states "*when a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.*"

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3.1 Adjusted benefit asset

PS 3250.053 states "*To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset. The adjusted benefit asset is the accrued benefit asset less net unamortized actuarial losses (determined on a basis using market value of assets)*".

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As there is an unamortized actuarial gain (determined on a basis using market value of assets), the adjusted benefit asset is equal to the Plan's surplus position on a market basis:

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

Present value of the Plan's expected future accruals

PS 3250.57 further states "*A government's expected future accruals for service for the current number of active employees are determined on a basis consistent with that used to determine its accrued benefit obligation…"*

Mercer's accounting results letter determined the following using the Province's assumptions for financial reporting under PSAB:

- The 2017 total service cost is $3.1B
- The total present value of expected future accruals is $100.1B as at 31 December 2016

Mercer also noted the present value of expected future accruals has been calculated on an open group basis using a perpetuity approach (i.e. the current number of active employees), by projecting the current service cost with the assumed salary scale and discounting with interest. This is in line with PSAS requirements.

We have validated Mercer's calculation of the total present value of expected future accruals of $100.1B. We have estimated the present value of the Plan's expected future accruals to be approximately $95B, based on the current number of active employees and the province's assumptions for financial reporting under PSAB as at the measurement date:

- Annual salary increase of 2.75% (ultimate rate)

- Discount rate of 6.00%

Our estimate of the present value of expected future accrual has been determined as follows: 2017 current service cost / (discount rate – ultimate rate of salary increase) = $3.1B / (0.06-0.0275) = $95B.

We note that our estimate is approximately $5B lower than the amount determined by the actuary. The actuary's result is likely more refined; however, the use of either figure will result in a valuation allowance of nil as the expected benefit exceeds the adjusted benefit asset. Therefore, we have not followed up with the actuaries to reconcile this difference.

Minimum contributions the Province is required to make regardless of any surplus

As there is no fixed contribution (as a percentage or dollar amount) requirement which is independent of the Plan's funding status, our interpretation is that there are no contributions that the Province is required to make, regardless of any surplus. The sponsors of the Plan can agree to any level of contribution through negotiation that leads to an actuarially balanced funding valuation. The Plan's funding level has an impact on the contribution rates, i.e. they are made with consideration for the Plan's funding surplus. Further, there is no minimum level of contribution required "regardless of any surplus". This interpretation is consistent with the interpretation we see applied in practice for other Canadian plan sponsors reporting under PSAS.

Commented [npp3]: See note above. To discuss.

Present value of the required employee contributions

We note that PS 3250.056 is written in the context of a single sponsor Plan while the OTPP is a joint-sponsored Plan. As such, the present value of the required employee contributions for OTPP is nil (i.e. the employee contributions being referenced by PS 3250.056 is in respect to contributions made by employees who are not sponsor of the Plan).

Plan surplus that can be withdrawn

As discussed in Section 2, we have assumed no Plan surplus can be withdrawn by the joint

sponsors. Expected future benefit

Using the actuary's estimate of the present value of the Plan's expected future accruals, the expected future benefit for the Plan is the present value of the Plan's expected future accruals:

Present value of the Plan's expected future accruals (PS 3250.57)	$100.1B
Present value of the required employee contributions (PS 3250.056a)	(0.0)B
Minimum required contributions regardless of any surplus (PS 3250.056a)	(0.0)B
Plan surplus that can be withdrawn (PS 3250.056b)	(0.0)B
Expected future benefit (PS 3250.056)	$100.1B

The Plan's expected future benefit is $100.1B.

3.3 Valuation allowance

PS 3250.054 states "*the adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required*".

Per 3.1 and 3.2 of this letter, we have determined that the Plan's expected future benefit exceeds the Plan's adjusted benefit asset:

Plan's adjusted benefit asset (PS 3250.053)	$51.8B
Plan's expected future benefit (PS 3250.056)	$100.1B
Valuation allowance (PS 3250.054) [max (0, $51.8B – 100.1B)]	$0.0B

The Plan's accrued benefit asset is not impaired, and accordingly, no valuation allowance is required.

3.4 Accrued benefit asset recognition

The Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Accrued benefit asset	$26.9B
Valuation allowance (PS3250.054)	0.0B
Accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B

Accordingly, the Province's portion of the Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Plan's accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B
Province's portion of the accrued benefit asset (50%) [PS3250.050 x 50%]	13.5B
Other Province specific adjustment made by OPCD	(1.2)B
Accrued benefit asset to be recognized by the Province (PS3250.050)	$12.3B

The accrued benefit asset of $12.3B without any asset impairment should be recognized for the Province's financial reporting under PSAB.

Commented [npp4]: Let's discuss

Appendix
Information Provided

Our analysis is based on the following information we received:

- Actuarial valuation report for OTPP as at 1 January 2016 prepared by Mercer for funding purposes
- Analysis of Pension Asset ceiling Accounting Considerations for the Office of the Provincial Controller Division re; Ontario Teachers' Pension Plan prepared by Deloitte for 31 March 2015 financial reporting
- Teachers' Pension Act
- OTPP Funding Management Policy
- Letter Re: Accounting results as at 31 March 2017 prepared by Mercer
-

Commented [npp5]: Let's discuss

Appendix
Applicable guidance under PS 3250

Measurement date

.39 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Limit on the carrying amount on accrued benefit asset

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

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

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

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

.54 The adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required.

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

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

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

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

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

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

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

Joint defined benefit plans

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

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

accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.

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

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

Glossary

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

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

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

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

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

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

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

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

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

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

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

benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.

OTPP Recognition of accrued benefit asset .rtf

From: Petsche, Nadine (TBS) []
To: Christina Chan (Christina.Chan@ca.ey.com) [Christina.Chan@ca.ey.com]; shayan.jafrani@ca.ey.com [shayan.jafrani@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: OTPP Recognition of accrued benefit asset
Date: Monday, April 03, 2017 12:01:07
Attachment 1: OTPP Recognition of accrued benefit asset (EY 30 March 2017)np.docx

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Hi Christina and Shayan.

Thanks for sharing the draft analysis on OTPP. I was hoping you might be available for a 15 minute call later today or tomorrow to discuss my comments (attached) and next steps.

Shyrose can help to set up a time to chat.

Thanks.

Nadine

OTPP Recognition of accrued benefit asset (EY 30 March 2017)np.pdf

Ernst & Young LLP
Ernst & Young Tower
222 Bay Street, PO Box 251
Toronto, ON M5K 1J7

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Nadine Petsche
Director, Accounting Policy and Financial Reporting
Office of the Provincial Controller Division
7 Queen's Park Crescent, 2nd Floor
Toronto ON M7A 1Y7

April XX, 2017

Ontario Teacher's Pension Plan - DRAFT
Accrued benefit asset recognition

The Office of the Provincial Controller Division ("OPCD") has asked EY to undertake an asset ceiling test to inform OPCD's decision as to whether a valuation allowance is required in relation to the Province's share of the Ontario Teachers' Pension Plan ("OTPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").
~~provide pension accounting support with the preparation of financial statements for the Province of Ontario (the "Province").~~ This document provides the results of our analysis and recommendations to OPCD management regardgin the ~~has been prepared to determine the~~recognition of ~~extent to which~~ an accrued benefit asset for OTPP ~~may be recognized~~ as at 31 March 2017. ~~in respect of the Province's share of the Ontario Teachers' Pension Plan ("OTPP", or the "Plan") under the Public Sector Accounting Standards ("PSAS").~~

As at 31 March 2017, prior to considering the possible need for a~~any~~ valuation allowance ~~(if any)~~, OPCD determined the followings:

- Plan's accrued benefit asset is $26.9B (obligation of $123.8, market related-value of asset of $169.8B, unamortized actuarial gain of $19.1B)
- The Province's portion (50%) of the accrued benefit asset is $12.3B[1]

Since o~~O~~ur analysis determined that a valuation allowance is not required at 31 March 2017, ~~and~~it would appear appropriate to report the Province's portion of the accrued benefit asset of $12.3B for it's respective potion of the plan ~~in respect of the Plan may be recognized as an asset without any impairment~~.

1 Background Information

1.1 Key characteristics of the Plan

Following key characteristics of the Plan are most relevant to our analysis:

- The Plan is a Joint Defined Benefit Plan ("JDBP") under PSAS. The Plan is jointly sponsored by the Province, through the Minister of Education, and the Ontario Teachers' Federation ("OTF"), representing the employees.
- The Province's portion of the Plan is 50% of the overall Plan, reflecting the sharing principle between the sponsors under the Teacher's Pension Act ("Act").
- Funding valuations must be filed at least once every three years. If there is a surplus/deficiency on a funding valuation basis, the joint sponsors must negotiate and agree to changes in future contribution levels or benefit levels to result in an actuarially balanced valuation.

Commented [npp1]: May wish to highlight the relevance of this requirement w.r.t. negating possibility of minimum contributions

[1] reflects specific downward net adjustment of $1.2B by OPCD to the Province's portion of the Plan for the Province's financial statements

- Changes to contribution levels and benefit levels must reflect the sharing principle in that each joint sponsor is responsible for their share of deficit or entitled to their share of surplus.
- The Act or the Plan documents do not prohibit contribution holidays (i.e. surpluses belonging to the joint sponsors may be applied to reduce contributions).

1.2 Assumptions for financial reporting

The following highlights key assumptions applied for the valuation of the obligation and costs at 31 March 2017 for the purpose of Province's financial statements. The assumptions represent best estimate assumptions, selected by the Province:

- The Province's financial statement year-end reporting is as at 31 March 2017 (the "measurement date")
- The measurement of assets and obligations are as at 31 December 2016 (this earlier measurement date is permitted under PSAS 3250.039)
- Assumed inflation protection for post-2009 service will be provided at 100% of the assumed inflation rate
- Valuation discount rate: 6.00%
- Inflation rate: 2.00%
- Salary escalation rate: 2.00% per annum to 2019 and 2.75% thereafter

Commented [npp2]: Does EY wish to include reference/comments regarding stub period considerations by OPCD? See Pauline/Bharat for history of OAG comments.

2 Considerations for the accrued benefit asset recognition

PSAS contains relevant guidance for recognition of an accrued benefit asset in respect of the Province's share of the Plan at 31 March 2017. We have considered the guidance under PS 3250 relating to recognition ~~the recognition~~ of an accrued benefit asset based on an expected future benefit available to the Province, in the context of accounting for a JDBP under PS3250.

Joint Defined Benefit Plans

PS 3250.081 states "*when a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.*"

The Province has an equal share (50%) in the costs and risks of the OTPP. Both entitlement to any surplus and responsibility for any deficiency are shared equally between the Province and employee sponsor. The determination of a net asset or liability (and valuation allowance, if applicable) is therefore performed on an aggregate Plan basis, and the Province's portion of that asset/liability is determined subsequently by applying 50% portion to the Province.

Province's ability to benefit from an accrued benefit asset

PS 3250.050 states "*an accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the*

expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs".

PS 3250.052 states "*a government may benefit from an accrued benefit asset either by withdrawing surplus assets or by taking a contribution holiday or receiving a refund of contributions. The accrued benefit asset may become impaired when there is a plan surplus for accounting purposes that the government is not entitled to benefit from fully. For example, there may be a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus*".

The Province is only able to recognize an accrued benefit asset to the extent that they are able to derive an expected future benefit from such asset. As per PS 3250.052, an expected future benefit may arise from (i) withdrawal of surplus or (ii) by taking a contribution holiday or receiving a refund of contributions. Based on Ontario case law and the Ontario Pension Benefits Act ("PBA"), it is difficult to establish the right of a plan sponsor to withdraw surplus. For purposes of determining the expected future benefit, our assumption is that the Province does not have a right to surplus withdrawal. However, contribution holidays are permitted by the Ontario PBA and the Plan documents. As such, the Province has access to an expected future benefit through future contribution reductions. The Funding Management Policy sets out an agreed upon framework of priorities for the sponsors in jointly determining how any funding surpluses can be utilized. The sponsors may negotiate lower contributions or an increase in benefits. There is no minimum level of contribution requirements set out by the Plan and contributions levels are negotiated. Therefore, the joint sponsors can each benefit from their respective portion of plan surplus for accounting purposes.

3 Determination of the accrued benefit asset recognition

This section provides details on the determination of the accrued benefit asset in respect of the Plan. Based on PS 3250.50 to 3250.059 (Limit on the carrying amount on accrued benefit asset), we have estimated the adjusted benefit asset, the expected future benefit, the valuation allowance, and the accrued benefit asset (net of valuation allowance) to be recognized by the Province under PSAS as at 31 March 2017.

3.1 Adjusted benefit asset

PS 3250.053 states "*To determine the extent to which an accrued benefit asset may be impaired, the government first determines the adjusted benefit asset. The adjusted benefit asset is the accrued benefit asset less net unamortized actuarial losses (determined on a basis using market value of assets)*".

Based on the financial information for the Plan as at the measurement date provided by OPCD, we have determined the unamortized actuarial gains/losses for the Plan on a basis using the market value of assets as follows:

Market value of assets ("MVA")	$175.6B
Market-related value of assets ("MVRA")	$(169.8)B
Actuarial gains/losses not recognized due to smoothing	$5.8B
Unamortized actuarial gains/(losses), on MRVA basis	$19.1B
Unamortized actuarial gains/(losses), on MVA basis	$24.9B

As there is an unamortized actuarial gain (determined on a basis using market value of assets), the adjusted benefit asset is equal to the Plan's surplus position on a market basis:

Market value of assets	$175.6B
Obligation	$(123.8)B
Plan surplus	$51.8B
Unamortized losses	$0.0B
Adjusted benefit asset (PS 3250.053)	$51.8B

The adjusted benefit asset for the Plan is $51.8B.

3.2 Expected future benefit

PS 3250.56 states **"***a government determines its expected future benefit the sum of:*

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

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

Present value of the Plan's expected future accruals

PS 3250.57 further states "*A government's expected future accruals for service for the current number of active employees are determined on a basis consistent with that used to determine its accrued benefit obligation…"*

Mercer's accounting results letter determined the following using the Province's assumptions for financial reporting under PSAB:

- The 2017 total service cost is $3.1B
- The total present value of expected future accruals is $100.1B as at 31 December 2016

Mercer also noted the present value of expected future accruals has been calculated on an open group basis using a perpetuity approach (i.e. the current number of active employees), by projecting the current service cost with the assumed salary scale and discounting with interest. This is in line with PSAS requirements.

We have validated Mercer's calculation of the total present value of expected future accruals of $100.1B. We have estimated the present value of the Plan's expected future accruals to be approximately $95B, based on the current number of active employees and the province's assumptions for financial reporting under PSAB as at the measurement date:

- Annual salary increase of 2.75% (ultimate rate)

- Discount rate of 6.00%

Our estimate of the present value of expected future accrual has been determined as follows: 2017 current service cost / (discount rate – ultimate rate of salary increase) = $3.1B / (0.06-0.0275) = $95B.

We note that our estimate is approximately $5B lower than the amount determined by the actuary. The actuary's result is likely more refined; however, the use of either figure will result in a valuation allowance of nil as the expected benefit exceeds the adjusted benefit asset. Therefore, we have not followed up with the actuaries to reconcile this difference.

Minimum contributions the Province is required to make regardless of any surplus

As there is no fixed contribution (as a percentage or dollar amount) requirement which is independent of the Plan's funding status, our interpretation is that there are no contributions that the Province is required to make, regardless of any surplus. The sponsors of the Plan can agree to any level of contribution through negotiation that leads to an actuarially balanced funding valuation. The Plan's funding level has an impact on the contribution rates, i.e. they are made with consideration for the Plan's funding surplus. Further, there is no minimum level of contribution required "regardless of any surplus". This interpretation is consistent with the interpretation we see applied in practice for other Canadian plan sponsors reporting under PSAS.

Commented [npp3]: See note above. To discuss.

Present value of the required employee contributions

We note that PS 3250.056 is written in the context of a single sponsor Plan while the OTPP is a joint-sponsored Plan. As such, the present value of the required employee contributions for OTPP is nil (i.e. the employee contributions being referenced by PS 3250.056 is in respect to contributions made by employees who are not sponsor of the Plan).

Plan surplus that can be withdrawn

As discussed in Section 2, we have assumed no Plan surplus can be withdrawn by the joint

sponsors. Expected future benefit

Using the actuary's estimate of the present value of the Plan's expected future accruals, the expected future benefit for the Plan is the present value of the Plan's expected future accruals:

Present value of the Plan's expected future accruals (PS 3250.57)	$100.1B
Present value of the required employee contributions (PS 3250.056a)	(0.0)B
Minimum required contributions regardless of any surplus (PS 3250.056a)	(0.0)B
Plan surplus that can be withdrawn (PS 3250.056b)	(0.0)B
Expected future benefit (PS 3250.056)	$100.1B

The Plan's expected future benefit is $100.1B.

3.3 Valuation allowance

PS 3250.054 states "*the adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required*".

Per 3.1 and 3.2 of this letter, we have determined that the Plan's expected future benefit exceeds the Plan's adjusted benefit asset:

Plan's adjusted benefit asset (PS 3250.053)	$51.8B
Plan's expected future benefit (PS 3250.056)	$100.1B
Valuation allowance (PS 3250.054) [max (0, $51.8B – 100.1B)]	$0.0B

The Plan's accrued benefit asset is not impaired, and accordingly, no valuation allowance is required.

3.4 Accrued benefit asset recognition

The Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Accrued benefit asset	$26.9B
Valuation allowance (PS3250.054)	0.0B
Accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B

Accordingly, the Province's portion of the Plan's accrued benefit asset, net of valuation allowance as at the measurement date is:

Plan's accrued benefit asset to be recognized (net of valuation allowance) (PS3250.050)	$26.9B
Province's portion of the accrued benefit asset (50%) [PS3250.050 x 50%]	13.5B
Other Province specific adjustment made by OPCD	(1.2)B
Accrued benefit asset to be recognized by the Province (PS3250.050)	$12.3B

The accrued benefit asset of $12.3B without any asset impairment should be recognized for the Province's financial reporting under PSAB.

Commented [npp4]: Let's discuss

Appendix
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Our analysis is based on the following information we received:

- Actuarial valuation report for OTPP as at 1 January 2016 prepared by Mercer for funding purposes
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-

Commented [npp5]: Let's discuss

Appendix
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Measurement date

.39 For a defined benefit plan, the plan assets and the accrued benefit obligation would usually be measured at the date of the financial statements. As a practical matter, an earlier date may be used provided the government adopts this practice consistently from year to year and as long as no significant change relevant to the valuation of the plan occurs between the valuation date and the financial statement date.

Limit on the carrying amount on accrued benefit asset

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

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

.54 The adjusted benefit asset is then compared to the expected future benefit. When the expected future benefit exceeds the adjusted benefit asset, the accrued benefit asset is not impaired, and, accordingly, no valuation allowance is required.

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

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

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

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

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

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

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

Joint defined benefit plans

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

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

accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.

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

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

Glossary

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

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

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

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

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

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

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

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

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

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

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

benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.

OTPP Summary of Discussion .rtf

From: Uros Karadzic [uros.karadzic@ca.ey.com]
To: Shanmugarajah, Ramya (TBS) [Ramya.Shanmugarajah@ontario.ca]; Jack, Shannon (TBS) [SOM3.Shannon.Jack@ontario.ca]; Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]; Bernard, Dena (TBS) [Dena.Bernard@ontario.ca]
Subject: OTPP Summary of Discussion
Date: Thursday, August 02, 2018 09:32:36
Attachment 1: ATT68969 1.jpg

From: Veinot, Cindy (TBS) [mailto:Cindy.Veinot@ontario.ca]
Sent: Thursday, August 2, 2018 9:31 AM
To: Uros Karadzic <uros.karadzic@ca.ey.com>
Subject: RE: OTPP Summary of Discussion

That works – I'll call you then – thanks,

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: August 2, 2018 9:22 AM
To: Veinot, Cindy (TBS)
Subject: RE: OTPP Summary of Discussion

Hi Cindy, would 11am work for a quick call?

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP
Office: +1 416 943 2087 | Mobile: +1 416 970 2087 | uros.karadzic@ca.ey.com
Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

From: Veinot, Cindy (TBS) [mailto:Cindy.Veinot@ontario.ca]
Sent: Thursday, August 2, 2018 9:13 AM
To: Uros Karadzic <uros.karadzic@ca.ey.com>
Subject: RE: OTPP Summary of Discussion

Hi Uros – thanks for sending this along – do you have time for a quick call on this?

From: Uros Karadzic [mailto:uros.karadzic@ca.ey.com]
Sent: August 1, 2018 5:32 PM
To: Veinot, Cindy (TBS)
Subject: RE: OTPP Summary of Discussion

Hi Cindy,

I've read through Mercer's response. I have no issue with the slight changes they proposed for the first 4 bullets, as they do not change the meaning, but rather provide additional clarity.

I'm struggling a bit with their logic on the last bullet. They agree that there are no minimum required contributions that would persist even if the plan was in a surplus position, yet seem to be reticent to say that the present value would be nil because the employees are currently making contributions. I don't see how this holds together. A good parallel is the interpretation of "minimum funding requirements" under IFRIC 14 – in Canadian jurisdictions where posting a Letter of Credit is available as a funding alternative, any cash contributions that the employer is actually making aren't considered as "required" if they have an alternative to post an LOC instead. This is widespread interpretation that Mercer uses for all its clients. So it should be possible for them to accept the concept that while some contributions are being made, they are not meeting the specific contribution definition in the standard ("required regardless of any surplus" under PSAB, in this case).

Practically, I see a couple of alternatives:

- We press them a bit further on this point, and ask them to explain why they think this present value would not be nil.
- We accept all their suggested changes, but ask that they add some language to the last bullet point to get to where we need to be (eg. adding at the end "Therefore, it is reasonable to expect that the province will be able to benefit from a surplus in the plan through future contribution reductions, meeting one of the requirements to recognize the surplus as an asset on the balance sheet."
- Organize an in-person meeting with you, us, Mercer and OTPP to dive into this in more detail and get to the same joint statement on this.

As a side comment, but perhaps relevant if we need to get into more detail on this, I don't see why there is an emphasis on the split between employee and employer contributions. In reality, neither of the plan sponsors has any requirements to continue overfunding a plan already in surplus, since as joint sponsors they have control over benefit and contribution levels.

Please let me know your thoughts.

Uros

Uros Karadzic, FSA, FCIA | Partner | People Advisory Services

Ernst & Young LLP
Office: +1 416 943 2087 | Mobile: +1 416 970 2087 | uros.karadzic@ca.ey.com
Assistant: Sarah Anderton | Phone: +1 416 943 3143 | sarah.anderton@ca.ey.com

From: Clausen, Scott [mailto:Scott.Clausen@mercer.com]
Sent: Wednesday, August 1, 2018 1:06 PM
To: Veinot, Cindy (TBS) <Cindy.Veinot@ontario.ca>; 'Mary Cover' <Mary_Cover@otpp.com>
Cc: Uros Karadzic <uros.karadzic@ca.ey.com>; Houle, Lise <Lise.Houle@mercer.com>; Doherty, Elizabeth (MOF) <Elizabeth.Doherty@ontario.ca>; Killoch, Alex (MOF) <Alex.Killoch@ontario.ca>; Donaldson, Mark (TBS) <Mark.Donaldson@ontario.ca>
Subject: RE: OTPP Summary of Discussion

Hi Cindy

Please find attached a copy of our response to the July 31, 2018 letter to Mary Cover.

Thank you,
Scott

From: Hosick, Sarah (TBS) [mailto:Sarah.Hosick@ontario.ca] **On Behalf Of** Veinot, Cindy (TBS)
Sent: Tuesday, July 31, 2018 10:31 AM
To: 'Mary Cover'
Cc: Uros Karadzic; Clausen, Scott; Houle, Lise; Doherty, Elizabeth (MOF); Killoch, Alex (MOF); Donaldson, Mark (TBS)
Subject: OTPP Summary of Discussion

Treasury Board Secretariat

Office of the Treasury Board
Office of the Provincial Controller Division

Frost Building South, 2nd Floor
7 Queen's Park Crescent
Toronto ON M7A 1Y7
Tel. (416) 325-8017
Fax. (416) 325-4834

Secrétariat du Conseil du Trésor

Bureau du Conseil du Trésor
Bureau du contrôleur provincial

Édifice Frost Sud, 2e étage
7 Queen's Park Cr.
Toronto ON M7A 1Y7
Téléphone: (416) 325-8017
Télécopieur: (416) 325-4834

July 31, 2018

Ms. Mary Cover
Managing Director, Pension Strategy & Enterprise Risk
Ontario Teachers' Pension Plan Board
5650 Yonge Street
Toronto, ON
M2M 4H5

Dear Ms. Cover,

I understand based on discussion with Uros Karadzic from EY, the following bullets reflect the key points discussed on the call between Uros Karadzic, Scott Clausen, Lise Houle and yourself on July 26, 2018 regarding the Ontario Teacher's Pension Plan. Could you please review and confirm that you are in agreement with the bullets, or if not, provide any amendments required to reflect your understanding of the key points of the discussions:

- During the actuarial call on July 26, it was clarified that the present value calculations presented in the letters to Mary Cover on January 26, 2018 and discussed further in July 2018, were calculated under the assumption that the plan terms and the contribution rates remain indefinitely as they currently are today

- Looking longer term, with reference to funding management policy (FMP), it is reasonable to expect that the contribution and benefit levels would change in response to an emerging surplus in the plan. For example, the employees could chose to apply some of the surplus to improving benefits, while the province could chose to reduce contribution rates. The 50/50% sharing mechanism would be maintained.

- There is no requirement under FMP or otherwise that any contributions continue regardless of any surplus in the plan. In other words, if there are surplus assets in the plan, the plan sponsors (employees and the province) can chose to use that surplus, while maintaining 50/50% sharing mechanism, in various ways including reducing contributions. There is no minimum level of contributions that must continue regardless of any surplus.

- The requirement for the province to match employee contributions at 100% may not carry past the point that surplus emerges. FMP also contemplates payout of surplus to the plan members (but likely not the province).

- Therefore, while the above referenced calculations are actuarially correct if one assumed no changes to contribution rates of benefits at any point in the future, if we were to take a broader view of present valuing only those contributions that would have to be made regardless of any surplus in the plan, such present value would be nil (since there is no requirement for any minimum level of contributions even if the plan was already in a surplus position).

We would appreciate if you could respond at your earliest convenience, and if possible by August 3, 2018.

Regards,

Original Signed By

Cindy Veinot
Assistant Deputy Minister & Provincial Controller

c. Uros Karadzic, EY
Scott Clausen, Mercer
Lise Houle, Mercer
Elizabeth Doherty, Ministry of Finance
Alex Killoch, Ministry of Finance
Mark Donaldson, Treasury Board Secretariat

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ATT68969 1.pdf

Ontario

Ontario Pension Plans - Accounting treatment .rtf

From: Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]
CC: Christina Chan [Christina.Chan@ca.ey.com]; Uros Karadzic [uros.karadzic@ca.ey.com]
Subject: Ontario Pension Plans - Accounting treatment
Date: Wednesday, May 10, 2017 21:47:20
Attachment 1: image001.png
Attachment 2: Accounting Approach Ontario pension plans.pdf

Further to our meeting this afternoon, the attached document describes key characteristics, current and proposed accounting treatment, and some additional considerations for the plans discussed.

We will look into the year-end adjustment for HOOPP and get back to you with our observations. In addition, we will prepare adjusted figures based on the proposed accounting treatment in the attached document for the remaining plans.

Please let us know if you have any questions.

Regards,

Shayan

Shayan Jafrani, FSA, FCIA | Senior Manager | People Advisory Services

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 2975 | Cell Phone: +1 647 885 9630
EY/Comm: 1675237 | Shayan.Jafrani@ca.ey.com
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image001.pdf

EY

Accounting Approach Ontario pension plans.pdf

Accounting Approach - Ontario Pension Plans

		OTPP	OPSEUPP	PSPP	HOOPP	CAATPP
Key characteristics	Joint sponsored	Yes	Yes	No	Yes	Yes
	Proportion related to other non-consolidated employers	2.0%	4.7%	4.8%	15.5%	0%
	Do non-consolidated employers bear funding risk?	Yes - contribution increases impact all employers	Yes - contribution increases impact all employers	No - Province is responsible for special payments to fund deficiencies, other employers only responsible for ongoing costs	Yes - contribution increases impact all employers	n/a
Accounting treatment - Current state	Assets and obligations	50% allocated to Province	50% allocated to Province	100% allocated to Province	84.5% of employer portion allocated to Province	50% allocated to Province
	Contributions	Only Province contributions considered, i.e. 49% of total contributions	Only Province contributions considered, i.e. 47.65% of total contributions	Only Province contributions considered, i.e. 47.6% of total contributions	Only Province contributions considered, i.e. consistent with expense, assets and obligations	50% allocated to Province
	Expense	50% of total plan expense allocated to Province, plus amortization of certain adjustments.	50% of total plan expense allocated to Province, plus amortization of certain adjustments.	Expense appears to be reduced to reflect contributions of non-consolidated employers	84.5% of employer sponsor portion of expense allocated to Province	50% allocated to Province
	Impact to year-end	Inconsistency between contributions and expense leads to balance sheet understatement. Corrected over time through amortization.	Inconsistency between contributions and expense leads to balance sheet understatement. Corrected over time through amortization.	An adjustment to balance sheet is applied to reflect difference between Province and total employer contributions leading to balance sheet understatement.	No impact aside from adjustments due to slippage - to be reviewed.	No impact
Proposed accounting treatment	Proposed treatment	Reduce employer share to reflect participation of non-consolidated employers (consistent with HOOPP)	Reduce employer share to reflect participation of non-consolidated employers (consistent with HOOPP)	Apply offset to expense to reflect participation of non-consolidated employers. Expense reduced but risk retained.	No change	No change
	Impact of proposed treatment	Reduction in annual expense, improvement to balance sheet asset from removal of current year-end adjustment, reduction in balance sheet asset and annual income to reflect reduced share of plan	Reduction in annual expense, improvement to balance sheet asset from removal of current year-end adjustment, reduction in balance sheet asset to reflect reduced share of plan	Improvement in balance sheet asset to reflect removal of current year-end adjustment	No change	No change
	Financial impact - Balance Sheet	+$251M removal of year-end adjustment -$246M due to reflecting 49% vs 50% of plan	+$116M removal of year-end adjustment at 3/31/17 combined with PSPP -$29M due to reflecting 47.65% vs 50% of plan	+$116M removal of year-end adjustment at 3/31/17 combined with OPSEU	No change	No change
	Financial impact - P&L	-$10M net reduction in pension income	$4M net increase in pension expense	No change	No change	No change
Additional considerations		Imprecise to apply a single percentage to all components of calculation. DBO/SC. However, likely reasonable if the participation of other employers does not change significantly each year.	Imprecise to apply a single percentage to all components of calculation. DBO/SC. However, likely reasonable. Need to consider how to reflect other consolidated employers.	Contributions from other non-consolidated employers treated similar to employee contributions. Need to consider how to reflect other consolidated employers.	Consider determining % based on proportion of contributions rather than headcount prorate as contributions relate more closely to costs.	Should an adjustment be made for the fact that the Province does not provide 100% of the CAAT budget (30%)

Ontario vs. BC Plans.rtf

From: Petsche, Nadine (TBS) []
To:
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Ontario vs. BC Plans
Date: Thursday, September 22, 2016 22:05:57
Attachment 1: Letter to Veinot re Surplus Rights in regards to Ontario and BC Plans - September 19 2016 (3).docx

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I was awaiting a final version of the attached doc, but it hasn't been revised over the last day, so I'm sending it as a good summary comparing ON's plans to those in BC.

Nadine

Letter to Veinot re Surplus Rights in regards to Ontario and BC Plans - September 19 2016 (3).pdf

KOSKIE MINSKY
JUSTICE MATTERS

September 20, 2016

Murray Gold
Direct Dial: 416-595-2085
Direct Fax: 416-204-2873
mgold@kmlaw.ca

Via E-mail

Cindy Veinot
Assistant Deputy Minister and Provincial Controller
Province of Ontario

Dear Ms. Vienot:

Re: Legal Opinion Concerning Surplus Rights in regard to the Ontario Teachers' Pension Plan, the OPSEU Pension Plan, the British Columbia Municipal Pension Plan, the British Columbia Public Service Pension Plan, the British Columbia Teachers' Pension Plan and the British Columbia Colleges Pension Plan
Our File No.: 162080

You have requested our legal opinion concerning the authorities of the sponsors and plan administrators of the above-captioned Plans with respect to ongoing surpluses in those plans.

In general, the sponsors of these pension arrangements are governments and sometimes other employer associations (the employer sponsor), and trade unions (the employee sponsor, or 'partner'). The 'plan administrators' of each Plan are either boards of trustees or, in the case of the OTPP, a board of directors. Plan administrators are independent entities that owe fiduciary obligations to the members of the Plan they administer.

The constating documents for each Plan set out the respective rights of the sponsors of each arrangement, and describe as well the powers of the fiduciary administrator of each Plan. In some cases, there is a clear differentiation between the powers of the sponsors and the powers of the plan administrators; in other cases, both the sponsors and the fiduciary administrator may have powers with respect to the same issue.

Below, we briefly review the relevant provisions of the constating documents for each of these Plan arrangements. Then, we summarize our opinions concerning the respective powers of the Plan sponsors and the fiduciary administrators in regard to surpluses arising under each arrangement.

This opinion is based on the documents referenced herein. In the event that there are any other constating documents with respect to any of the Plans described below, the conclusions expressed in this opinion may change and cannot be relied upon.

In general, the Plans' constating documents sometimes refer to "surplus", and other times to "actuarial gains" or "excess assets". The term "surplus" may refer either to an ongoing surplus, or to a surplus that is crystalized upon the termination and wind-up of a plan. For the purposes of this opinion, we treat these terms as being equivalent.

KOSKIE MINSKY
JUSTICE MATTERS

I. ONTARIO PLANS

A. Ontario Teachers' Pension Plan ("OTPP")

The OTPP is governed by:

(a) the *Teachers' Pension Act*, R.S.O. 1990, c.T.1 (the "TPA");

(b) Plan text for the OTPP (the "Plan text");

(c) an Agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training (the "Minister") and The Ontario Teachers' Federation represented by its Executive (the "OTF"), dated July 15, 1991 (the "Partners' Agreement"), as amended; and

(d) a Funding Management Policy, attached as Appendix "A" to the Partners Agreement.

The TPA provides, at sections 5(1) and 5(1.1), that the Minister of Finance is required to pay from the Consolidated Revenue Fund contributions payable by the Minister of Education and provides that the total amount of such contributions "…shall not exceed the amount of contributions payable by or on behalf of active Plan members in respect of credited service for that year" (section 5(1.1)). The Plan text requires, at section 25, "that the Minister of Education contribute to the OTPP an amount equal to the required contributions made during the year before the preceding year by or on behalf of those members for whom the Minister is required to make employer contributions" (section 25(1)). Additional provisions of section 25 of the Plan text contain other provisions with respect to the Minister's obligation to make contributions to the OTPP.

The Partners' Agreement stipulates, at section 8 that the Partners are generally responsible for benefits and contribution rates:

> "8. The partners will be responsible for designing the plan structure, setting the benefits of the plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, making changes to the plan, this agreement or other plan documents, deciding whether or not to file a valuation more frequently than required by the *Pension Benefits Act,* appointing the Board, and defining the role of the Board."

By contrast, section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the partners to the OTPP have the authority to utilize ongoing surpluses.

The process governing the use of ongoing surpluses by th Partners is set out in the partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73). The Partners are then required to bargain in good faith with respect to the disposition of any surpluses, or any adjustments to address Plan deficiencies (section 74). Section 77 of the Partners' Agreement anticipates that the Partners may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the

appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

B. The OPSEU Pension Plan ("OPTrust")

The OPTrust is governed by:

(a) a Sponsorship Agreement made as of April 18, 1994 between Her Majesty the Queen in right of the Province of Ontario as represented by the Chair of the Management Board of Cabinet ("Ontario") and the Ontario Public Service Employees' Union ("OPSEU") (the "Sponsorship Agreement");

(b) an Agreement and Declaration of Trust of the Trust Fund dated October 25, 1994 (the "Trust Agreement"); and

(c) OPTrust Plan text.

Section 56 of the Sponsorship Agreement addresses the use of actuarial gains disclosed under an actuarial valuation report prepared after March 31, 1997. Section 56(d) provides that once the 'Transferred Initial Unfunded Liability' of the OPTrust has been fully liquidated (we understand that it has been liquidated), then actuarial gains disclosed by a valuation of the OPTrust are divided into two equal pools, one of which "…shall be used for the benefit of Ontario, to be applied against any special payments required to be made by Ontario and thereafter to reduce Ontario's normal costs…" and the other pool is to be used by OPSEU for the benefit of Plan Members (section 56(c) of the Sponsorship Agreement). Section 56(d) also anticipates that OPSEU and Ontario may collectively bargain an allocation of gains that is different from 50/50.

The Trust Agreement provides that only the Sponsors (Ontario and OPSEU) may amend the Plan (section 4.02), and further specifies that the plan administrator, i.e. the Board of Trustees of the OPTrust, "…shall have no power to amend either the Plan or this Agreement" (section 4.03). Accordingly, under the Sponsorship Agreement and Trust Agreement, the OPTrust plan administrator has no authority to utilize actuarial gains. Rather, that authority is conferred, by section 56 of the Sponsorship Agreement on the Sponsors, being Ontario and OPSEU. Moreover, the OPTrust Board of Trustees is not able to increase OPTrust benefits using ongoing surpluses, as only the Sponsors of the OPTrust are able to amend the Plan.

II. BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsorred pension plans to jointly sponsored plans in accordance with the *Public Sector Pension Plans Act*, S.B.C. 1999, c.44 (the PSPPA").

KOSKIE MINSKY
JUSTICE MATTERS

A. ***British Columbia Municipal Pension Plan (the "MPP")***

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at

the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan ("PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[1] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed

[1] It is noteworthy that s. 14.2(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the same way as the other BC Plans.

The Partners have the authority (s.14(2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the

administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities.

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario *Pension Benefits Act*, R.S.O. 1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

OPTrust - The OPTrust governing documents also stipulate that it is the Sponsors of the OPTrust, being the Province of Ontario and OPSEU, who have the authority to utilize ongoing Plan surpluses. OPTrust's Board of Trustees, being the OPTrust administrator for purposes of the Ontario PBA, has no authority to utilize ongoing Plan surpluses. Pursuant to section 56(c) of the OPTrust Sponsorship Agreement, ongoing surpluses are divided into two equal pools (although the equal division may be altered through collective bargaining), and each of Ontario and OPSEU may utilize those pools without the agreement of the other party. In other words, Ontario may unilaterally determine the disposition of its pool, and OPSEU may unilaterally determine the disposition of its pool, subject only to Ontario's PBA. Neither OPSEU nor Ontario requires the agreement of the other party in order to utilize its allocated amount of ongoing surplus.

B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or

increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations. At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations.

Transitional Period - In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

We trust that these comments have been of assistance to you. Should you have any questions in regard to them, please do not hesitate to contact the undersigned.

Yours truly,

KOSKIE MINSKY LLP

Murray Gold

MG:jn

Osler opinion re_ OTPP surplus.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Osler opinion re: OTPP surplus
Date: Tuesday, September 20, 2016 12:59:08
Attachment 1: Opinion dated September 20, 2016.pdf

Lucy,

Please find attached a copy of the external legal firm's opinion for your reference.

Please let me know if you have any questions.

Nadine

416 325 8027

Opinion dated September 20, 2016.pdf

Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8
416.362.2111 MAIN
416.862.6666 FACSIMILE

OSLER

Toronto
Montréal
Calgary
Ottawa
New York

September 20, 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"**).

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.

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1 See letter from Bonnie Lysyk (Auditor General) to Greg Orencsak (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

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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 deficiency[9] (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

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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

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[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 fund[12] 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

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[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

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[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

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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]

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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 plan[25] 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:

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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' Agreement[29] 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

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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).

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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'

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[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,

Osler, Hoskin & Harcourt LLP

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

Outline of position paper proposed allocations Oct 7.docx.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Outline of position paper proposed allocations Oct 7.docx
Date: Friday, October 07, 2016 16:02:01
Attachment 1: Outline of position paper proposed alloations Oct 7.docx

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Hi Lucy.

As discussed, the attached version of the paper outline includes proposed section allocations. Please let me know if any of the notes are inconsistent with your understanding.

Thanks and have a wonderful Thanksgiving weekend!

Nadine

Outline of position paper proposed alloations Oct 7.pdf

Outline of position paper

Background Summary of facts relevant to plan, incorporating: • Facts in Deloitte opinion • Facts in Oslers opinion • Facts in Koskie Minsky opinion Summary of build-up of accounting asset since 2001-02, including components -- current service cost, interest on obligation, expected interest on assets; also include economic assumptions used each year and explanation of market related value impact (may need to include an explanation of the accounting for a JSPP) • Pauline has all of this information • Summary of the difference between OTPP's f/s, the funding valuation and the government's accounting • Commentary on discount rate differences, OTPP as an outlier re: use of corporate borrowing rate (Pauline has an analysis), and whether there is any interaction between the various valuations of the projected benefit obligation	Jim Keates with input from Pauline Fong
Accounting Analysis Question 1 – Recognition What standard governs the recognition of a pension asset? Views a. PS 3250 o PS 3250 contemplates the existence of an asset, 50-59 are measurement standards which would only be needed if an asset exists o PS 3250 was developed based on the existing conceptual framework – e.g. developed in the context of the current definition of an asset b. Go beyond 3250 • Shared control i. Used in definition of a joint defined benefit plan ii. Set up of criteria for government partnership has parallels to definition of joint defined benefit plan iii. Consider consultation with PSAB – what was considered when PS 3250 was developed (developed after government partnerships); what is meant by footnote 3 in PS 3060; if 3250 was meant to be excluded from 3060 why wasn't it listed as a scope exclusion [Note – Stephenie Fox at CPA Canada was the project manager on PS 3250] iv. Contrast the governance framework of the Ontario plans (OTTP and OPSEUPP) to the BC plans (Koskie Minsky) and NB plans	

Commented [np1]: Jim Keates with input from Pauline Fong

Commented [np2]: Lucy (PwC)

Commented [np3]: Jim Keates

Commented [np4]: Lucy (PwC)

Commented [np5]: Jim Keates

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Outline of position paper

c. Go beyond 3250 • Control i. One of the criteria to meet the definition of an asset ii. Does control have to be unilateral iii. What other assets are recognized based on an expected future benefit • Income taxes – don't control generating future income • Regulatory assets -- don't control decision of regulator • Others? iv. What does the profile of recognition look like if no asset is recognized until you have an agreement with the co-sponsor d. Go beyond 3250 • Contingent asset i. Assess definition and criteria of a contingent asset Conclusion re: recognition	
Question 2 – Measurement Is uncertainty factored into the calculation or does uncertainty have to be eliminated to have a valuation allowance of less than the value of the asset? a. Uncertainty is factored into the calculation • Number of factors articulated in Deloitte opinion to consider i. Structure of agreements re: shared decision making ii. History of decisions made iii. Impact of "share-the-pain" payments iv. CRA cap v. Impact of improving benefits vs. reducing contributions b. Uncertainty has to be NIL to recognize an asset • Analogy to receivable • Assume contributions at the current level continue into perpetuity in the absence of another agreement with the co-sponsor • How does an asset get recognized under this model – e.g. what is impact on the model • c. Other factors • Benefit realization (surplus withdrawal vs. contribution reductions vs. fungibility of compensation-related benefits • Impact of benefit improvement to use of surplus and obligation PV Conclusion re: measurement	
Need to ensure that all of AG's views are incorporated into the position paper,	

Commented [np6]: Lucy (PwC)

Commented [np7]: OPCD

Commented [np8]: OPCD

Commented [np9]: Lucy (PwC)

Commented [np10]: OPCD

Commented [np11]: Lucy (PwC)

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Outline of position paper

some of which may be in an appendix (e.g. the relevance/irrelevance of the difference between the rate OTPP uses in its f/s vs. the province – Pauline has a comparison for all of provinces demonstrating that the rate OTPP uses is an outlier)	
Fair Presentation Also – should profile the impact of the AG's memo in years of significant losses (e.g. unamortized actuarial losses can result in the reversal of part of the valuation allowance – see 2008-09 calcs from Pauline)	
Additional considerations: • Do we want to raise this issue to the PSADG? • How/when do we discuss with the PSAB task force	Lucy, as facilitator to keep log of possible items for discussion/submission

Commented [np12]: Pauline Fong

Commented [np13]: PwC/OPCD

DRAFT

PLEASE SIGN AND RETURN .rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: PLEASE SIGN AND RETURN
Date: Monday, September 19, 2016 17:53:21
Attachment 1: PWC SOW Pensions Accounting Opinion 20160915 clean v2 to Lucy.docx
Attachment 2: Scanned from a Xerox multifunction device.pdf

Hi Lucy.
Attached is the revised SOW (track changes and clean signed version), dated September 16, 2016. Subject to any concerns or further edits, please sign and return a copy.
Thanks.
Shyrose

PWC SOW Pensions Accounting Opinion 20160915 clean v2 to Lucy.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective September 16, 2016.

PricewaterhouseCoopers LLP (the "Vendor" or "PwC") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client" or the "Province") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of March 22, 2016 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$100,000.00, excluding HST.

4. *Project Start Date:* September 16, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide accounting advice (the "accounting advisory services") regarding the acceptability of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards. The accounting advice may include:

   - Review of background information, position papers developed by the Client or third parties that have been engaged by the Client to draft accounting positions on accounting for the recognition and measurement of pension assets for jointly-sponsored pension plans, and other supporting information.
   - Provide written or oral comments on draft position papers as provided by the Client with respect to the application of Canadian Public Sector Accounting Standards.
   - Participation in discussions with internal and external stakeholders and other parties as directed by the Client.

   During the course of this project, the Client will provide to PwC a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements with the Client's auditor. If an accounting opinion is to be provided, the Client's auditor will confirm to us in writing that the information the Client

has provided to PwC is complete and consistent with their knowledge of the facts and circumstances of the specific transaction.

If requested to by the Client during the course of the project, the Vendor shall provide an accounting opinion (the "accounting opinion"), prepared in accordance with Section 7600, *Reports on the application of accounting principles* of the CPA Canada Handbook – Assurance ("Section 7600"), regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards.

Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting advice or accounting opinion (if applicable), including discussions with the Office of the Auditor General.

The Client agrees that any accounting advisory services are solely for the information and use of the Client. Subject to the obligations in Article 27 (Privacy) of the Master Agreement and as required by law by the Client's independent auditors, the Client agrees that any written work product of PwC will not be made available to any other persons or entities. An accounting opinion prepared in accordance with Section 7600 will, in compliance with Canadian GAAS, include restriction of use language identifying the parties to whom use is restricted and a statement that the report is not intended to be and should not be used by anyone other than the specified parties or for any other purposes. However the Client may provide access to PwC's observations and an accounting opinion prepared under Section 7600 (if applicable) to the Client's independent auditors solely for their informational purposes. Except as provided for in the preceding sentence, the Client agrees to seek and obtain the Vendor's written consent before including our accounting opinion (if applicable) or referring to the Vendor in any document disclosed to third parties, including disclosure of a summary of the accounting opinion or publication of the opinion in documentation that may be accessible to or intended for the public. The Vendor may, in their own discretion, waive the requirement to obtain written consent. The Client agrees that prior to or as part of providing their independent auditors with any written work product of PwC, including an accounting opinion prepared under Section 7600, the Client will notify its independent auditors that it is PwC's desire to be notified of, and to consent to, the disclosure of any PwC written work product or reference to any PWC work product in any materials to be disclosed to third parties. PwC agrees that the Client's obligation is only to notify its independent auditors of PwC's desire to be notified about, and to consent to, disclosure, and that the Client is not making any representation or warranty that its independent auditors will notify PwC or seek PwC's consent.

Acknowledgements and agreements

The Client acknowledges and agrees to the following:

a. The performance of the accounting advisory services does not constitute an engagement to provide audit, compilation, review or attest services in accordance with professional standards issued by the Chartered Professional Accountants of Canada ("CPA Canada") and, therefore, PwC will not express an opinion or any other form of assurance with respect to the accounting advisory services.
b. The accounting advisory services and accounting opinion (if applicable) to be provided do not include the delivery of any verbal or written advice on the application of accounting principles to a hypothetical transaction.
c. This engagement cannot be relied on to disclose internal control deficiencies, errors or fraud, should they exist.

d. PwC has no responsibility for updating the accounting advisory services or accounting opinion or for performing any additional services, except as agreed to in writing with the Client.
e. The Client's purpose for engaging PwC to perform the accounting advisory services is to supplement management's own technical accounting resources in performing accounting analysis and to assist management in making its determination as to the application of accounting principles and not to obtain an opinion from PwC as to such application, unless an accounting opinion is requested by the Client.
f. The Client shall be solely responsible for, among other things: (a) making all management decisions and performing all management functions; (b) designating one or more individuals who possess suitable skill, knowledge and/or experience, preferably within senior management to oversee the accounting advisory services (c) evaluating the adequacy and results of the accounting advisory services; (d) accepting responsibility for the results of the accounting advisory services; and (e) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities.
g. All management decisions and final conclusions reached in connection with the accounting advisory services will be the responsibility of the Client. PwC will not perform any management functions, make management decisions, or perform in a capacity equivalent to that of an employee of the Client.
h. PwC has no responsibility related to the Client's accounting or disclosure conclusions, whether or not such conclusions of the Client are related to the accounting advisory services and PwC has no responsibility for any disagreements between the Client and its independent auditor related to the Client's accounting.
i. The Client will be solely responsible for all decisions regarding the accounting treatment of any item or transaction and acknowledges that the accounting advisory services do not include the recording of any amounts in the Client's books or records. All amounts derived from the performance of the accounting advisory services will be reviewed and approved by, and will be the responsibility of, the Client's management.
j. The nature, scope and design of the accounting advisory services and the accounting opinion are solely the responsibility of the Client. PwC will rely, without independent verification, on the facts, information and assumptions provided by the Client. PwC will make no representation nor provide any assurance with respect to the adequacy of the services for the Client's purposes. Furthermore, PwC has no responsibility to advise the Client of other procedures that might be performed.
k. The Client will be solely responsible for providing accurate and complete information requested by PwC. PwC has no responsibility for the accuracy or completeness of the information provided by or on behalf of the client.
l. PwC's accounting and technical assistance will be based on the existing public sector generally accepted accounting principles. Should those generally accepted accounting principles be amended, superseded or revised in any manner, PwC's advice might change. PwC has no responsibility to inform the Client of any changes in generally accepted accounting principles that may occur after the completion of the engagement or any other oral or written work product prepared hereunder that would impact PwC's advice on the appropriate application of generally accepted accounting principles or to update its recommendations or any other oral or written work produce to take any such changes into account.
m. This engagement does not create a relationship between PwC and any person or party other than the Client. This engagement is not intended for the express of implied benefit of any third party.

n. The Client will identify an appropriate individual to serve as the project manager, including overseeing the accounting advisory services.

7. *Ownership and Licences* - **Attachment D** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be Lucy Durocher who is the engagement leader.

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Charges On Per Diem Rate Basis*– The Vendor and the Client agree that Work performed under this Statement of Work will be charged on a Per Diem Rate basis. The Per Diem Rate will vary, based on the nature of the final deliverable, as follows:

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Accounting Advisory	General Consultant, Level 2	Service Category 2	20-25	$390/hour
Accounting Opinion	General Consultant, Level 2	Service Category 2	30-35	$990/hour

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Individual's Legal Name	Individual's Role and Experience Level	Service Category	Per Diem Rate
Lucy Durocher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Martin Boucher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Sean Cable (or alternative as agreed to by the Client)	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"
Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client: Treasury Board Secretariat,
Office of the Provincial Controller Division
Branch: Accounting Policy and Financial Reporting

Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Clients designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all Confidential information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

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Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

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Vendor Representative:	**Lucy Durocher**
Telephone number:	**416-869-2311**
E-mail:	**Lucy.durocher@ca.pwc.com**
Backup Vendor Representative:	**Martin Boucher**
Telephone number:	**514-205-5415**
E-mail:	**Martin.boucher@ca.pwc.com**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: _____

Name: _____

Title: _____

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature:

Name: _____

Title: _____

I have the authority to bind the Vendor.

Scanned from a Xerox multifunction device.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective September 16, 2016.

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Martin Boucher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
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Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

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Client: Treasury Board Secretariat,
Office of the Provincial Controller Division
Branch: Accounting Policy and Financial Reporting

Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

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Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

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Vendor's address for receipt of notices:	**PricewaterhouseCoopers LLP, PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2**
Vendor Representative:	**Lucy Durocher**
Telephone number:	**416-869-2311**
E-mail:	**Lucy.durocher@ca.pwc.com**
Backup Vendor Representative:	**Martin Boucher**
Telephone number:	**514-205-5415**
E-mail:	**Martin.boucher@ca.pwc.com**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: N. Petsche

Name: Nadine Petsche

Title: Director, Accounting Policy & Financial Reporting

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor.

PSAB Accounting Discussion Group and Pension-related matters.rtf

From: Petsche, Nadine (TBS) []
To: 'Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca)' [mcolley@deloitte.ca]
CC: pjesty@deloitte.ca [pjesty@deloitte.ca]; Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: PSAB Accounting Discussion Group and Pension-related matters
Date: Thursday, October 20, 2016 08:17:06

Hi Matt.

It would be good if we could touch base on the upcoming PSAB ADG agenda as well as the pension related SOW.

With respect to the ADG, I understand that there will be a couple of items on the agenda for the November 18th meeting which may relate to/impact Ontario's financial reporting. Specifically, the ADG is expected to address whether an investment holdco could be accounted for as a GBE, as well as the determination of shared control.

I was told that both of these items arose from discussions among the large firms. I was hoping that you might be able to confirm your understanding that these items will be addressed at the November 18th ADG, and also that you might be able to share a copy of the ADG submissions for each of these items at your earliest convenience.

On pension-related matters, would like to touch base on next steps. As you know, the original SOW contemplated additional work by Deloitte beyond the initial assessments done by Martin. In light of the current Panel initiative, we would like to start some of the incremental work now.

Unfortunately, my schedule is pretty hectic, but Shyrose can help to find some time for us to chat on these two items. Talk to you soon.

Nadine

PSPP HOOP and CAAT.rtf

From: Virani, Shyrose (TBS) []
To: Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Chan, Vanessa W. (TBS) [Vanessa.W.Chan@ontario.ca]; christina.chan@ca.ey.com [christina.chan@ca.ey.com]; 'Gregory Winston' [gregory.winston@ca.ey.com]
Subject: PSPP HOOP and CAAT
Date: Wednesday, January 17, 2018 11:44:40

PSPP HOOP and CAAT.rtf

From: Virani, Shyrose (TBS) []
To: Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Chan, Vanessa W. (TBS) [Vanessa.W.Chan@ontario.ca]; christina.chan@ca.ey.com [christina.chan@ca.ey.com]; 'Gregory Winston' [gregory.winston@ca.ey.com]
Subject: PSPP HOOP and CAAT
Date: Wednesday, January 17, 2018 11:37:51

Pension - PWC.rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Pension - PWC
Date: Tuesday, October 04, 2016 15:22:55

Hi Lucy

We are forecasting our budget and would like to know how much monies have already been spent as of last Friday (Sep 30th) Please advise asap.

Thanks

Shyrose

Pension Asset - additional advice.rtf

From: Virani, Shyrose (TBS) []
To: uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Donaldson, Mark (TBS) [Mark.Donaldson@ontario.ca]; sarah.anderton@ca.ey.com [sarah.anderton@ca.ey.com]
Subject: Pension Asset - additional advice
Date: Friday, June 22, 2018 10:36:00

Pension Asset - additional advice.rtf

From: Donaldson, Mark (TBS) []
To: Uros Karadzic [uros.karadzic@ca.ey.com]
CC: Christina Chan [Christina.Chan@ca.ey.com]; Gregory Winston [gregory.winston@ca.ey.com]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]
Subject: Pension Asset - additional advice
Date: Monday, May 14, 2018 15:55:26
Attachment 1: Additional Asset Ceiling Detail (EY 12 June 2017).pdf

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Hi Uros – hope all is well. Spring has finally arrived!

In reviewing our 2017-18 Audit Plan with the AG, the following request has been made:

· Request the asset ceiling test to be performed for each significant pension plan with an accrued benefit asset using the perpetuity assumption for both service costs and contributions.

Cindy has asked me to reach out to you and ask for the "additional advice" letter that was provided last year (see attached) w.r.t. the asset ceiling calculation. We would then appreciate your confirmation that we may share this letter with the Auditor General's office as it pertains to our 2017-18 audit.

If you require something more formal for this request, please let me know.

Happy to discuss,

Thanks.

Mark Donaldson, CPA, CMA

Director, Financial Reporting and Fiscal Support

Office of the Provincial Controller Division, Treasury Board Secretariat

7 Queen’s Park Cres, 2nd Floor

Toronto, Ontario

M7A 1Y7

(416) 325-8027

Additional Asset Ceiling Detail (EY 12 June 2017).pdf

Ernst & Young LLP
EY Tower
100 Adelaide Street West, PO Box 1
Toronto, ON M5H 0B3

Tel: +1 416 864 1234
Fax: +1 416 864 1174
ey.com

Building a better working world

Cindy Veinot
Assistant Deputy Minister & Provincial Controller
Office of the Provincial Controller Division
Office of the Treasury Board, Treasury Board Secretariat
Frost Bldg S, 7 Queen's Park Cres E
Toronto ON M7A 1Y7

12 June 2017

Additional information on asset ceiling calculation

Dear Cindy,

This document is in response to the request received from Nadine Petsche on 6 June 2017 to provide our advice to you regarding the request from the Office of the Auditor General of Ontario (AG). In particular, we understand that you would like some additional advice related to the asset ceiling calculation we performed, and the AG's ask to prepare and provide a calculation of the asset ceiling test using the "perpetuity assumption" for both Service Cost and Contributions for each significant pension plan.

This document provides this additional advice and is intended to inform and support OPCD in forming its opinion on appropriate accounting related to OTPP and OPSEUPP in the Province's financial statements. This document does not constitute an accounting opinion and should not be used as such. This document is intended for OPCD's use only. Please inform us in writing of any parties outside of the OPCD that you would like to share this document with before it is shared.

Asset ceiling test for OTPP and OPSEUPP

As you know, we have completed our analysis and calculation of the asset ceiling tests for OTPP and OPSEUPP that was provided to your office via two draft documents dated 16 May 2017. [1]

The asset ceiling test analysis and calculation we prepared for you showed that there is no impact on the asset ceiling test, and that there is no valuation allowance required in respect of OTPP and OPSEUPP. This is because the expected future benefit exceeds the value of any contributions that the plan sponsors must make regardless of any contributions [PS 3250.50-59]. The following table summarizes the results:

As at 31 March 2017	OTPP	OPSEUPP
1. Adjusted benefit asset (PS 3250.053)	51.8B	2.30B
2. Expected future benefit (PS 3250.056)		
a. Present value of service cost (PS 3250.057)	100.1B	13.88B
b. Present value of minimum contribution requirement, regardless of any surplus (PS 3250.056a)	(0.0)B	(0.0)B
c. Expected future benefit [(2.a) – (2.b)]	100.1B	13.88B
3. Valuation allowance (PS 3250.054) [max (0, (1)-(2.c)]	0.0B	0.00B

[1] Those documents are in draft form to allow for a final update once the discussions on year-end adjustments are complete. However, our conclusions as they relate to the asset ceiling calculation, and in particular to the "perpetuity assumption" are not affected by any changes that may be made to that year-end adjustment process.]

4.	Accrued benefit assets	26.9B	1.95B
5.	Valuation allowance	(0.0)B	(0.0)B
6.	Accrued benefit assets, net of valuation allowance (PS3250.050) [(4) – (5)]	26.9B	1.95B
7.	Province's portion of accrued benefit asset	50%	50%
8.	Province's portion of accrued benefit asset [(6) x (7)]	13.5B	n/a
9.	Province's portion of accrued benefit asset, reflecting unused RSF in excess of OPSEU's RSF[2]	n/a	1.02B

The above analysis does not reflect any year-end adjustments to the balance sheet position by OPCD.

Since the plans have significant future service cost accruals, the present value of which exceeds the current surplus, it is reasonable to conclude that the government can benefit from the entire surplus asset and therefore can recognize it on the balance sheet under PSAS.

In the above analysis we have considered, in perpetuity, any minimum contributions that the plan sponsors (Province and the employee unions) are required to make regardless of any surplus, in accordance with 3250.56. As there are no minimum contributions that are required to be made regardless of any surplus for either OTPP or OPSEUPP, this present value in perpetuity is nil.

For ease of reference, we will refer to the "minimum contributions the government is required to make regardless of any surplus" in PS 3250.56(a) as "MCRS" in the remainder of this document.

For greater clarity, we have not included the currently required funding contributions, in perpetuity or otherwise, into the asset ceiling test calculation as it is our understanding that this would not be in compliance with PSAS. These contributions are currently in place to fund deficits, and to provide for current service costs for which there are no assets currently in place. However, there is no requirement for these contributions to continue regardless of any possible surplus in the plan (ie. they are not MCRS). When there is surplus, these contributions can be reduced, or a contribution holiday can be put in place, as permitted by the legislation and plan documents related to OTPP and OPSEUPP. There is no requirement in OTPP and OPSEUPP to maintain a minimum level of contributions regardless of any surplus that may exist. Because of this, for the purposes of the calculations we prepared for you we determined that there are no MCRS as per 3250.56(a) that would need to be included in the asset ceiling calculation for these plans.

Further detail on these points, and additional matters for your consideration, are contained in the remainder of this document.

[2] Based on the Rate Stabilization Fund ("RSF") allocation as at 31 December 2014, the most recent funding valuation date, OPSEU has utilized their RSF $0.09B more than the Province. The Province portion, reflecting RSF allocation is determined as 50% x (1.95B-0.09B) +0.09B

“Perpetuity Assumption” and MCRS considerations

PSAS guidance

PS 3250.56 states **“***a government determines its expected future benefit the sum of:*

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

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

The purpose of the asset ceiling test is to ensure that the financial statements do not include any assets that the government cannot expect to benefit form. A pension asset may have a value if it can be refunded from the pension plan to the government (PS 3250.56(b) above), or it may have value if it can be used to reduce future contributions that otherwise might need to be made (PS 3250.56(a)). We understand based on the pension legislation and plan documents, and our discussions with the OPCD, that it would be difficult or impossible for the plan sponsors to withdraw assets from either OTPP or OPSEUPP. Thus, the only way the plan sponsors may expect to benefit from any surplus assets in the plan is via future contribution reductions or holidays. The asset ceiling test is used to determine the amount of assets that can be used in this way, and hence the amount of assets that can therefore be recognized on the balance sheet.

As PS 3250.57 states, the test is performed by first determining the total present value of all future service costs. This present value represents the total cost of all benefits that will be earned by plan members in the future. This cost can either be met through future contributions, or if there is a surplus in the plan and the legislation and the plan terms permit, from that surplus. This is the maximum amount of surplus that could be used to offset future cost, and therefore the maximum pension asset that the government could recognize on its balance sheet. Reducing this maximum value would be any contributions that the government/plan sponsors are required to make regardless of any surplus. The logic here is that if the plan sponsors must continue contributing to the plan even if the plan was in surplus (ie. “regardless of any surplus”), then the government’s benefit from that surplus is reduced. The reduction in the asset equals to the present value of any such MCRS.

As discussed in detail in the Pension Expert Panel report, neither OTPP nor OPSEUPP have any requirements that would compel the plan sponsors to continue to contribute into these plans, even if the plans were in surplus. The contribution levels for both plans are negotiated directly by the plan sponsors who make them, and the funding level of the plan is a key determining factor in those negotiations, allowing the plan sponsors to increase or decrease contributions as they deem appropriate, and reducing or eliminating any contributions that may not be needed if the plan is already in a surplus position. This is in contrast to other plans, some of which have requirements to continue contributing regardless of any surplus. For example, the public service pension plan in New Brunswick has a minimum contribution level of 8% of payroll that cannot be reduced. Therefore, this plan would have MCRS (ie. 8% of payroll) that must be used in the asset ceiling test. In our understanding, it is this requirement that results in full valuation allowance and no pension asset being recognized in New Brunswick government’s financial statements.

Canadian practice

The MCRS language contained in PS3250.56 mirrors the same language in other current and former Canadian standards:

- Part II – Accounting Standards for Private Enterprises (where 3462.69 has the same reference to MCRS)
- Part III – Accounting Standards for Not-for-Profit Organizations (which incorporates 3462 provisions)
- Part V – pre-changeover CICA 3461 (where 3461.105 has the same reference to MCRS)

Under all these standards, in our experience, the Canadian practice has been to interpret the "perpetuity assumption" and MCRS as we describe in this document, and in the same manner as we applied it in our calculations shared with you on 16 May 2017 for OTPP and OPSEUPP. We have never seen MCRS interpreted in a way that would treat any and all contributions as MCRS; to do so would be more in line with the type of analysis that would need to be carried out under IFRIC 14. However, IFRIC 14 only refers to minimum funding requirements, and does not qualify them as the requirements that exist "regardless of any surplus". This is the main reason that adoption of IFRIC 14 in Canada caused significant concern and discussion, that highlighted differences between IFRIC 14 requirements and the existing Canadian practice, with the "regardless of any surplus" qualifier being one of the key difference areas. In the non-IFRIC 14 context, the only instances where the "regardless of any surplus" qualifier applied, and affected the asset ceiling tests, were those where the employer had committed to a minimum contribution level that was not dependent on the funding status of the plan (eg. a commitment to match employee contributions of 4% of earnings).

Expert panel report

The Pension Asset Expert Advisory Panel report ("Report") stated the following:

> "*A question arises as to whether the surplus that is contemplated in the phrase "regardless of any surplus" is an accounting surplus or a funding surplus. The Panel understands that in practice actuaries interpret this to be a funding surplus. If any contributions are required even when there is a funding surplus, these would be "minimum contributions the government is required to make regardless of any surplus". This interpretation rests on the logic that funding contributions, including any minimum funding requirements, are driven by funding surpluses/deficits, and not accounting surpluses/deficits."*

The Report also outlines in detail how the funding contributions are set for OTPP and OPSEUPP. It concludes that there are no contributions that would be required to continue even if the plans were in a surplus position.

The recommendations of the Report are therefore consistent with the approach we describe in this document, and with our asset ceiling calculations shared with you on 16 May 2017 for OTPP and OPSEUPP.

Purpose of Asset Ceiling under PSAS

In our view, the purpose of the asset ceiling tests under PSAS, as well as other standards, is to ensure that only those assets that the government can expect to benefit from should be included on the balance sheet. Any assets that the government cannot expect to be able to use should be written down via a valuation allowance.

It is important to note that the true ultimate cost of a pension promise (ie. the total of all benefits paid to pensioners over time) does not depend on the measurement of that cost. In other words, both the funding valuations and the accounting valuations are attempting to measure the same real costs, each for a different

depend on how we measure it. Accounting and funding valuations merely allocate those costs to periods of time. With that in mind, it is reasonable to expect that in some periods the surplus or deficit will be measured differently under the accounting standards vs. funding valuations. Nevertheless, the economic question that the asset ceiling is attempting to address is if at any point there may be a surplus in the plan that for some reason could not be used either by reducing contributions or withdrawing assets. Put another way, there should only be an asset impairment if the plan is both overfunded, and the contributions could not be reduced in order to use up excess assets. While this may be the case for some plans, we understand that this is not the case for OTPP and OPSEUPP.

cc: Karen Hughes, Associate Deputy Minister
Helen Angus, Deputy Minister
Nadine Petsche, Director, Accounting Policy and Financial Reporting Branch

Pension Asset Ceiling.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
Subject: Pension Asset Ceiling
Date: Saturday, September 10, 2016 08:54:05

Hi Matt.

Just wanted to get back to you on the possible need for an accounting opinion on the pension asset ceiling work (as related to OTPP at this time). We will draft a statement of facts. As our original SOW didn't envision an accounting opinion, it would be helpful if you could provide an estimate of cost for such an opinion and let me know how much is left on the original engagement (just to check if would be sufficient to cover). This information will be helpful in upcoming internal discussions (if required).

Thanks in advance.

Nadine

Pension Comparison - question and timelines confirmation.rtf

From: Kaufman, Paul (TBS) []
To: Hatzis, Len (TBS) [Len.Hatzis@ontario.ca]; Murray Gold [mgold@kmlaw.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Pension Comparison - question and timelines confirmation
Date: Friday, September 16, 2016 20:38:18

Hi Murray -

To confirm our discussion, you are going to provide a comparative legal/governance analysis of how the frameworks for the two Ontario pension plans we identified (OTPP and OPSEU) and the four BC plans we identified (municipal, teachers, college, public service) compare on the issue of the authority of the pension boards and the plan partners to determine the utilization of plan surpluses. Your preliminary thinking is that in Ontario this determination is left to the partners, while in BC either the boards or the partners can make this determination.

You expect that you can provide this analysis by Monday or Tuesday.

We've provided the relevant joint trust agreements for the plans noted above and you don't expect that you need further documentation from us to respond to this request, but you will let us know if any need arises.

Cindy, if the above is inconsistent with what you are looking for please advise.

Paul

Pension Planning.rtf

From: Virani, Shyrose (TBS) []
To: christina.chan@ca.ey.com [christina.chan@ca.ey.com]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Chan, Vanessa W. (TBS) [Vanessa.W.Chan@ontario.ca]
CC: 'Gregory Winston' [gregory.winston@ca.ey.com]
Subject: Pension Planning
Date: Tuesday, December 12, 2017 11:21:00

Pension Planning.rtf

From: Virani, Shyrose (TBS) []
To: christina.chan@ca.ey.com [christina.chan@ca.ey.com]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Fong, Pauline (TBS) [Pauline.Fong@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]; Chan, Vanessa W. (TBS) [Vanessa.W.Chan@ontario.ca]
CC: 'Gregory Winston' [gregory.winston@ca.ey.com]
Subject: Pension Planning
Date: Tuesday, December 12, 2017 09:54:04

Pension Re-modelling.rtf

From: Fong, Pauline (TBS) []
To: Shayan.Jafrani@ca.ey.com [Shayan.Jafrani@ca.ey.com]
CC: christina.chan@ca.ey.com [christina.chan@ca.ey.com]; Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]; Patel, Bharat (TBS) [Bharat.Patel3@ontario.ca]; Sun, Alicia (TBS) [Alicia.Sun@ontario.ca]; Li, Wendy (TBS) [Wendy.Li@ontario.ca]; Ma, Patricia (TBS) [Patricia.Ma2@ontario.ca]
Subject: Pension Re-modelling
Date: Tuesday, June 06, 2017 16:57:05
Attachment 1: image002.jpg

Hi Shayan,

After our meeting today with Cindy, the direction right now is to open 2016-17 only and leave 2015-16 alone. As we are currently under tight deadlines for 2016-17 Public Accounts, we would like to know roughly how long it would take to do the detail re-modelling of OTPP, OPSEU & PSPP (including agency adjustments), using our current model and making changes it to align with the proposed?

As the detail modelling will likely involve the our team as well, we likely need you to come on site to go through things in detail so we are comfortable with all the pieces and incorporate any year-end adjustments we do as part of the model as well. Can you let me know tomorrow after having your internal discussions on the projected time-lines? Thanks.

Regards,

Pauline Fong, CPA, CA

Senior Analyst, External Reporting

Office of the Provincial Controller Division |Office of the Treasury Board |Treasury Board Secretariat

7 Queen's Park Crescent, Frost South, 2nd Floor, Toronto, ON, M7A 1Y7

Phone: (416) 212-4007

Pauline.fong@ontario.ca

image002.pdf

ONTARIO
150

Pension SOW (track changes and signed version).rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Pension SOW (track changes and signed version)
Date: Friday, September 16, 2016 22:01:41
Attachment 1: PwC SOW Signed npp to LD Sept 16.pdf
Attachment 2: PWC SOW Pensions Accounting Opinion 20160915 Comparenp to ld .docx

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Hi Lucy.

Please find attached a track changes version of the SOW reflecting additional edits based on review by our legal dept, as well as a signed copy for your signature. Please advise of any concerns or further edits required.

Thanks.

PwC SOW Signed npp to LD Sept 16.pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective September 16, 2016.

PricewaterhouseCoopers LLP (the "Vendor" or "PwC") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client" or the "Province") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of March 22, 2016 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$100,000.00, excluding HST.

4. *Project Start Date:* September 16, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide accounting advice (the "accounting advisory services") regarding the acceptability of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards. The accounting advice may include:

   - Review of background information, position papers developed by the Client or third parties that have been engaged by the Client to draft accounting positions on accounting for the recognition and measurement of pension assets for jointly-sponsored pension plans, and other supporting information.
   - Provide written or oral comments on draft position papers as provided by the Client with respect to the application of Canadian Public Sector Accounting Standards.
   - Participation in discussions with internal and external stakeholders and other parties as directed by the Client.

   During the course of this project, the Client will provide to PwC a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements with the Client's auditor. If an accounting opinion is to be provided, the Client's auditor will confirm to us in writing that the information the Client

has provided to PwC is complete and consistent with their knowledge of the facts and circumstances of the specific transaction.

If requested to by the Client during the course of the project, the Vendor shall provide an accounting opinion (the "accounting opinion"), prepared in accordance with Section 7600, *Reports on the application of accounting principles* of the CPA Canada Handbook – Assurance ("Section 7600"), regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards.

Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting advice or accounting opinion (if applicable), including discussions with the Office of the Auditor General.

The Client agrees that any accounting advisory services are solely for the information and use of the Client. Subject to the obligations in Article 27 (Privacy) of the Master Agreement the Client agrees that any written work product of PwC, other than an accounting opinion prepared in accordance with Section 7600, will not be made available to any other persons or entities. However the Client may provide access to PwC's observations to the Client's independent auditors solely for their informational purposes. The Client agrees to seek and obtain our written consent before including our accounting opinion (if applicable) or referring to us in any document disclosed to third parties, including disclosure of a summary of the accounting opinion or publication of the opinion in documentation that may be accessible to or intended for the public. The Vendor may, in their own discretion, waive the requirement to obtain written consent. The Vendor acknowledges that the Auditor General at its discretion may include the accounting opinion or refer to PwC LLP in documents disclosed to third parties, or may require the Province to do so, and the vendor agrees that the client is not in breach of this statement of work should this occur.

Acknowledgements and agreements

The Client acknowledges and agrees to the following:

a. The performance of the accounting advisory services does not constitute an engagement to provide audit, compilation, review or attest services in accordance with professional standards issued by the Chartered Professional Accountants of Canada ("CPA Canada") and, therefore, PwC will not express an opinion or any other form of assurance with respect to the accounting advisory services.
b. The accounting advisory services and accounting opinion (if applicable) to be provided do not include the delivery of any verbal or written advice on the application of accounting principles to a hypothetical transaction.
c. This engagement cannot be relied on to disclose internal control deficiencies, errors or fraud, should they exist.
d. PwC has no responsibility for updating the accounting advisory services or accounting opinion or for performing any additional services, except as agreed to in writing with the Client.
e. The Client's purpose for engaging PwC to perform the accounting advisory services is to supplement management's own technical accounting resources in performing accounting analysis and to assist management in making its determination as to the application of accounting principles and not to obtain an opinion from PwC as to such application, unless an accounting opinion is requested by the Client.

f. The Client shall be solely responsible for, among other things: (a) making all management decisions and performing all management functions; (b) designating one or more individuals who possess suitable skill, knowledge and/or experience, preferably within senior management to oversee the accounting advisory services (c) evaluating the adequacy and results of the accounting advisory services; (d) accepting responsibility for the results of the accounting advisory services; and (e) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities.

g. All management decisions and final conclusions reached in connection with the accounting advisory services will be the responsibility of the Client. PwC will not perform any management functions, make management decisions, or perform in a capacity equivalent to that of an employee of the Client.

h. PwC has no responsibility related to the Client's accounting or disclosure conclusions, whether or not such conclusions of the Client are related to the accounting advisory services and PwC has no responsibility for any disagreements between the Client and its independent auditor related to the Client's accounting.

i. The Client will be solely responsible for all decisions regarding the accounting treatment of any item or transaction and acknowledges that the accounting advisory services do not include the recording of any amounts in the Client's books or records. All amounts derived from the performance of the accounting advisory services will be reviewed and approved by, and will be the responsibility of, the Client's management.

j. The nature, scope and design of the accounting advisory services and the accounting opinion are solely the responsibility of the Client. PwC will rely, without independent verification, on the facts, information and assumptions provided by the Client. PwC will make no representation nor provide any assurance with respect to the adequacy of the services for the Client's purposes. Furthermore, PwC has no responsibility to advise the Client of other procedures that might be performed.

k. The Client will be solely responsible for providing accurate and complete information requested by PwC. PwC has no responsibility for the accuracy or completeness of the information provided by or on behalf of the client.

l. PwC's accounting and technical assistance will be based on the existing public sector generally accepted accounting principles. Should those generally accepted accounting principles be amended, superseded or revised in any manner, PwC's advice might change. PwC has no responsibility to inform the Client of any changes in generally accepted accounting principles that may occur after the completion of the engagement or any other oral or written work product prepared hereunder that would impact PwC's advice on the appropriate application of generally accepted accounting principles or to update its recommendations or any other oral or written work produce to take any such changes into account.

m. This engagement does not create a relationship between PwC and any person or party other than the Client. This engagement is not intended for the express of implied benefit of any third party.

n. The Client will identify an appropriate individual to serve as the project manager, including overseeing the accounting advisory services.

7. *Ownership and Licences* - **Attachment D** of the Master Agreement forms a part of this Statement of Work.

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be Lucy Durocher who is the engagement leader.

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

11. *Administrative Services and Supplies* – All administrative services and supplies used by the Vendor to complete the Services will be provided to the Client at no additional charge.

12. *Charges On Per Diem Rate Basis*– The Vendor and the Client agree that Work performed under this Statement of Work will be charged on a Per Diem Rate basis. The Per Diem Rate will vary, based on the nature of the final deliverable, as follows:

Nature of final deliverable	Per Diem Rate	Service Category	Estimated hours	Per Diem Rate
Accounting Advisory	General Consultant, Level 2	Service Category 2	20-25	$390/hour
Accounting Opinion	General Consultant, Level 2	Service Category 2	30-35	$990/hour

13. *Billing and Payment Process* – The Vendor shall invoice the Client in accordance with the requirements of the Master Agreement. Billing statements should include all billing information as set out in the Master Agreement.

13. *Names and Roles of Vendor's Personnel:*

Individual's Legal Name	Individual's Role and Experience Level	Service Category	Per Diem Rate
Lucy Durocher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Martin Boucher	General Consultant, Level 2	Service Category 2	See "charges on a per diem rate basis"
Sean Cable (or alternative as agreed to by the Client)	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"
Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client:	Treasury Board Secretariat, Office of the Provincial Controller Division
Branch:	Accounting Policy and Financial Reporting
Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027
Email:	Nadine.petsche@ontario.ca

15. *Knowledge Transfer:* The Vendor will work closely with the Client to ensure knowledge transfer to the Clients designated staff, and as necessary with the Auditor General.

16. *Destruction of Information* - The Vendor shall destroy all Confidential information contained on any media that was provided by the Client or at the direction of the Client, if requested to do so by the Client, except as required to be retained in accordance with professional standards requirements. The Client may choose to witness this destruction. The Vendor shall provide a certificate of destruction to the Client, if requested to do so by the Client.

17. *Client Representative and Receipt of Notices*

Client's address for receipt of notices:	**Treasury Board Secretariat**
Client Representative:	**Nadine Petsche**
Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

18. *Vendor Representative and Receipt of Notices*

Vendor's address for receipt of notices:	**PricewaterhouseCoopers LLP, PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2**
Vendor Representative:	**Lucy Durocher**
Telephone number:	**416-869-2311**
E-mail:	**Lucy.durocher@ca.pwc.com**
Backup Vendor Representative:	**Martin Boucher**
Telephone number:	**514-205-5415**
E-mail:	**Martin.boucher@ca.pwc.com**

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature: N. Petsche

Name: Nadine Petsche

Title: Director, Accounting Policy + Financial Reporting

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature: _____

Name: _____

Title: _____

I have the authority to bind the Vendor.

PWC SOW Pensions Accounting Opinion 20160915 Comparenp to ld .pdf

Statement of Work for Management Consulting Services

This Statement of Work no. **OPCD-PWC-01** is made in duplicate and effective ~~[insert date].~~September 16, 2016.

PricewaterhouseCoopers LLP (the "Vendor" or "PwC") and Her Majesty the Queen in right of Ontario as represented by the President of the Treasury Board (the "Client~~")~~" or the "Province") enter into this Statement of Work pursuant to the Master Agreement for Management Consulting Services made as of ~~June 16, 2014~~ March 22, 2016 between the Vendor and Her Majesty the Queen in Right of Ontario as represented by the Minister of Government and Consumer Services (such Master Agreement, as from time to time amended, is referred to as the "Master Agreement").

In consideration of their respective agreements set out below, the parties agree as follows:

1. *Structure* - The terms and conditions of the Master Agreement are hereby incorporated by reference in this Statement of Work to the same effect as if fully set out in this Statement of Work. This document and the Master Agreement together comprise a separate Statement of Work between the Vendor and the Client. All capitalized terms used in this Statement of Work without definition have the meanings ascribed to them in the Master Agreement. In the event of any conflict or inconsistency between any term or provision of this Statement of Work and any term or provision of the Master Agreement, the terms and provisions of the Master Agreement shall govern.

2. *Statement of Work* - The Vendor agrees to provide to the Client, and the Client agrees to acquire from the Vendor, the Services and Deliverables described in this Statement of Work upon and subject to the terms of this Statement of Work.

3. *Maximum Price:* C$~~xx0~~60100,000.00, excluding HST.

4. *Project Start Date:* September ~~15~~16, 2016.

5. *Project End Date:* December 31, 2016.

6. *Scope of Services and Deliverables* - The Services and Deliverables to be provided by the Vendor under this Statement of Work include the following:

   The Vendor shall provide ~~an accounting opinion~~accounting advice (the "accounting advisory services") regarding the acceptability of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards. The accounting advice may include:

   - Review of background information, position papers developed by the Client or third parties that have been engaged by the Client to draft accounting positions on accounting for the recognition and measurement of pension assets for jointly-sponsored pension plans, and other supporting information.
   - Provide written or oral comments on draft position papers as provided by the Client with respect to the application of Canadian Public Sector Accounting Standards.
   - Participation in discussions with internal and external stakeholders and other parties as directed by the Client.

   During the course of this project, the Client will provide to PwC a written statement of all relevant facts and assumptions, and a description of the circumstances and the nature of any relevant disagreements with the Client's auditor. If an accounting opinion is to be

Commented [LD1]: I do not have quick access to the copy of the Master Agreement. Per the Cap and Trade SOW this was March 22, 2016, so I am assuming it would be the same date for purposes of this SOW. Please confirm.

Commented [PN(2]: ok

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provided, ; and the Client's auditor will confirm to us in writing that the information the Client has provided to PwC is complete and consistent with their knowledge of the facts and circumstances of the specific transaction.

If requested to by the Client during the course of the project, the Vendor shall provide an accounting opinion (the "accounting opinion"), prepared in accordance with Section 7600, *Reports on the application of accounting principles* of the CPA Canada Handbook – Assurance ("Section 7600"), regarding the appropriateness of the Province's accounting treatment and measurement of pension assets for jointly-sponsored pensionspension plans on the consolidated financial statements of the Province prepared under Public Sector Accounting Standards.

Vendor may be required to participate in meetings with the Client and other stakeholders, and to support the Client with respect to the Vendor's accounting advice or accounting opinion, (if applicable), including discussions with the Office of the Auditor General.

VendorThe Client agrees that theany accounting advisory services are solely for the information and use of the Client. Subject to the obligations in Article 27 (Privacy) of the Master Agreement the Client agrees that any written work product of PwC, other than an accounting opinion or a summary of itprepared in accordance with Section 7600, will not be made available to any other persons or entities. However the Client may be disclosed by Ontario to the public,provide access to PwC's observations to the Client's independent auditors solely for their informational purposes. The Client agrees to seek and obtain our written consent before including our accounting opinion (if applicable) or referring to us in any document disclosed to third parties, including disclosure of a summary of the accounting opinion or publication of the opinion in documentation that may be accessible to or intended for the public. The Vendor may, in their own discretion, waive the requirement to obtain written consent. The Vendor acknowledges that the Auditor General at its discretion may include the accounting opinion or refer to PwC LLP in documents disclosed to third parties, or may require the Province to do so, and the vendor agrees that the client is not in breach of this statement of work should this occur.
[insert other services/deliverables required,

Acknowledgements and any termsagreements

The Client acknowledges and conditions in respect agrees to the following:

a. The performance of the accounting advisory services does not constitute an engagement to provide audit, compilation, review or attest services in accordance with professional standards issued by the Chartered Professional Accountants of Canada ("CPA Canada") and, therefore, PwC will not express an opinion, or any other form of assurance with respect to the accounting advisory services.

b. The accounting advisory services and accounting opinion (if applicable) to be provided do not include the delivery of any verbal or written advice on the application of accounting principles to a hypothetical transaction.
c. This engagement cannot be relied on to disclose internal control deficiencies, errors or fraud, should they exist.
d. PwC has no responsibility for updating the accounting advisory services or accounting opinion or for performing any additional services, except as agreed to in writing with the Client.
e. The Client's purpose for engaging PwC to perform the accounting advisory services is to supplement management's own technical accounting resources in performing accounting analysis and to assist management in making its

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determination as to the application of accounting principles and not to obtain an opinion from PwC as to such application, unless an accounting opinion is requested by the Client.

f. The Client shall be solely responsible for, among other things: (a) making all management decisions and performing all management functions; (b) designating one or more individuals who possess suitable skill, knowledge and/or experience, preferably within senior management to oversee the accounting advisory services (c) evaluating the adequacy and results of the accounting advisory services; (d) accepting responsibility for the results of the accounting advisory services; and (e) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities.

g. All management decisions and final conclusions reached in connection with the accounting advisory services will be the responsibility of the Client. PwC will not perform any management functions, make management decisions, or perform in a capacity equivalent to that of an employee of the Client.

h. PwC has no responsibility related to the Client's accounting or disclosure conclusions, whether or not such conclusions of the Client are related to the accounting advisory services and PwC has no responsibility for any disagreements between the Client and its independent auditor related to the Client's accounting.

i. The Client will be solely responsible for all decisions regarding the accounting treatment of any item or transaction and acknowledges that the accounting advisory services do not include the recording of any amounts in the Client's books or records. All amounts derived from the performance of the accounting advisory services will be reviewed and approved by, and will be the responsibility of, the Client's management.

j. The nature, scope and design of the accounting advisory services and the accounting opinion are solely the responsibility of the Client. PwC will rely, without independent verification, on the facts, information and assumptions provided by the Client. PwC will make no representation nor provide any assurance with respect to the adequacy of the services for the Client's purposes. Furthermore, PwC has no responsibility to advise the Client of other procedures that might be performed.

k. The Client will be solely responsible for providing accurate and complete information requested by PwC. PwC has no responsibility for the accuracy or completeness of the information provided by or on behalf of the client.

l. PwC's accounting and technical assistance will be based on the existing public sector generally accepted accounting principles. Should those generally accepted accounting principles be amended, superseded or revised in any manner, PwC's advice might change. PwC has no responsibility to inform the Client of any changes in generally accepted accounting principles that may occur after the completion of the engagement or any other oral or written work product prepared hereunder that would impact PwC's advice on the appropriate application of generally accepted accounting principles or to update its recommendations or any other oral or written work produce to take any such changes into account.

m. This engagement does not create a relationship between PwC and any person or party other than the Client. This engagement is not intended for the express of implied benefit of any third party.

n. The Client will identify an appropriate individual to serve as the project manager, including overseeing the accounting advisory services.

7. *Ownership and Licences* - **Attachment ~~E~~ D** of the Master Agreement forms a part of this Statement of Work.

Commented [LD3]: I do not have quick access to the copy of the Master Agreement. Per the Cap and Trade SOW this was attachment D, so I am assuming it would be the same attachment for purposes of this SOW. Please confirm.

Commented [PN(4]: OK

8. *Communications and Reporting* - The structure of Vendor's working relationship with OPCD is vital to the success of their engagement. Vendor's main point of contact will be ~~[insert name]~~,Lucy Durocher who is the ~~[insert title]~~.engagement leader.

9. *Work Location* - All meetings will be within the Greater Toronto Area.

10. *Working Hours* – The Client's normal working hours are 7.25 hours per day, between 8:15 a.m. to 4:30 p.m. Monday to Friday inclusive. If required by the Client, the Vendor must provide Services outside of the normal working hours and/or on non-Business days. The Vendor will not be entitled to charge more than the Per Diem Rate.

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~~[insert name]~~Martin Boucher	General Consultant, Level 2	Service Category 2	~~$~~See "charges on a per diem rate basis"
~~[insert name]~~Sean Cable (~~TBC~~or alternative as agreed to by the Client)	~~General Consultant~~Quality reviewer, Level 2	Service Category 2	~~$~~See "charges on a per diem rate basis"
Michael Walke	Quality reviewer, Level 2	Service Category 2	See "charges on a per diem rate basis"

~~**[Note to Draft: Confirm role and experience level and service category.]**~~

14. **Invoices** - Invoices for payment of any charges under this Statement of Work shall be sent to:

Client:	Treasury Board Secretariat, Office of the Provincial Controller Division
Branch:	Accounting Policy and Financial Reporting
Representative:	Nadine Petsche
Title:	Director, Accounting Policy and Financial Reporting
Phone number:	416-325-8027

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Email: Nadine.petsche@ontario.ca

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Telephone number:	**416-325-8027**
E-mail:	**Nadine.petsche@ontario.ca**

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Vendor's address for receipt of notices:	~~[insert address]~~PricewaterhouseCoopers LLP, PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
Vendor Representative:	~~[insert name and title]~~Lucy Durocher
Telephone number:	~~[insert telephone number]~~416-869-2311
E-mail:	~~[insert email address]~~Lucy.durocher@ca.pwc.com
Backup Vendor Representative:	~~[insert name]~~Martin Boucher
Telephone number:	~~[insert telephone number]~~514-205-5415
E-mail:	~~[insert email address]~~Martin.boucher@ca.pwc.com

IN WITNESS WHEREOF the parties hereto have executed this Statement of Work as of the date first above written.

HER MAJESTY THE QUEEN IN RIGHT OF ONTARIO, as represented by The President of the Treasury Board

Per:

Signature:

Name: _____

Title: _____

Pursuant to delegated authority.

PRICEWATERHOUSECOOPERS LLP

Per:

Signature:

Name: _____

Title: _____

I have the authority to bind the Vendor.

Pension advisory - expiration of mandate.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Pension advisory - expiration of mandate
Date: Tuesday, March 21, 2017 11:07:09

Hi Nadine,

I just spoke to Shyrose and she told me that the pension advisory engagement was dated up to December 2016, and so has expired.

If you expect that you may need my assistance on some of the CAATPP/HOOPP issues then perhaps Shyrose can move the unused room forward to 2017/2018. However, do we need to sign something to extend the time frame to be able to do this into the next fiscal year? Please advise.

Thanks,
Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

This e-mail is intended only for the person to whom it is addressed (the "addressee") and may contain confidential and/or privileged material. Any review, retransmission, dissemination or other use that a person other than the addressee makes of this communication is prohibited and any reliance or decisions made based on it, are the responsibility of such person. We accept no responsibility for any loss or damages suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

Ce courriel est strictement réservé à l'usage de la personne à qui il est adressé (le destinataire). Il peut contenir de l'information privilégiée et confidentielle. L'examen, la réexpédition et la diffusion de ce message par une personne autre que son destinataire sont interdits. Nous déclinons toute responsabilité à l'égard des pertes ou des dommages subis par une personne autre que le destinataire par suite de décisions ou de mesures fondées sur le contenu de cette communication ou autrement. Si vous avez reçu ce courriel par erreur, veuillez communiquer avec son expéditeur et en détruire toutes les copies.

Pension analysis.rtf

From: Petsche, Nadine (TBS) []
To: Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
Subject: Pension analysis
Date: Wednesday, October 19, 2016 17:00:21

Matt,
Wondering if we can chat when you have some time. N

Pension file.rtf

From: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Pension file
Date: Thursday, November 24, 2016 13:21:25

Hi Nadine,

I didn't get a chance to catch up with you after our meeting yesterday - I think everyone had other things to get to. I wanted to ask you how the pension panel presentation went on Friday?

Michael has mentioned that the SOW for the panel is being worked on - I am connecting with him on this.

In the meanwhile, it seems it would be a good time to send you an invoice for the rest of the work performed on the memo and slide deck for the panel. We currently have a WIP balance of $14,097, based on the agreed upon hourly rates. If you agree, I can get my assistant to draft up an invoice.

Lucy

Lucy Durocher
PwC | Partner, National Accounting Consulting Services
T: +1 416 869 2311
Email: lucy.durocher@ca.pwc.com
Assistant: Tracey Whelan | T: +1 416 941 8383 ext. 14223
PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto ON M5J 0B2
http://www.pwc.com/ca

This e-mail is intended only for the person to whom it is addressed (the "addressee") and may contain confidential and/or privileged material. Any review, retransmission, dissemination or other use that a person other than the addressee makes of this communication is prohibited and any reliance or decisions made based on it, are the responsibility of such person. We accept no responsibility for any loss or damages suffered by any person other than the addressee as a result of decisions made or actions taken based on this communication or otherwise. If you received this in error, please contact the sender and destroy all copies of this e-mail.

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Pension paper .rtf

From: Virani, Shyrose (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: Pension paper
Date: Friday, August 24, 2018 08:57:52
Attachment 1: 20180823150724654.pdf

Hi Lucy:

Thank you for returning my call. Basically I am looking for the above paper in final version. Would you be able to provide it to me?

Thanks
Shyrose

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Position paper for Ontario Teachers' Pension Plan

Preamble

This document addresses the accounting for pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, HOOPP and CAAT.

Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP.

As described in PSAS, a pension asset arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. Contributions reflect the funding objectives of the plan. The benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the asset balance (or plan surplus for accounting purposes) in OTPP is an asset to the province and it is suitable to reflect it in the financial results.

The OAG disagrees with this position. The OAG 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 Ontario Teachers' Federation (OTF) with respect to how the surplus would be utilized such that it would provide a benefit to the Province, a pension asset in the Public Accounts is not appropriate.

Ontario had followed the same pension accounting treatment for all of the past 14 years. This had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals. There has been no change to the relevant PSAS (i.e. RETIREMENT BENEFIT, Section PS 3250) over the past 14 years.

A regulation was filed to allow the public service to sign-off on the impact of the OAG's view on accounting for pension assets in Ontario's 2015-16 financial statements. The regulation is time-limited and legislates the accounting for pension assets of its two jointly-sponsored pension plans (OTPP and

OPSEUPP) for 2015-16 in a manner that is consistent with the fiscal outcome proposed by the Auditor General. The impact of the change resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's accounting, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to reflect the Auditor General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt.

Background

Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1.

The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the Ontario Teachers' Federation represented by its Executive (the "OTF") (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. The OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for the OTPP ;

---

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
a. It provides defined benefits.
b. The defined benefits are contributory benefits.
c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners Agreement (FMP);
f) The Ontario Teachers' Pension Plan; and
g) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA 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 TPA the Province is required to make additional contributions to the OTPP in the event that there are insufficient assets to make required payments out of the plan in any particular year. [5] The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (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, in practice there has been 50/50 cost sharing of the normal contribution cost under the OTPP since the OTPP became jointly sponsored (and

Commented [CV1]: Let's discuss this next section – its new to me – was it in one of the legal opinions?

Yes, per the Osler September 20, 2016 letter – pages 7 and 8 – included in this section as we discuss that OTPP qualifies as a JSPP

Also – I'm confused by the footnotes below – 3. And 4. And then 2.3.4.?

The characteristics of a JSPP in footnote 1 includes 4 parts which were the first series of 1, 2, 3 and 4 – I have changed to a, b, c and d

Commented [CV2]: Does this have any impact on the JSPP status of the plan

I believe it is consistent with the characteristics of a JSPP- characteristic c

LD – I think there are a number of ways to interpret this clause It could be argued that the clause is there to ensure that there is sufficient money from a liquidity perspective. This does not necessarily negate the broader agreement to share on an equitable basis – i.e. it's not clear if this injection by the Province would be balanced by the OTF in some other form – one might argue that the rest of the arrangement (partner's agreement) would require it to.
The TPA does require that the assets of the pension fund should be maintained at a level that is reasonably sufficient to meet the liabilities. Therefore, if this requirement has been met then the requirements of subsection 5(3) would only be for liquidity/short term in nature and not for long term funding.

I can see how one might also argue that it indicates that residual risk is with the Province – for example, does this clause kick in when the pension plan has no more active members and runs out of assets to pay for the liabilities then is the Province on the hook. Again – the rest of the Plan's terms would indicate that this should not happen, While "should not" might not be the same as "cannot" it could be countered that the majority of the funding risk is not with the province, because the other requirements in the Partners' Agreement require shared funding.
However this would likely be a matter of interpreting the arrangement as a whole.

I don't know what the original thinking by mgt/OAG was when this was agreed upon to be a JDBP, but the above would be my guess as to how it was considered.

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).
[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).

for the majority of periods of time since the inception of the plan in 1917). [7] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Currently, the Sponsors are required to mutually agree upon how any plan deficits are to be addressed. [8] 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.

Commented [CV3]: Not sure what we are referring re: the use of also

Section 3.11 of the FMP discusses options available to the partners to eliminate any deficit in the plan (i.e. change benefits, contributions, or both)

Joint governance and cost sharing form two of the core features of the OTPP. Consistent with the equal sharing of risk permitted under a JSPP, 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.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the Sponsors are included in appendix E. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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):

---

[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/101791209401-l5e47lc2b-23f1-44e6-b5cld22e3e50dbc3lHow+ Contribution+Rates*HaverEvolved.pdf As noted above, for the period from January l, 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%/11.20lo versus l0.4yo/l2Vo, 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.

[8] See, for example, Section 3.09 and 3.11 of the FMP.

Pension paper.rtf

From: Virani, Shyrose (TBS) []
To: Hosick, Sarah (TBS) [Sarah.Hosick@ontario.ca]
Subject: Pension paper
Date: Tuesday, August 28, 2018 12:16:33
Attachment 1: Draft Pension Asset Position Paper November 14 PwC clean.docx

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25C

We noted that you left the contract information sheet blank for “evidence of any deliverable(s) received.” Can you confirm that there is nothing available for this in terms of support? (i.e. per SOW: report for the accounting opinion received, written comments on draft position papers, etc.)

Yes; Support for deliverable received (if any)

See attached

Draft Pension Asset Position Paper November 14 PwC clean.pdf

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Position paper for Ontario Teachers' Pension Plan

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1.0 Preamble

This document addresses the accounting for the net pension assets by the Province of Ontario in relation to the Ontario Teachers' Pension Plan (OTPP).

The constating documents of OTPP are different from those of the Ontario Public Service Employees' Union Pension Plan (OPSEUPP), the Healthcare of Ontario Pension Plan (HOOPP), and the CAAT pension plan (CAAT). The appropriate accounting for OTTP may be different than for other pension plans in Ontario as well as pension plans in other provinces, for example New Brunswick and British Columbia, as a result of differences in the respective constating documents.

2.0 Issue to be considered

In connection with the preparation and audit of the 2015-16 Public Accounts, the Office of the Auditor General of Ontario (OAG) and the government's professional accounting staff disagreed on an appropriate application of Public Sector Accounting Standards (PSAS) to net pension assets related to two pension plans that the Province jointly sponsors –OTPP and OPSEUPP. This position paper addresses the analysis for OTPP. A separate document will provide further analysis on the Province's accounting in relation to OPSEUPP, as well as HOOPP and CAAT.

This position paper addresses the following three questions in relation to the accounting for OTPP:

1. For accounting purposes, what type of pension plan is OTPP (i.e. how should OTPP be classified under Public Sector Accounting Standards (PSAS))?
2. As a result of the classification, how should the Province of Ontario account for the pension surplus of OTPP in the Public Accounts?
3. How should the pension asset of OTPP be measured in the Public Accounts of the Province of Ontario?

3.0 Conclusions

The following conclusions were reached regarding each of the above questions:

1. Classification of OTPP - The Province has concluded that OTPP meets the definition of a joint defined benefit plan as the Province and Ontario Teachers' Federation are shared sponsors of the plan. The Teachers' Pension Act, the Partners' Agreement and the plan text for OTPP collectively set out this shared control and equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a joint defined benefit plan in RETIREMENT BENEFITS, Section PS 3250 in PSAS. The classification of OTPP as a joint defined benefit plan for accounting purposes has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

2. Recognition of a pension asset for a joint defined benefit plan - The Province has concluded that PSAS (Section PS 3250) supports the recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets be subject to unilateral control. Shared control is relevant and appropriate for a situation involving a joint defined benefit plan. The Province's share of OTPP's pension surplus meets the definition of an accrued benefit asset under Section PS 3250 which requires the Province to recognize its portion of the plan (50% for OTPP).
3. Measurement of a pension asset - The Province has concluded that the attributes of the joint defined benefit plan arrangements for the OTPP entitle the Province to access its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surpluses to reduce contributions in the future. The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of those models to date no valuation allowance appears to be required and the OTPP pension assets should be recorded on the books of the Province. The Province recognizes that professional judgement must be applied in deriving an estimate of a potential valuation allowance under Section PS 3250.

4.0 Background Information

4.1 Accrued benefit asset

As described in PSAS, an accrued benefit asset (net pension asset) arises when the government's total contributions to a plan, including income earned thereon, are greater than the cumulative retirement benefit expense recognized since the start of the plan. An Accrued Benefit Asset (AcBA) includes the effect of net unamortized experience gains or losses. Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation. OTPP currently has net unamortized experience gains. The following illustration reflects the compilation of the net pension asset (accrued benefit asset) reported on the Province's books for the OTPP.

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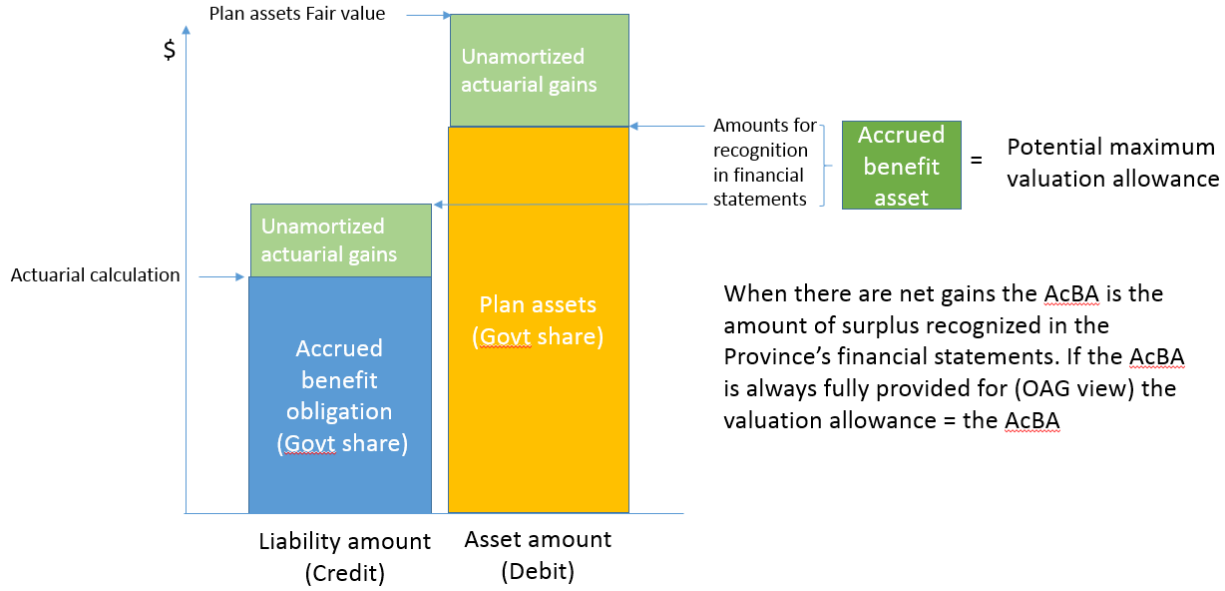
An Accrued Benefit Asset (AcBA) occurs when there is a plan surplus, including the effect of net unamortized experience gains or losses. OTPP currently has net unamortized experience gains.
Actuarial (experience) gains can occur in respect to both plan assets as well as the pension obligation



It is important to note that contributions to the plan are based on funding objectives of the plan. In contrast, benefit expense reflects the estimated cost of the pensions earned during the year that will be paid out to retirees in the future.

The Province's position is that the net asset balance (plan surplus for accounting purposes) in OTPP is an asset to the Province and it is appropriate to reflect it in the financial results in accordance with PSAS. The Province has also concluded that no valuation allowance under PSAS is required against the asset as at March 31, 2016.

The OAG disagrees with the Province's position. Specifically, the OAG has indicated that the Province does not have the legally enforceable right to unilaterally access the assets of the plan, and as such that the Province does not control the assets which the OAG interprets PSAS as requiring. Further, the OAG considers the lack of an enforceable agreement at year-end with the Ontario Teachers' Federation (OTF as the joint sponsor of the plan) that would provide for lower contributions in the future as requiring that a full asset valuation allowance be taken against the net asset under PSAS.

Financial statements for the Province have been prepared over the prior 14 years in accordance with the CPA Canada Public Sector Accounting (PSA) Handbook. RETIREMENT BENEFITS, Section PS 3250 of the PSA Handbook, addresses the accounting of obligations for employee retirement benefits in government financial statements. Since 2001, there have been no consequential changes to Section PS 3250. As a result Ontario has followed the same pension accounting treatment for OTPP over the past 14 years. The pension liability (asset) and expense reported by the Province of Ontario for OTPP over the period is reflected in Appendix A. Unqualified audit reports have been received for each of the years from the

OAG on the Public Accounts. The pension accounting initially adopted by the Province for OTPP had been accepted by the current Auditor General for the last two years and by the three previous Auditors Generals for the prior years.

In light of the contrasting views on interpretation of PS 3250 to the Province's jointly sponsored pension plans, a regulation was necessary to allow the public service to sign-off on the impact of the OAG's view on accounting for net pension assets in Ontario's 2015-16 financial statements. The regulation is time-limited and legislates the accounting for net pension assets of its two jointly-sponsored pension plans (OTPP and OPSEUPP) for 2015-16 in a manner that is consistent with the interpretation proposed by the Auditor General. The change in accounting treatment for 2015-16 resulted in an additional $10.7 billion being added to the net debt and accumulated deficit and an increase in the 2015-16 annual deficit of $1.5 billion.

To clarify, the government's regulated accounting for the 2015-16 Public Accounts although resulting in a consistent fiscal impact as would be reflected under the Auditor General's interpretation, does not reflect the Province's interpretation of pension accounting under the PSAS.

On October 5, 2016, the Auditor General issued a qualified report on the 2015-16 Public Accounts. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to reflect the Auditor General's interpretation of PSAS. Restating the previous year's results would have had no impact on the financial results for 2015-16, including the annual deficit and net debt and would have only been appropriate if the government had agreed with the Auditor General's interpretation of PSAS which would have acknowledged errors in the prior year's comparative results.

4.2 Overview of OTPP

OTPP is a jointly sponsored pension plan[1] (JSPP) as defined in the *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 and as established under the *Teachers' Pension Act (Ontario),* R.S.O. 1990, c. T.1. The sponsors of OTPP are the Province of Ontario (the "Province"), through the Minister of Education and the OTF (collectively, the "sponsors").

The plan administrator of the OTPP is a board of directors. The plan administrator is an independent entity, members of which are appointed by the sponsors.

[1] **Jointly sponsored pension plans**
(2) For the purposes of this Act, a pension plan is a jointly sponsored pension plan if it has the following characteristics:
a. It provides defined benefits.
b. The defined benefits are contributory benefits.
c. Members of the pension plan are required, by virtue of the documents that create and support the plan, to make contributions in respect of any going concern unfunded liability and solvency deficiency of the plan.
d. The plan satisfies such additional criteria as may be prescribed. 2005, c. 31, Sched. 18, s. 1 (2).

The constating documents for OTPP set out the respective rights of the sponsors, and describe the powers of the plan administrator. OTPP is governed by:

a) The *Teachers' Pension Act* (TPA), R.S.O. 1990, c.T.1 (TPA);
b) The *Pension Benefits Act (Ontario),* R.S.O. 1990, c. P.8 (PBA) and the regulations thereunder (PBR);
c) Plan text for OTPP ;
d) An agreement between Her Majesty the Queen in right of the Province of Ontario represented by the Minister of Education and Training and The Ontario Teachers' Federation represented by its Executive, dated July 15, 1991, as amended (The Partners' Agreement);
e) A Funding Management Policy, attached as Appendix A to the Partners' Agreement (FMP); and
f) The Term Sheet agreed to by the Sponsors dated March 13, 2013 (the "2013 Term Sheet") describing the implications of the Freeze Period on the Funding Management Policy.

Three material implications for OTPP as a result of qualifying as a JSPP under the PBA are:
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. [2]
2. Funding – OTPP is exempt from solvency funding requirements under the PBR. [3]
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. [4]

With respect to the cost-sharing principle referred to in #3 above, the TPA contains limitations on the contributions that the Province (and other participating employers) may make under 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 TPA the Province is required to make additional contributions to OTPP in the event that there are insufficient assets to make required payments out of the plan in any

[2] PBR, subsection 3.1(1).
[3] PBR, subsection 1.3.1(3).
[4] PBA, subsection 1(2) and subsection 55(4).

particular year. [5] This clause has been interpreted as a short term solvency protection clause, rather than a clause that transfers substantive residual risk to the Province, as the rest of the arrangement is structured such that the risk of these payments is minimal and the risks of the long term funding of the plan must still be equitably shared. The Province is also permitted to make additional contributions in respect of a solvency deficiency[6] (although, as noted above, solvency funding is not required under OTPP). Notwithstanding that subsection 5(1.1) of OTPP provides a cap on the Province's normal cost contribution obligation, rather than requiring 50/50 cost sharing, in practice there has been 50/50 cost sharing of the normal contribution cost under OTPP since OTPP became jointly sponsored (and for the majority of periods of time since the inception of the plan in 1917). [7] The plan text itself also provides for equal contributions, at the basic level (see sections 25(1) and 26(1)).

Joint governance and cost sharing form two of the core features of OTPP. Consistent with the equal sharing of risk permitted under a JSPP, there is a requirement for decisions relating to plan design and plan amendments to be made jointly by the sponsors. In this regard, the Partner's Agreement requires the sponsors to negotiate and agree upon decisions relating to surplus or deficit utilization, which currently is outlined in the FMP. [8] The FMP indicates that deficits (or surpluses) may be addressed through increases (decreases) to the contribution rates, lowering (increasing) the amount of indexation and/or other decreases (increases) in benefits. While not binding upon the sponsors, as the sponsors can change the FMP at any time, any changes are required to have the mutual consent of both sponsors. Accordingly, the sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process.

Additional excerpts from constating documents for OTPP relating to use of the Plan's surplus and the sharing of responsibilities amongst the sponsors are included in appendix B. Some important elements of these are:

1. Paragraph 10(1)3 of the TPA 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

[5] TPA, subsection 5(3).
[6] TPA, subsection 5(7).
[7] See, Ontario Teachers' Pension Plan: "How Contribution Rates Have Evolved" available at: https://www.otpp.com/documents/10179/20940/-/5e471c2b-23f1-44e6-b5c1d22e3e50dbc3/How+ Contribution+Rates+Have+Evolved.pdf As noted above, for the period from January l, 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%/11.20% 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.
[8] See, for example, Section 3.09 and 3.11 of the FMP.

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 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 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 funding surpluses that may arise under the plan.

4. Negotiations on the use of the surplus occur as specified in the Partners' Agreement. The Partner's Agreement requires that any actuarial funding valuation submitted to the pension regulators must be "actuarially balanced" (Section 57 of the Partners' Agreement). This must occur at least once every three years, but can occur every year if the partners agree. If a preliminary funding valuation shows a funding surplus or deficit then the joint sponsors must negotiate how this surplus or deficit is to be resolved prior to filing the funding valuation.

4.3 Accounting for OTPP by the Province

Since fiscal year 2001-2002, the Province has recorded a net pension asset for OTPP on the Statement of Financial Position in accordance with Section PS 3250. A net pension asset has arisen because the government's share (50%) of the total contributions to OTPP plus recognized investment returns on the plan's assets have exceeded the government's share of the accumulated retirement benefit expense (see illustrative examples in Appendix J). The accounting for the accrued benefit obligation results from a complex process involving significant assumptions and actuarial calculations covering a very long time frame as is required by RETIREMENT BENEFITS, Section PS 3250.

The various valuations prepared for the OTPP – i.e. those for the Province's public accounts, those for the funding valuation and those for the OTPP stand-alone financial statements, can create confusion when assessing the Province's accounting. Therefore, this next section sets out the differences in those valuations.

With regards to any comparisons between surplus or deficit amounts reported in the Province's financial statements verses OTPP's financial statements or funding reports, it is important to acknowledge the different objectives of funding and accounting for a pension plan which are also explicitly addressed in Section PS 3250 as follows:

> *.008 Determining whether a retirement benefit plan should be funded and the amount to be funded each period is a financial management matter. The funding objective is to determine an acceptable policy for financing the estimated ultimate cost of a benefit plan. An actuarial valuation for funding purposes is performed to calculate the contributions required to secure the benefits promised.*
>
> *.009 The accounting objective is to measure and report the obligation for employee retirement benefits and to attribute the costs of those benefits to the periods in which the related services are rendered. To meet that objective, a method is needed to determine the amount of the obligation for retirement benefits outstanding, which represents the liability at the financial statement date, and the value of the benefits employees earned during the period, which represents the expense of that period. …*
>
> *.010 Because the objectives of determining the most appropriate funding policy are not necessarily the same as those of determining the most appropriate accounting method, the liability for accounting purposes may not be the same as the amount due but not yet funded at the financial statement date according to the funding plan. In addition, the retirement benefit expense of the period for accounting purposes may not be the same as the contribution computed in the period for funding purposes.*

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Section PS 3250 paragraph .051 includes an explicit acknowledgement that the accounting position and funding position can be quite different, as follows: “Contributions reflect the funding objectives of the Plan. The benefit expense reflects the accounting objectives and may differ for a number of reasons…”

OTPP’s most recent preliminary funding valuation reported a preliminary funding surplus of $13.2 billion as at January 1, 2016, as reported on the OTPP website (https://www.otpp.com/home). The Province’s relative portion of this surplus would be $6.6 billion. OTPP’s published stand-alone financial statements showed a deficit for accounting purposes of $1.8 billion in its financial statements as at December 31, 2015, for which the Province’s portion would be a deficit of $900 million. The following background helps to clarify the reasons for these different results. OTPP’s financial statements are prepared under accounting standards for pension plans in Part IV of the CPA Canada Handbook (“Part IV”), which is a different accounting framework than the Province uses for its financial reporting and is also a different framework than is used to calculate the net surplus or deficit for funding purposes.

Accounting for employee future benefits requires the use of assumptions and methodologies to calculate both the obligation incurred to date and the value of the assets already set aside to meet those obligations. Accounting frameworks differ in standards that must be applied in determining appropriate assumptions and methodologies. Further, the assumptions and methodologies used in developing a “funding valuation” on a going concern basis also differ from those required by accounting standards. These differences result in a number of different valuations for the same plan, depending on the purpose of the valuation and can be affected by certain choices made between acceptable options within each framework. A summary of the main differences between the methodologies used to calculate a going concern funding valuation, OTPP’s accounting valuation and the Province’s accounting valuation is shown in Appendix D.

Specifically, the discount rate used to value the obligations of the plan has a significant impact on the overall position of the plan. A lower discount rate results in a higher liability and a higher discount rate results in a lower liability, all else being equal. Put another way, a higher estimate of the time-value of money results in the value the promises made today that will be paid out in the future cheaper. OTPP uses a discount rate based on corporate/government bond rates in its financial statements, as permitted by Part IV. The Province uses a discount rate based on the expected asset return, as permitted by PSAS. The rationale for using a corporate or government bond approach is that a pension promise is akin to a bond as it is a promise to pay a series of cash flows in the future regardless of what the asset returns actually are (which could be higher or lower than expected). The rationale for using an asset return approach is that it represents the amount of contributions that, combined with investment returns, should be sufficient to pay the promised benefits, particularly as pension plans will often invest in higher risk/higher return assets then simple corporate bonds. Both a discount rate based on the expected asset return and one based on corporate/government bonds are “best estimate” rates; they must both be based on management’s best estimate of the applicable discount rate. In both cases the estimates must be supportable. The difference results not from one being more “right” or “wrong” relative to the other but from fundamentally different approaches within the accounting standards to what the discount rate should be.

Typically the funding discount rate used for the funding valuation falls between the bond discount rate and the expected asset return, but it differs in that it does not purport to be the "best estimate" of the discount rate, rather it is designed to indicate the contributions that are required to fund the promised benefits with an additional conservative margin for adverse deviations. Note that over the long term the difference between funding valuations and accounting valuations would diminish as the impact of the discount rate unwinds and the asset valuation methods converge.

In practice, the discount rates used in the financial statements of government sponsored and joint defined benefit pension plans prepared under Part IV of the CPA Canada Handbook (Section 4600) use diverse methodologies. For example, in Alberta there are seven plans which prepare their financial statements under Part IV with reference to IFRS (same framework as OTPP). Of these none use a government bond discount rate and all use a discount rate calculated with some reference to a rate of return on invested assets, which may include factors for expenses, diversification and rebalancing. The analysis of a number of government sponsored plans is included as Appendix E. The analysis demonstrates that in their stand-alone financial statements, a significant number of government sponsored plans use a discount rate aligned to an asset investment return rather than a bond discount rate. OTPP is actually in the minority of plans that choose to use the rate required by IFRS, resulting in a lower discount rate and higher liability for financial reporting purposes.

The above analysis explains how different discount rates impact the net surplus/deficit reported on OTPP's financial statements, OTPP's funding reports and the Province's financial statements. The fact that OTPP reports a deficit on its financial statements, or that the 50% of the net surplus reported by OTPP for funding purposes is lower than the surplus reported on the government's financial statements under PSAS does not impact the net pension asset amount or pension expense reported by the Province for OTPP.

To further clarify, that there is a deficit reported in OTPP's stand-alone financial statements while the Province of Ontario calculates a surplus under PSAS requirements does not mean that there is no accounting surplus and therefore no reportable asset for the Province. In fact, **if** OTPP had chosen (as an acceptable accounting policy choice) to use a discount rate more consistent with its counterparts in other jurisdictions (see Appendix E) such as a discount rate based on an expected asset return which would be closer to that used by the Province, it would eliminate much of the existing difference between the reported net surplus/deficit amounts in OTPP's stand-alone financial statements and the Province's share of OTPP reported for accounting purposes in the Province's Public Accounts.

4.4 Applicability of PS 3250 as primary source of GAAP

GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section PS 1150 prescribes that, in developing and applying accounting policies, all primary sources of GAAP should be applied (Section PS 1150 paragraph .04). Primary sources of GAAP are Sections PS 1201-PS 3510, Public Sector Guidelines and appendices and illustrative material to those pronouncements. Only when there are no primary sources of generally accepted accounting principles (GAAP) that relate to the transactions or events under consideration, or more specific guidance is needed (Section PS 1150 paragraph .05), does an entity

consider other primary sources of GAAP dealing with similar issues and also the concepts described in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 (issued January 2003). Section PS 1000 is not, however, a "primary source of GAAP" under the PSA Handbook.

The primary sources of GAAP specific to the accounting for pension assets is RETIREMENT BENEFITS, Section PS 3250 (issued in September 2001 replacing the prior EMPLOYEE PENSION OBLIGATIONS, also titled Section PS 3250).

Other primary sources of GAAP that deal with similar issues might also be considered where additional interpretation or guidance may be required. For the issues dealt with in this paper - recognition and measurement of a joint defined benefit plan - this could include standards that relate to shared control, as OTPP is a joint defined benefit plan, standards that relate to the definition of an asset and standards that relate to measurement uncertainty:

- GOVERNMENT PARTNERSHIPS, Section PS 3060 (issued in October 1999)
- ASSETS, Section 3210 (issued in June 2015, effective from April 1, 2017)
- CONTINGENT ASSETS, Section 3320 (issued in June 2015, effective from April 1, 2017)
- MEASUREMENT UNCERTAINTY, Section PS 2130 (issued in April 2005)

There have not been consequential changes to any of the above standards since their introduction into the PSA Handbook. Furthermore, all the standards were developed several years ago with the exception of ASSETS, PS 3210 and CONTINGENT ASSETS, Section PS 3320 which are more recent and will be effective in for periods beginning on or after April 1, 2017. Section PS 3210 provides additional guidance on the various components of the existing asset definition found in Section PS 1000; it does not change the definition.

5.0 Question 1 – Classification of a pension asset

The analysis below addresses whether the Province's share of the pension surplus in OTPP, calculated in accordance with PSAS under Section PS 3250, represents a reportable asset to the Province of Ontario in the Public Accounts.

5.1 RETIREMENT BENEFITS PSAS 3250

The focus of the following analysis is on the accounting requirements in RETIREMENT BENEFITS, Section PS 3250 as this standard is a primary source of GAAP which specifically addresses the accounting for pension assets. The following highlights some key concepts and guidance contained in this standard.

5.1.1 Section PS 3250 – Purpose and Scope

The purpose and scope of Section PS 3250 is included in paragraph .001 which states:

PURPOSE AND SCOPE

> *.001 This Section establishes standards on how to account for and report obligations for employee retirement benefits in government financial statements. Other employee future benefits are specifically dealt with in POST-EMPLOYMENT BENEFITS, COMPENSATED ABSENCES AND TERMINATION BENEFITS, Section PS 3255.*

Obligations for retirement benefits are further explained in RETIREMENT BENEFITS, Section PS 3250.003 as follows:

> *.003 Obligations for **retirement benefits** result from a promise by a government to provide these benefits to employees because of retirement in return for their services. Pensions and other retirement benefits, such as extended health care and life insurance benefits, are a form of compensation offered for services rendered and accrue over the years employees render those services. The fundamental accounting task is to determine the amount of the obligation for retirement benefits to attribute to each period of employee service. Determining such amounts involves not only accounting for past transactions and events; it also requires forecasts of future events, such as inflation, investment returns, medical costs and employee turnover and mortality.*

RETIREMENT BENEFITS, Section PS 3250 applies to the accounting for OTPP in the Province of Ontario's financial statements as the pension plan represents an obligation of the Province to provide retirement benefits to the members of the plan in return for their services.

5.1.2 PS 3250 – Types of pension plans

RETIREMENT BENEFITS, Section PS 3250 addresses the accounting for different types of pension plans including:

- defined benefit plans (of which joint defined benefit plans are a subset),
- defined contribution plans, and
- multi-employer and multiple-employer benefit plans.

The definition of a joint defined benefit plan is included in the glossary to Section PS 3250 as follows:

> *A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:*
>
> *(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;*
>
> *(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;*
>
> *(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and*

> *(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.*
>
> *The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.*

Additional guidance on identifying joint defined benefit plans (JDBPs) is in Section PS 3250 paragraphs .79 to .80 which similarly highlight the importance of both shared control and shared risks and rewards in a JDBP as follows:

> *.079 Governments may participate jointly in defined benefit plans where the government shares the risks and rewards jointly with plan participants, represented by a sponsor or sponsors. Joint defined benefit plans are governed by a formal agreement between the sponsors, which establishes that the sponsors have shared control over the plan. A governing board is generally appointed by the joint sponsors with equal representation and a mutually agreed-upon chair.*
>
> *.080 A government would consider the characteristics of the plan to determine whether it meets the definition of a joint defined benefit plan. In a joint defined benefit plan, funding contributions are shared mutually between the government and the plan members. The sponsors have control over decisions related to the administration of the plan and the level of benefits and contributions on an ongoing basis based on the terms of the contractual agreement. The sponsors share, on an equitable basis, the significant risks associated with the benefit plan. Risk would not be considered to be equitably shared in an arrangement where the government and the joint sponsors fund the plan equally but where the government retains the full risk of the accrued benefit obligation. If the government retains the residual risks it is unlikely that the plan meets the definition of a joint defined benefit plan.*

It should be noted that the definition of a JDBP under Section PS 3250 is not the same as the definition of a JSPP under the PBA, although there are some overlapping concepts between the two. A JDBP is a unique sort of retirement benefit plan where the sponsors have shared control over the plan. As a result, no one party can, by itself, control decisions around funding, benefits and other matters; funding contributions, risks and benefits are to be shared mutually between the sponsors. The Province has concluded that OTPP meets the definition of a JDBP as the Province and OTF are sponsors of the plan. OTPP is a contractual arrangement between the Province and OTF in which:

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

(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 5(1.1) of the TPA for example);

(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis (addressed in paragraph 8 of the Partners' Agreement for example) ; and

(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor (addressed in paragraph 10(1)3 of the TPA for example).

The TPA, the Partners' Agreement and the plan text collectively set out this shared control and that the Province of Ontario has an equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a JDBP.

The classification of OTPP as a JDBP for accounting purposes [and a JSPP under the PBA] by the Office of the Provincial Controller has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

5.2 Conclusion on classification

The Province has concluded that OTPP meets the definition of a joint defined benefit plan as the Province and Ontario Teachers' Federation are shared sponsors of the plan. The Teachers' Pension Act, the Partners' Agreement and the plan text for OTPP collectively set out this shared control and equitable sharing of the risks and rewards (surpluses and deficits) of the plan, thus meeting the definition of a joint defined benefit plan in RETIREMENT BENEFITS, Section PS 3250 in PSAS. The classification of OTPP as a joint defined benefit plan for accounting purposes has been consistent since 2001 and had been consistently accepted without question by the OAG, including throughout the 2015/16 Public Accounts.

6.0 Question 2 – Recognition of a pension asset for a JDBP

6.1 Standards in the PSA Handbook

RETIREMENT BENEFITS, Section PS 3250 paragraphs .081 to .082 provide guidance on the accounting for a JDBP in the financial statements of the government sponsor. As OTPP meets the definition of a JDBP for the reasons noted above, the relevant guidance for the Province for purposes of reporting retirement benefits in the Public Accounts includes:

> *.081 When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans. [SEPT. 2001]*
>
> *.082 A government may convert an existing defined benefit plan for which it is the sole sponsor to a joint defined benefit plan where the risks and benefits are shared. When converting to a joint plan, a government would consider whether there are any special accounting issues that arise, including whether the predecessor plan has been settled or partially settled and/or curtailed or partially*

> *curtailed. In assessing such issues a government would have regard to its specific circumstances and the terms of the joint defined benefit plan.*

Section PS 3250 paragraph .081 clearly states that "The government should account for its portion of the plan in accordance with the standards for defined benefit plans". It is clear from this that only the government's portion of the plan is included in the government's financial statements consistent with the requirements of Section PS 3250 (recognition) and the measurement of that portion is based on the requirements of Section PS 3250 (measurement). It is also then clear that the requirements of the standard for recognition and measurement, including the Limit of the Carrying Amount of an Accrued Benefit Asset guidance, are designed to be applied to a shared control situation and not only to situations where there is unilateral control. If it was intended that no pension asset could be recognized because the asset was subject to shared control and not unilateral control Section PS 3250 paragraph .081 would have made this clear. This paper discusses the question of measurement separately in Question 3.

The balance sheet recognition guidance for retirement benefits is stated in Section PS 3250 paragraphs .016 to .017:

> *.016 The statement of financial position should report the retirement benefit liability and the statement of operations should report the expenses for retirement benefits on the basis of the value of the benefits attributed to employee service to the financial statement date. [SEPT. 2001]*
>
> *.017 The components of the retirement benefit liability are:*
>
> > *(a) accrued benefit obligation including the effects of plan amendments, settlements and curtailments;*
> >
> > *(b) plan assets, if any; and*
> >
> > *(c) unamortized actuarial gains and losses.*

As OTPP is a funded plan there are plan assets that are recognized as part of the retirement benefit liability. When plan assets and the net impact of unamortized actuarial gains and losses exceed the accrued benefit obligation then there is an "Accrued benefit asset" (ABA). An ABA is defined in Section PS 3250 as follows:

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

Accordingly, the portion of the government's plan to be recognized includes their share of the accrued benefit obligation and also their share of the plan assets. In the case of the Province's portion of OTPP there is no uncertainty regarding the *existence* of an ABA for the government's portion of the plan; the

ABA is calculated by reference to accrued benefit obligation and plan assets, both determined based on the best estimate assumptions and the methodologies required by with Section PS 3250 for these items. As noted above an ABA is defined as the sum of the government's accumulated cash contributions less the sum of the current and prior years' benefit expenses (before any change in the valuation allowance). For a jointly sponsored plan, this is the government's accumulated cash contributions less the government's share of the current and prior years' benefit expenses that are attributable to the government under the JDBP. The Province's portion of OTPP resulted in an ABA of $10.1 billion as at March 31, 2016. There is no uncertainty regarding the occurrence of the cash contributions made (and the interest earned thereon) measured in accordance with Section PS 3250 and the existence of the government's obligation. As Section PS 3250 paragraph .080 *requires* a government to account for its portion of the plan in accordance with the standards for defined benefit plans, this would include the recognition of any asset that meets the definition of an ABA under the standard.

Further, Section PS 3250 paragraph .050 refers to the presentation of the ABA; this amount is presented in the financial statements, net of any valuation allowance. This indicates that an ABA should be recognized in the financial statements, but measured in reference to the limit on the carrying amount of the asset - essentially a measurement requirement rather than a recognition requirement, as the limit could result in an ABA being measured at anything from $nil to its full amount. Note that the *measurement* of any net asset is subject to guidance in Section PS 3250 paragraphs .050-.059 and is discussed later in this paper.

To recognize only their share of the liability and not their share of the plan assets, or to recognize only a net liability (when the accrued benefit obligation exceeds plan assets) but never a net asset (when plan assets exceeds the accrued benefit obligation, subject to the valuation allowance guidance discussed in the Measurement section below), would indicate that the Province does not share equitably in the risks and rewards of OTPP because they bear only the risk of increased liabilities without being able to bear any rewards of investment returns on the plan assets and under this interpretation the plan would not therefore be a JDBP.

6.2 Concept of Shared Control and Asset Recognition

Included in the definition of a JDBP is the concept of shared control. Points (b) and (d) of the definition of a JDBP require shared control of decisions relating to administration, levels of benefits and contributions between the sponsors; and the sharing of risks between the government and the plan members. The concept of shared control resulting in a recognition of an asset could on the surface appear to conflict with the definition of an asset under FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210, as part of the definition of an asset under Section PS 1000 would suggest that the government must control the economic resource and access to the future economic benefits. Since shared control does not equate to control, there is a need to consider whether the recognition of any asset under PS 3250 is appropriate where there is only shared control.

The Province's position is that PSAS does not preclude asset recognition for assets under shared control and specifically for plan assets of JDBPs for the following reasons:

- As discussed above GENERALLY ACCEPTED ACCOUNTING PRINCIPLES Section PS 1150 states that a reporting entity applies every primary source of GAAP that deals with the transactions and events encountered by that entity. Section PS 3250 is a primary source of GAAP for dealing specifically with JDBPs and, as noted above, requires the government to account for their portion of the plan – both the accrued benefit obligation and plan assets in accordance with Section PS 3250. As such, reference to Section PS 3250 is sufficient to indicate that the recognition criteria are met for JDBP assets, no further source of PSAS guidance need be considered.

- Similarly, if other primary sources of GAAP are considered then it is relevant to consider GOVERNMENT PARTNERSHIPS, Section PS 3060 which also includes the concept of shared control. Under Section PS 3060, shared control is sufficient for asset recognition.

- The concept of shared control is not addressed in the definition and guidance of an asset in FINANCIAL STATEMENT CONCEPTS, Section PS 1000 and ASSETS, Section PS 3210. Although shared control is not included in FINANCIAL STATEMENT CONCEPTS, Section PS 1000, it has been a concept in the PSA Handbook since the introduction of Sections PS 3060 and PS 3250. With the introduction into the PSA Handbook of Section PS 1000 or Section PS 3210, the concept of shared control was not removed from Sections PS 3060 and PS 3250. This indicates that the Public Sector Accounting Board (PSAB) did not consider Section PS 3250 (or Section PS 3060) to be inconsistent with the general concepts in Section PS 1000.

- The Province's reporting of a pension asset for the JDBP is therefore consistent with these primary sources of GAAP, subject to measurement guidance including impairment considerations.

The similarities between the definitions of a JDBP and a government partnership under PSAS are demonstrated in Appendix F to this paper, and further support Section PS 3060 as being a relevant primary source of GAAP dealing with similar circumstances, should it be considered necessary to go outside of the requirements of Section PS 3250 to look for further clarification and guidance on recognition.

Under Section PS 3060 a critical condition for a Government partnership is shared control. Section PS 3060 explicitly acknowledges that under shared control "none of the partners is in a position to exercise unilateral control over the government partnership" (Section PS 3060 paragraph .20), yet the accounting model required by Section PS 3060 for non- GBPs[9] is that of proportionate consolidation which is the recognition of a pro rata share of assets, liabilities, revenues and expenses of the partnership. JDBPs (or pension plans in general) are not specifically excluded from the scope of Section PS 3060 (Section PS

[9] Government business partnerships (GBPs) are accounted for under the modified equity method rather than proportionate consolidation.

3060 paragraph .05 lists a number of exclusions from its scope and pension plans are not noted), however some may interpret that they are excluded from the scope of Section PS 3060 on the basis that control is shared with employees rather than with a party outside of the reporting entity (Section PS 3060 paragraph .06 footnote 3). The Province of Ontario and OTF, which represents employees of the Province (Teachers), share control of OTPP. This interpretation indicates that such plans are excluded because of a closer relationship between the government and the other party than normally exists for government partnerships. Even when an independent third party shares control, Section PS 3060 still requires the recognition of a share in an asset subject to shared control, indicating that the PSAS framework does not require unilateral control in order to support asset recognition when there is shared control. It would not be appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3060 for proportionate consolidation, and similarly it is not appropriate to use Section PS 1000 to over-ride the requirement in Section PS 3250 to account for the government's portion of a JDBP. In other words, Section PS 3250 is a primary source of GAAP and provides sufficient and complete guidance on how to account for assets related to JDBPs.

6.3 Concept of Contingent Asset

CONTINGENT ASSETS, Section PS 3320, provides guidance on the disclosure of contingent assets in a government's financial statements. It characterizes a contingent asset as one where there is uncertainty as to the existence of an asset (Section PS 3320 paragraph .04). It is the Province's position that the existence of the pension asset is not uncertain – there is an accrued benefit asset calculated in accordance with Section PS 3250 as noted above that is based on past transactions, being the impact of cumulative contributions and benefit expense. The fact that shared control exists with regards to access to the assets of the plan does not create additional uncertainty that would impact asset recognition under PSAS. The Province anticipates that in a broad sense, any OTPP surplus would be shared in an "equitable manner" under the terms of the arrangement, and this is enabled through the ability to negotiate the utilization of the surplus including the ability to prevent the utilization of the surplus in a manner that does not benefit the Province. This expectation is further supported by past history of surplus utilization (see Appendix G). The method, extent and timing during which the Province will obtain the expected future benefits (contributions reductions vs increase in benefits) is not certain. However Section PS 3320 also states "The mere fact that an estimate of an amount is involved (measurement uncertainty) does not, in and of itself, constitute the type of uncertainty that characterizes a contingent asset. For example, even though there may be measurement uncertainty related to income tax receivable, there is nothing uncertain about the fact that this asset exists. Any uncertainty is related solely to the amount thereof" (Section PS 3320 paragraph .07). Based on past history of surplus utilization for OTPP and based on the constating documents, expected future benefits for the Government are present. The uncertainty as with many types of assets relates to measurement uncertainty which will be discussed below.

6.4 Conclusion on recognition

Therefore the Province has concluded that PSAS supports the recognition of a pension plan asset in respect of a joint defined benefit plan and does not require that all recognized assets must be subject to unilateral control. The Province's share of OTPP's pension surplus meets the definition of an Accrued Benefit Asset under Section PS 3250. The measurement of that accrued benefit asset is determined by reference to the guidance in Section PS 3250 regarding the Limit on the Carrying Amount of an Accrued Benefit Asset, discussed in Question 3 of this position paper.

7.0 Question 3 – Measurement of a pension asset

7.1 Standards in the PSA Handbook

Section PS 3250 addresses how to measure a pension asset. This is a two-step process for OTPP. Firstly the accrued plan obligation (a Credit) and the plan assets (a Debit) are measured in accordance with the standard, and adjusted for any unamortized actuarial gains or losses (a Debit for gains not yet realized, a Credit for losses not yet realized). This measurement results in a retirement benefit liability when it is a net liability (a Credit) amount or an accrued benefit asset when it is a net asset (a Debit) amount. When the resulting amount is an asset, the standard requires a second step to test that the asset is not impaired. It should be noted that impairment testing in some form is required for all assets recognized under PSAS standards except those carried at fair value, although the methodology of impairment tests will vary depending on the nature of the asset. The amount that is tested is the "adjusted benefit asset". When there are net unamortized gains the ABA is equal to the adjusted benefit asset. When there are net unamortized losses the ABA is reduced by those net unamortized losses to calculate the adjusted benefit asset. A graphical illustration of the calculation of the Accrued Benefit Asset (AcBA) and the Adjusted Benefit Asset (AdBA) are shown in appendix C. Section PS 3250 paragraphs .052 to .059 go on to explain what the standard means by expected future benefit and how a government may benefit from the ABA or adjusted benefit asset. Note that for OTPP the accrued benefit asset equals the adjusted benefit asset as there are net unamortized actuarial gains.

Section PS 3250 paragraphs .050-.059 are included here for completeness and ease of reference:

> ***Limit on the carrying amount of an accrued benefit asset (i.e. Asset Ceiling Test)***
>
> *.050 An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs. [SEPT. 2001]*

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

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

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

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

.055 The objective of the standard in Section PS 3250 paragraph .050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions.

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

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

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

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

calculate this present value is the expected rate of return on plan assets used to determine the benefit expense in the period.

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

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

Section 3250 paragraph .052 states that a government may benefit from an ABA by either i) withdrawing surplus assets from the plan or ii) by taking a contribution holiday or receiving a refund of contributions. This is an explanatory paragraph on how a government may benefit from an ABA and why a valuation allowance may be needed, rather than detailing the test to be applied. Part of this justification is to note that that an ABA may be impaired when "the government is not entitled to benefit from [the ABA] fully". Examples of when a government may not be entitled to benefit from the ABA fully are given, such as a regulatory moratorium on pension surplus withdrawals or uncertainties as to a government's legal right to use a plan's accounting surplus.

Section PS 3250 paragraph .059 gives additional guidance to apply when an entity contemplates realizing future benefits <u>through a surplus withdrawal</u>: "A key factor in determining a government's expected future benefit from a defined benefit plan with a plan surplus for accounting purposes is the ability of the government to withdraw assets from the plan. The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal". This introduces the concept of a legally enforceable right but only in the context of a government's withdrawal of surplus and <u>not in the context of contribution holidays</u>. If the standard setters had intended legal enforceability

to be the test throughout the standard, they would not have raised it only in the context of a withdrawal of surplus, but as a more fundamental notion in the guidance on expected future benefit. [10]

It is acknowledged that the Province does not have a unilateral legal right to reduce its contribution levels without agreement from the OTF because OTPP is by nature a JDBP subject to shared control, they are entitled to an equitable share of the risks and rewards of the JDBP, essential to the definition of a JDBP. Section 3250 paragraph .052 does not state that being "entitled to benefit" means having a legally enforceable right as at the reporting date to take contribution holidays. When considering the ability to realize expected future benefits under Section PS 3250 paragraph .052, the Province's legal rights to utilize a surplus to reduce future contributions must be analyzed. Our interpretation of this guidance is that it presents a lower threshold than legal enforceability which is not explicitly required by the standard to support recognition and measurement of JDBP pension assets. Specifically, the amount of pension asset that gets recorded needs to take into account considerations around any legal uncertainties. This consideration involves significant professional judgment. However, it is our view that uncertainty does not need to be reduced to zero in order to recognize a pension asset in the Public Accounts. Pension plans, by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". Expected does not equate to certainty or the absence of uncertainty (Section PS 3250 paragraph .056).

Under the Plan and Partners' Agreement, if funding surpluses occur the partners are required to negotiate the use of the funding surplus (at least once every three years) and the Province is entitled to negotiate a reduction in contributions in respect of its share of the surplus. Under the Partners' Agreement any funding surplus must be dealt with (which includes the option of parking the surplus in the contingency reserve) so that the funding valuation becomes actuarially balanced. *In other words when there is a funding surplus over a certain range the "status quo" cannot be maintained, the surplus must be reduced by a combination of reductions in contributions, increases in benefits or withdrawals of surplus*. This is confirmed by the Partners' Agreement Section 57 that requires an actuarially balanced valuation to be prepared at least once every three years, allowing for a contingency reserve, combined with the FMP which sets out the framework for determining when a surplus or deficit outside of agreed upon ranges are met and action must be taken. While the Province might choose to accept an increase in member benefits rather than to reduce funding, any such decision is at the Province's discretion since the OTF cannot force the Province to increase benefits instead of reducing contributions. In other words

[10] Per page 10 of the October 2, 2016 dated letter from Deloitte LLP addressed to Ms. Karen Hughes, Associate Deputy Minister, Treasury Board Secretariat

it is at the Province's discretion whether to address the actuarial balancing requirements by allowing its portion of the surplus to be utilized through increased benefits. The OTF equally has the right to not agree to reduced contributions from the Province, but they do not have the right to force an inequitable sharing of the surplus. Therefore, the Province is entitled to negotiate their share of the JDBP which may include taking contribution holidays in future negotiations and can effectively use their power in negotiations to benefit from the ABA. The joint partners do have the ability to renegotiate all aspects of the partners' agreement including the FMP. However all changes require the agreement of both parties and as such the Province can veto any changes to the agreement. Note that while the negotiations are based on funding surplus amounts rather than accounting surplus amounts, any differences would be captured in the mechanics of the calculation of the expected future benefit rather than precluding an ability to benefit from any of the accounting surplus.

Further, Section PS 3250 paragraph .055 indicates "The objective of the standard in Section PS 3250.050 is to limit a government's accrued benefit asset to the amount it can realize in the future. The expected future benefit is a calculated amount representing the benefit a government expects to realize from a plan surplus. An expected future benefit includes any withdrawable surplus or reduction in future contributions". Many generally accepted accounting frameworks use "expected" in a number of principles and it is typically used in the probabilistic sense – something is expected when it is probable at some level, it does not equate to certainty. The Province has an expectation that they will benefit fully from the ABA by exercising their current rights under the plan arrangements to negotiate the use of current and future surpluses in the form of contribution holidays. This position is supported by the review of the constating documents and past history of negotiations that indicate[11]:

1. The TPA prohibits the total amount of the contributions payable by the Province (and other participating employers) from exceeding the amount of contributions paid by or on behalf of active members in respect of credited service for the year[12] (subject to certain exceptions for payment of a solvency deficiency and where there are insufficient cash and liquid assets in the fund). 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.
2. 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 (refer to Appendix G for a history of surplus utilization for OTPP). 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.

[11] Per pages 3 to 6 of the September 20, 2016 dated letter from Osler, Hoskin & Harcourt LLP addressed to Len Hatzis and Paul Kaufman, Treasury Board Secretariat Legal Services
[12] TPA, subsection 5(1.1)

3. The inability for either party to unilaterally require surplus to be utilized in a particular manner (subject to the OTF Call Right[13])[14], and the requirement to negotiate and agree (or in the absence of agreement, mediate and/or arbitrate) presents the Sponsors with an equal opportunity to benefit from surplus utilization.
4. One could argue that the obligation to bargain in "good faith" found in the Partners' Agreement (section 74) 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. Under the plan, contributions are generally borne equally by the Province and the employees. Employees benefit economically from both an increase in benefits and from a reduction of contributions. The Province benefits economically directly from a reduction in contributions. This makes it reasonable that at least some contribution reductions would be agreed to by the joint sponsors as a highly unequal weighting towards increases in benefits would not balance the interests of taxpayers and teachers therefore may be unlikely to be a reasonable outcome of “good faith” negotiations between the Province and the OTF.

   This is further supported by the historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses, and therefore, which should also be considered. In respect of conditional indexing, reduced indexation for current retirees was matched by an increase in payments by the Province for the first 50% of the indexation reduction. As the sponsors agreed to utilize the funding surplus to partially restore indexation, this restoration of indexation resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change,$1.98B for the 2015 change, and $1.68B for the 2014 change). This demonstrates that historically and over the long term an equitable sharing of the deficits and surpluses has resulted in changes in the Province’s contributions, even when there are decreases or increases to benefits for employees.

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, a mediator may be chosen by agreement of the sponsors (section 77 of the Partners’ Agreement). If the sponsors do not accept the report of the mediator, an arbitration board will be appointed (section 84 of the Partners’ Agreement). The arbitration board would consist 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

[13] The OTF Call Right is a one-time arrangement intended to compensate Plan members for absorbing 100% (rather than 50%) of funding shortfalls arising the government initiated Freeze period. Part of a previously agreed upon arrangement to ensure equitable sharing of the risks and rewards over the long term of the plan, it is not a general unilateral right to utilize future surpluses beyond the recovery of the specific funding shortfalls.
[14] FMP, section 6.03

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).

Based on the above analysis, the Province believes that the uncertainties around how and when to utilize a surplus in the OTPP do not result in an inability or lack of entitlement to utilize the surplus in accordance with Section PS 3250 paragraph .052.

7.2 Calculating the limit on the carrying amount of an accrued benefit asset

Section PS 3250 paragraphs .053 to .058 lay out a mathematical calculation that determines the value of the adjusted benefit asset and the expected future benefit, and tests whether a government can expect to recover its accrued benefit asset through a withdrawal of surplus or through the reduction of future contributions. The stated objective of this exercise, as set out in Section PS3250 paragraph .055, is to limit the amount of the government's accrued benefit asset to the amount "it can realize in the future." The expected future benefit is further described as "a calculated amount representing the benefit a government expects to realize from a plan surplus", where actual realization of the benefit would be reflected in a reduction in future contributions. A valuation allowance is recorded against the pension asset to limit the asset value, if necessary, based on this analysis. This is a prescriptive test under Section PS 3250, specifically that the amount of an asset is limited to the "expected future benefit" as defined in Section 3250 paragraph .56.

Therefore in accordance with Section PS 3250 paragraph .56 the Province calculated the expected future benefit as the sum of:

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

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

Each of these is discussed separately.

7.3 Considerations re: withdrawal of the surplus (Section PS 3250 paragraph .056 (b))

In relation to the ability of a government to benefit from a surplus through the withdrawal of the surplus, Section 3250 paragraph .059 indicates “The expected future benefit includes amounts to which a government has a legally enforceable right of withdrawal.”

The TPA for OTPP does not specify a method for a potential withdrawal of surplus funds. Section 10(1), item 3 states:

> 10(1) The Minister of Education and the executive of The Ontario Teachers' Federation may enter into an agreement that provides for the following matters:
>
> 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.

Therefore, the conditions under which a surplus may be withdrawn from the fund is outlined outside of the text of the TPA itself, as OTF and the Province must reach mutual agreement on these terms in the form of the OTPP Funding Management Policy, as envisioned in Section 10(1).3 above.

Section 4.06 of the OTPP Funding Management Policy states:

> 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.

4.04(d) and 4.04(e) refer to actions that may be taken in the event that"...assets exceed current liabilities" (Section 4.04), meaning a surplus.

As Section 4.06 stipulates, a written agreement must be established between the sponsors (the Province and the OTF) to provide a surplus distribution. The Province does not have a legally enforceable right to withdraw assets from OTPP until such an agreement is reached.

The consent of the OTF would need to be obtained to be able to access surplus assets in OTPP through a withdrawal. As the Province does not have consent of OTF to withdrawal the plan surplus (for example at the end of fiscal year 2015-16), no expected future benefit should be recognized by the government based on its ability to withdrawal surplus from the plan.

The Province's position is that there is no amount of expected future benefit included in respect of withdrawable plan surplus.

7.4 Considerations re: reduced future contributions (Section PS 3250 paragraph .056 (a))

Section PS 3250 paragraph .056(a) sets out that the government's calculation of expected future benefit would be the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and minimum contributions the government is required to make regardless of any surplus. Note that in the case at hand, the calculations are done on a 50% basis since the starting point, per Section PS 3250 paragraph.081 and as set out in the fact summary above, is that the government accounts for its portion of the Plan. For this same reason, employee contributions are also excluded in this case since they would represent the teachers' portion of the Plan.

Section PS 3250 paragraph .055 indicates that the expected future benefit is a calculation that represents the benefit a government expects to realize from a plan surplus. The expected future benefit would operate as a ceiling on the pension asset value to be recorded in the accounts. For example, if the pension asset were $150, but the expected future benefit calculated as described above were $100, a valuation allowance of $50 would be recorded against the pension asset and the asset recorded in the government's financial statements would be reduced to $100.

There are two parts to the calculation of expected future benefit. The first part of the calculation is the sum of the present value of the expected future accruals for service for the current number of active employees. This amount is required to be calculated using consistent assumptions as those used for the calculation of the accrued benefit obligation itself. It is therefore relatively straightforward and is typically calculated based on the Province's share of the current service cost reported in the actuarial valuation taken into perpetuity unless there is evidence to indicate the workforce will significant diminish over time (for example a closed plan).

The second part of the calculation is the present value of required employee contributions and minimum required contributions by the government itself, regardless of any surplus. The main area for

judgment in the above calculation is in this second part of the calculation. Note that consistent with the calculation of the expected future accruals for service, no amounts are considered for employee contributions as these relate to the OTF's portion of the plan. The number of years that contributions are assumed in determining the asset ceiling are those minimum contributions that are required to be made "regardless of any surplus" (Section PS 3250 paragraph .056(a)). There is no further guidance in Section PS 3250 as to how the calculation of minimum required contributions should be performed and what restrictions or parameters should be factored into this calculation. Typically for defined benefit plans minimum contributions include those that are required by the pension regulator to be made for funding. However, minimum contributions regardless of any surplus, may be required by plan text, legislation or other agreements with employees. For OTPP a key element of judgment is determining what contributions are required by the current plan arrangements "regardless of any surplus". The constating agreements for OTPP require that the parties negotiate every 3 years as a minimum, and when there is a funding surplus.

Determining the number of years of contributions to include should involve an assessment of the facts and circumstances of the plan and should consider uncertainty. With respect to this uncertainty, there are a number of considerations that may be relevant. Uncertainties should be evaluated taking into consideration the contractual agreements between the sponsors that provide for the sharing of risks and benefits and specifically in respect of assessing the minimum contributions required by the plan agreements (there is no minimum contributions stipulated in the Plan text, legislation or Partners' Agreement) including the following:

- One view of minimum contributions might be that the agreed upon level of contributions are the minimum contributions until they are altered in the plan text. As this can only happen with agreement from OTF it cannot be assumed that changes will be made and therefore that the contribution formula as stated in the current agreements will continue in perpetuity. This view provides the most conservative view of minimum payments. However as the current contribution amounts are greater than the government's share of the annual current service cost for the existing workforce this indicates that continued contributions at this rate will result in ever increasing surpluses. Extrapolating the surpluses, at a certain point other requirements that are currently incorporated into the plan text, such as provisions in the Income Tax Act that limit the accumulation of surplus in a plan will apply to reduce the contributions. The effect of these caps on contributions would have to be estimated but cannot be ignored as they form part of the current contribution arrangements. Modelling could be performed to develop expectations as to when these CRA limits could be expected to be reached assuming no changes in the contribution levels. As is the most conservative view (highest minimum contributions) the impact of this has been considered, as discussed below.
- An alternative view of the minimum contributions required by the plan is that there is a contractual obligation under the Partners' Agreement that the Province and OTF negotiate and set both the benefits and the contributions every three years. A failure to agree might lead to mediation or arbitration, but not an assumption of the 'status quo'. On this basis it could be

argued that any agreed upon contribution levels are mandatory for only a three year period, after which the contributions must be renegotiated to stay the same, increase or decrease, such that the stated contribution level in the plan text constitute minimum payments for only three years. It should be noted that the plan text requires an actuarially balanced funding valuation, so to the extent that a funding deficit currently existed a contribution holiday (contributions lower than the annual cost of the plan) could not be negotiated. However because the funding situation at the time of future negotiations is not known it could be argued that no amount is a fixed "minimum contribution" in this context, because all of the contribution amount is subject to future changes in funding and negotiation by the joint sponsors.

- Other views of what the minimum contributions are would fall between these two views, such as that the current funding level is set to ensure that there is no funding deficit over a 11 year period and after that changes in contributions would be negotiated. This view has been used in calculating the actuarial calculation of the asset ceiling as noted in the table below.
- Another consideration might be the specific framework within the Funding Management Plan for OTPP which contemplates specified funding zones and expectations regarding possible contribution reductions by the sponsors. Informed stochastic modelling would be necessary to estimate when the different funding zones will be reached and probability of contribution reductions may be increased.
- The historical actions of the parties, which reflect a history of working together to resolve both funding deficits and use of funding surpluses should also be considered. As previously discussed, most recently in 2014, 2015 and 2016 with respect to OTPP, the sponsors agreed to use some of the funding surplus to restore indexation, which resulted in a decrease in the amount of future contributions that the Province would have otherwise had to pay to the plan in the amount of $7.8 billion ($4.3B for the 2016 change, $1.98B for the 2015 change, and $1.68B for the 2014 change).

In determining the range of possible outcomes, it is noted that measurement uncertainty may exist (Section PS 2130 paragraph .03). This paragraph also notes that many items are measured using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. As noted in Section PS 2130 paragraph .13, "As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements."

As part of the 2015/16 Public Accounts audit, the Office of the Provincial Controller engaged external consultants to conduct asset ceiling tests to assess the requirement for a valuation allowance against the $10.1 billion of net pension assets reported by the Province for OTPP . The results of those reports are summarized in Table 1 below.

Table 1: Summary of Asset Ceiling Models performed for OTPP

Model Assumptions	Expected Future Benefit or Asset Ceiling ($ Billions)	Results
1. There is no minimum employer contribution under the plan/legislation that is required if a surplus is present.	$44.6	There is no reduction in the expected future benefit (EFB) as at March 31, 2016.
2. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of the current funding report. Contribution requirements are $1.7B per year for 2015, 2016 and 2017.	$41.2	The minimum contribution requirement applies to the current period of the funding report and until a new report is completed. EFB is reduced for 2 years by $1.7B at March 31, 2016.
3. The employer minimum contribution considers the most recent funding valuation dated January 1, 2015 for the period of contribution requirement (i.e. 11 years through 2026) not just for the period of the current funding report.	$29.3	Uses a period to 2026 (11 year period) based on the funding report special contribution requirement. The EFB at March 31, 2016 is reduced by $15.3B.
4. The surplus is never used until the time it reaches the Income Tax Act (ITA) threshold. Once attained, the excess surplus is used at 50% for employees and 50% for the Province to reduce contributions in the following years.	$23.2	The ITA surplus limit is reached at the end of 2025, leading to forced contribution reductions from 2026. EFB is reduced by $21.4B at March 31, 2016
5. Every year, 50% of current	$12.9	The ITA surplus limit is reached at

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year surplus is applied to improve member benefits and the remaining 50% of the current year surplus is retained and continues to accrue. Once the ITA threshold is attained, the excess surplus is used 50%-50% to reduce contributions by employees and the Province.		the end of 2041 leading to forced contribution reductions from 2042. EFB is reduced by minimum $31.7B at March 31, 2016.

Note: Models above made no assumption on any value of the surplus withdrawal.

In all 5 models above, the expected future benefit (EFB) for OTPP is greater than the accrued pension asset of OTPP of $10.1 billion, at March 31, 2016. Even under the most conservative model (number 5 above) under which 50% of the current year surplus is applied to improve member benefits while the remaining 50% is retained and continues to accrue a return on assets until the Income Tax Act (IITA) surplus threshold is reached, the EFB of $12.9 billion is greater than the accrued pension asset of $10.1 billion. As such no valuation allowance was required and reported for OTPP as of March 31, 2016.

For purposes of OTPP, 11 years has been used. However, it is worth noting that up to 33 years of contributions could be factored into this calculation before the calculation would result in a conclusion that the OTPP asset is impaired.

In addition to the above calculations, the impact of the provision in the Income Tax Act that limits the amount of surplus that can be held in a plan should also be considered. Based on preliminary analysis assuming no changes to management's assumptions, contribution levels and benefits provided to employees, we believe that the OTPP will be required to begin using its surplus through a reduction in contributions in between 10 and 15 years into the future. Taking this timing into account, the pension asset ceiling is in excess of the pension asset recognized (pension asset ceiling of between $19.9 Billion and $22.3 Billion); therefore indicating that no valuation allowance is required.

The determination of the minimum contribution levels required as input to the calculation of the expected future benefit involves significant judgements, estimation and assumptions about future funding surplus levels. These judgements, estimates and assumptions should be made on a consistent basis with best estimates used in developing the accrued benefit obligations and plan asset amounts. Regardless of the need to apply judgements, estimates and assumptions for the calculation, this does not imply that no asset can be recognized or that it cannot be reliably measured. In fact, pension plans,

by their nature, include significant estimates - whether they be related to the value of assets held by the plan that are not publicly traded (e.g. investments in private companies and real assets) or in the present value of the projected benefit obligation that is based on a series of economic assumptions related to inflation, salary escalation, mortality and the rate of return that the assets in the plan will earn over the period that benefit payments are paid to pensioners. Any change in these assumptions will have an impact on the accounting surplus, so to apply a test requiring no uncertainty to the recognition of an asset is inconsistent with the accounting for pension plans as a whole. Further, the term used to describe the cap in the asset ceiling test is "expected future benefit". From the Province's perspective, 'expected' does not equate to 'certainty' or the absence of uncertainty.

The assumptions used in the calculation of the accrued benefit obligation are required to be the "government's best estimate of expected long-term experience and short-term forecasts" (Section PS 3250 paragraph .042) and each key assumption must be based on the government's best estimate of those future events that have an effect on the accrued benefit obligation (Section PS 3250 paragraph .041). This approach is designed to recognize the long-term nature of the retirement promises with appropriate consideration of, but not undue influence of, experience expected in the short-term. Section PS 3250 paragraph .057 requires that the future service cost calculation included in the calculation of the valuation allowance be determined on a consistent basis with that used to determine the accrued benefit obligation itself. The Province has determined the discount rate to be used in valuing the pension obligation related to OTPP by referencing the expected rate of return on plan assets, which is one of the acceptable references suggested on Section PS 3250 paragraph .044.

The OAG and the Province differ in their interpretation regarding whether it needs to be "expected" that the Province will benefit from the surplus in OTPP through future contribution reductions or whether it needs to be "legally enforceable". The OAG considers there needs to be the same level of assurance the government will benefit from the surplus through reduced contributions (legal enforceable) as is required in Section PS3250 paragraph .059. The Province considers that it needs to be expected that future economic benefits are to be obtained reflected in the definition of "expected future benefit" defined in the glossary to Section PS 3250 with consideration as to uncertainties as to the right to benefit from a plan surplus.

7.5 Other guidance in the PSA Handbook on measurement

MEASUREMENT UNCERTAINTY, Section PS 2130 provides guidance on dealing with measurement uncertainty through additional disclosure in the financial statements, which we believe would be a useful addition to the financial statements. Section PS 2130 also provides guidance on how to deal with measurement uncertainty and includes the following guidance:

> *.12 The estimation of the amount of an item to be accrued or disclosed in financial statements may be based on information that provides a range of amounts. When a particular amount within such a range appears to be a better estimate than any other, that amount would*

be used. When uncertainty exists, estimates used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated. Estimates of the financial effect are determined using professional judgment, supplemented by experience of similar transactions and, in some cases, reports from independent experts. Estimates include any additional evidence provided by subsequent events occurring after the financial statement date.

.13 As a result of the estimation process, a government would be able to determine a range of reasonably possible amounts in accordance with assumptions that are realistic, supportable, internally consistent, and consistent with planned courses of action. The range of reasonably possible amounts would exclude amounts at the outer edges of possibility since such amounts, while possible, are considered to be outside the best estimate range. Relevant information available to the government to develop a reasonable range includes past experience, precedents, and opportunities to reach alternative arrangements.

The estimate of the valuation allowance, and in fact pension plan accounting as a whole, is subject to measurement uncertainty. As previously noted, accounting for pension plans involves significant estimates in all aspects of the accounting whether that be in valuation of non-traded assets, estimation of the economic assumptions used to value current service cost and the projected benefit obligation or the valuation allowance. One of the key assumptions impacting the measurement of the net pension asset is the discount rate which reflects management's best estimate of rate of return. The rate used by the government is an acceptable alternative under PSAB and consistent with rates followed by other senior Canadian governments. Actual historical results since the inception of the plans corroborate the reasonableness of the rates used by management and the continued appropriateness for purposes of determining pension expense and pension assets reported in the Public Accounts. Appendix J includes a comparison of the OTPP funding rate assumptions, the Provincial discount rate for OTPP and the actual performance of OTPP from 2005 to 2016. Historical rates of return on plan assets have supported the past discount rates used by the Province in relation to OTPP.

7.6 Impact of valuation allowance

The current Auditor General's view challenges previous interpretations of the Provincial Controller and former Auditor Generals regarding the interpretation and application of Section PS 3250 to those JDBPs where the government is a joint sponsor. The impact of the OAG's view is that no net pension asset should be recognized in the Province's Public Accounts for JDBPs until the joint sponsors agree to a change in the plan text to provide for unilateral authority to the Province to access surplus or reduce future contributions or the sponsors enter into an agreement by year-end enabling the government to take a contribution holiday. In the absence of meeting either the criteria set out by the Auditor General, any ABA would therefore be fully provided for through a valuation allowance, impacting each year's

statement of operations by the amount by which the asset would otherwise increase in value. These results are counterintuitive with pension expense being higher in years in which increased funding is made and also higher when poor investment returns create actuarial losses that have not yet been amortized into the statement of operations. These examples are illustrated in Appendix C.

For information purposes, refer to Appendix H for a comparison of the pension expense, surplus (deficit), net debt and net debt-to-GDP of the Province over the prior 10 years following the Auditor General's approach to pension accounting for OTPP compared with following the Province's interpretation of the PSAS. Of particular note is the impact in 2008 when the deficit would have been lower by $3 billion in a year when pension asset values fell significantly because of the financial crisis.

7.7 Comparability of Ontario's accounting to other Provinces defined benefit plans

Not all of the jurisdictions noted in this comparative overview have joint defined benefit plans. Furthermore, the specific terms and conditions of any jurisdiction's plans will determine the appropriate accounting under PSAS. This information is provided for reference purposes only and has no direct impact on the Province's accounting treatment for OTPP or other defined benefit plans on the Province's financial reports.

The Province of British Columbia does have a jointly sponsored pension plan. Appendix I provides details from a legal opinion prepared by lawyers, Koskie Minsky which compared access to the pension surplus of OTPP relative to JDBPs in British Columbia. The Province of British Columbia does not report a pension asset in their financial statements as the Province has given up any rights to the surplus in the Joint Trust Agreements. The provision was established to support the independence of the four pension plan Boards. As a result the accounting by British Columbia is appropriately different than the accounting by Ontario for OTPP.

The Province of Manitoba has a multi-employer defined benefit plan for their healthcare employees. The Province neither records the net pension liability or the net pension asset on their financial statements as the Province is not a direct sponsor of the plan. The Province of Manitoba appropriately reduces the accrued benefit asset to nil in accordance with Section PS 3250 paragraph .050 as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

The Province of Nova Scotia's Public Service Superannuation Plan transitioned to a joint governance structure in April 1, 2013. Due to the wording of the legislation, the Province has determined it no longer has any residual liability for the plan, and therefore has no entitlements to its assets. The legislation and funding policy alleviated the Province from any responsibility to fund shortfalls or to benefit from fund surpluses. As a result, the Province no longer records a net pension asset or liability in their financial statements. The Province of Nova Scotia therefore appropriately reduces the accrued

benefit asset to nil in accordance with Section PS 3250 paragraph .050 as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

Quebec has two joint sponsored plans: Government and Public Employees Retirement Plan, and Pension Plan Management Plan. These plans are structured such that employee and employer contributions are in separate funds. Currently both of these plans are in net pension liability positions.

In New Brunswick, the target benefit pension plans are governed by an Agreement and Declaration of Trust which restricts the Province's access to the plan assets. On this basis, the Province records the value of the plan net assets as nil when these plans are in a net asset position. These plans are shared risk plans that are governed by a Board of Trustees to which the Province has appointed one-half of the members. The Plans are jointly funded by employees and the Province. These target benefit plans target retirement benefits as opposed to guaranteeing them. Two of the four target benefit plans are in a net asset position, where a full allowance is taken by the Province against the net pension asset. The Province of New Brunswick appropriately reduces the accrued benefit asset to nil in accordance with Section PS 3250 paragraph .050 (there is no specific guidance on target benefit plans in PSAS) as the Province does not expect future benefits from any plan surplus in contrast to OTPP and the Province of Ontario.

As noted above, the constating documents for pension plans in other provinces are different than those of OTPP, therefore caution should be exercised when trying to compare accounting among the jurisdictions, or others.

7.8 Conclusion on measurement

As discussed, there is significant professional judgement and estimation in determining how to measure the valuation allowance under Section PS 3250, including the determination of the minimum contributions required by the current plan arrangements. It is the Province's position that the attributes of the JDBP arrangements for the OTPP entitle the Province to access its portion of any plan surplus through the right to negotiate its use to the Province's benefit and that this results in an expected future benefit through the use of any plan surplus through reduced contributions.

The Province has applied reasonable estimates of the plan's funding status necessary to determine what minimum contributions are required under the current plan contribution arrangements. Based on the results of various actuarial assessments for the asset ceiling test date, no valuation allowance appears to be required and the OTPP pension assets should continue to be recorded on the books of the Province.

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Appendix A – Pension liability (asset) and expense reported by the Province of Ontario for OTPP over the prior 14 years

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)						
$ Millions						
Fiscal Year	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans						
Accrued benefit obligation, closing balance	27,544	32,185	33,660	35,505	37,045	40,186
Less: pension fund assets (market related values), closing balance	(34,390)	(36,215)	(37,929)	(39,579)	(41,396)	(44,347)
Unamortized experience gains (losses)	6,066	2,750	2,646	2,112	2,028	1,493
Adjustment for different year ends	421	436	449	472	497	523
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	642	507	383	256	135	20
Pension liability (Asset) at March 31 Reported before any valuation	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**282**	**(336)**	**(791)**	**(1,233)**	**(1,691)**	**(2,126)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans						
Current period benefit cost	650	770	848	868	878	955
Amortization of experience gains	(568)	(235)	(247)	(222)	(233)	(234)
Pension interest expenditure	(353)	(374)	(250)	(272)	(261)	(281)
Cost of plan amendment	-	2,260	-	-	-	-
Less: recognition of unamortized experience gains	-	(2,260)	-	-	-	-
Amortization of Other amounts	(134)	(131)	(130)	(132)	(134)	(135)
Pension expense before valuation	**(405)**	**29**	**221**	**241**	**250**	**305**
Expense increase (reduction) in valuation Allowance						
Pension Expense after valuation Allowance	**(405)**	**29**	**221**	**241**	**250**	**305**

Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	2006-07	2007-08	2008-09	2009-10	2010-11
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	41,560	44,178	46,011	48,304	49,559
Less: pension fund assets (market related values), closing balance	(47,425)	(52,459)	(53,479)	(54,556)	(57,123)
Unamortized experience gains (losses)	2,888	4,560	2,617	277	772
Adjustment for different year ends	529	650	687	764	774
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	(114)	54	136	206	220
Pension liability (Asset) at March 31 Reported before any valuation	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
Valuation Allowance	**-**	**-**	**-**	**-**	**-**
Pension Liability (Asset) after valuation Allowance	**(2,562)**	**(3,016)**	**(4,027)**	**(5,005)**	**(5,799)**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	998	1,051	1,118	1,175	1,217
Amortization of experience gains	(235)	(355)	(557)	(458)	(294)
Pension interest expenditure	(258)	(381)	(536)	(481)	(397)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(146)	38	34	30	(4)
Pension expense before valuation	**359**	**354**	**60**	**266**	**523**
Expense increase (reduction) in valuation Allowance					
Pension Expense after valuation Allowance	**359**	**354**	**60**	**266**	**523**

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Ontario Teachers' Pension Plan (excluding Retirement Compensation Plan)					
$ Millions					
Fiscal Year	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**
50% Pension Liability (Asset) Reflecing Accounting Policy for Joint Plans					
Accrued benefit obligation, closing balance	51,847	52,977	54,762	56,901	58,184
Less: pension fund assets (market related values), closing balance	(57,843)	(59,932)	(65,434)	(71,538)	(78,499)
Unamortized experience gains (losses)	(1,648)	(1,237)	1,851	4,816	9,001
Adjustment for different year ends	799	826	853	882	895
Other Unamortized Amounts (initial unfunded liability, difference in contributions, etc.)	222	242	257	273	272
Pension liability (Asset) at March 31 Reported before any valuation	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**(10,147)**
Valuation Allowance	**-**	**-**	**-**	**-**	**10,147**
Pension Liability (Asset) after valuation Allowance	**(6,623)**	**(7,124)**	**(7,711)**	**(8,667)**	**-**
50% Pension Expenditure Reflecing Accounting Policy for Joint Plans					
Current period benefit cost	1,283	1,396	1,327	1,462	1,451
Amortization of experience gains	(245)	(91)	35	(156)	(362)
Pension interest expenditure	(495)	(387)	(457)	(707)	(939)
Cost of plan amendment	-	-	-	-	-
Less: recognition of unamortized experience gains	-	-	-	-	-
Amortization of Other amounts	(24)	(26)	(30)	(31)	(33)
Pension expense before valuation	**519**	**892**	**875**	**569**	**118**
Expense increase (reduction) in valuation Allowance					**1,480**
Pension Expense after valuation Allowance	**519**	**892**	**875**	**569**	**1,598**

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Appendix B – Guidance in the various constating documents for OTPP relating to use of the surplus and the sharing of responsibilities

Pension Benefits Act (PBA) and the regulations (PBR)
While they do address surplus withdrawals, 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' Pension Act and to the Partners' Agreement and Funding Management Policy in order to determine how ongoing surplus is dealt with under the OTPP.
Teachers' Pension Act (TPA)
Paragraph 10(1)3 of the TPA 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. Pursuant to Section 10 of the TPA, the Minister of Education and the OTF (collectively the sponsors) have entered into an agreement for the management of the Plan (Partners' Agreement), to which is appended a Funding Management Policy (FMP) that is deemed to form part of the Partners' Agreement. The FMP provides a framework for the funding of the Plan and how deficits and surpluses will be addressed. The Partners (sponsors) can deviate from the FMP by agreement.
Partners' Agreement
The Partners' Agreement is between the Province of Ontario and the OTF and sets out the formal relationship between the partners (sponsors) in sponsoring the OTPP. Paragraph 8 of the Partnership Agreement states that the partners will be responsible for designing the Plan structure, setting the benefits of the Plan, developing new policy, deciding what the contribution rate will be, what the funding levels, margins and contingency reserves will be, how to make changes to the Plan and other Plan documents, deciding whether or not to file a valuation more frequently than required by the PBA, appointing the OTTP Board, and defining the role of the Board. Section 10 requires that the partners meet and negotiate changes to the plan every three years. Section 19 of the Partners Agreement sets out the responsibilities of the OTPP Board, and does not confer any authority on the OTPP Board to change benefits or contribution rates that are provided under the OTPP. This means that the OTPP Board has no authority to use ongoing surpluses either to improve benefits or reduce contributions. Only the sponsors to the OTPP have the authority to utilize ongoing surpluses. Section 19 also requires the Board to prepare a valuation at least every three years to comply with the PBA.

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Paragraph 57 requires a valuation prepared for filing with the Superintendent of Financial Services to be actuarially balanced so that the present value of benefits and costs to be paid out of the fund (plus any contingency reserve) be equal to the present value of sponsor contributions. An actuarial valuation for funding purposes of the pension fund shall be prepared by the Board's actuary as at the 1st day of January and filed annually with the Superintendent of Financial Services, unless the partners jointly agree to instruct the Board not to file the valuation. The partners shall establish a committee to deal with accounting matters relating to joint pension plan sponsorship and agree to contact the Public Sector Accounting Board to raise issues of concern to the partners.

Paragraphs 58 to 60 indicate the actions to be taken based on the preliminary results of a valuation prepared for filing with the Financial Services Commission of Ontario. If the valuation indicates a need to increase the contribution rate, the partners need to meet as soon as possible to discuss how to adjust for that need on an equally shared basis. If the valuation indicates the contribution rate can be decreased, the actuarial gain can be applied to reduce the payments required to liquidate any unamortized balance of a solvency deficiency.

The process governing the use of ongoing surpluses by the sponsors is set out in the Partners' Agreement. It anticipates that the OTPP Board will prepare an actuarial valuation of the OTPP every three years (section 73).

Paragraph 74 requires negotiation in good faith regarding changes to the Plan that flow from a valuation that is be filed with the regulators.

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

Section 77 of the Partners' Agreement anticipates that the sponsors may appoint a mediator to assist them and sections 84 and 86 of the Partners' Agreement provide for the appointment of a Board of Arbitration to make a final and binding order with respect to the utilization of an ongoing surplus disclosed by the actuarial valuation. A Board of Arbitration is empowered to change contribution rates and/or benefits under the Plan, or to keep an amount of surplus in reserve, but is subject to certain limits that are set out in section 92.

If the sponsors cannot agree on the changes required to the Plan, a mediator is appointed to assist the sponsors in coming up with an agreement. The mediator is responsible for submitting a report to the sponsors on his or her views on the positions of the partners and provide a recommendation to the sponsors. If the sponsors do not accept the mediator's report, the arbitration process will begin and an arbitration board will be appointed. The board will consist of 3 people, with each partner selecting one

representative and two appointees will select the final member who is an umpire. Paragraph 94 of the Partners' Agreement indicates that the report created by the arbitration board will be implemented.

Paragraph 92 sets some parameters for the arbitration, including part (c), which sets out that the parameters that the award of the arbitration will provide that the contributions from the Minister and employers be equal to those of the members.

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.

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

Funding Management Policy (FMP)

The FMP is an appendix to the Partners' Agreement that speaks to how the Plan should be funded and how surpluses should be utilized by both parties. The protocol for the use of a surplus under the OTPP is detailed in the FMP adopted by the Ontario Government and OTF as sponsors of the OTPP. The FMP sets out a complex series of considerations surrounding funding management and the use of any excess of assets over liabilities. The FMP sets out a number of "funding zones", depending on the level of funding in the Plan. The following three are most relevant to addressing surpluses:

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

ii) Temporary improvement zone (Article 4 of the FMP) is the zone where contributions can be temporarily reduced, a surplus distribution can be made on a temporary basis and/or benefits can be temporarily improved (as long as it does not create a long term cost) (Section 4.05).

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

The ability to reduce contributions or increase benefits through the temporary or permanent improvement zone are subject to ensuring that the requirements of 3.06 in the restoration zone are met. Article VIII of the FMP sets out that the parties must agree to any changes arising out of FMP decisions. For filing valuations, if the sponsors are unable to agree the mediation process set out in the

Partners' Agreement, the arbitration process outlined in the Partners' Agreement will be followed. For valuations that are not filed, either party can decide not to negotiate.

The Plan is currently in the Restoration Zone. Contributions to the OTPP currently include a 1.1% special contribution on all earnings and that the Restoration Contribution Reduction under Section 3.06(e) would if agreed to by both sponsors, permit this special contribution to be eliminated. This special contribution is scheduled to end in 2026.

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

Section 8.01 of the FMP provides the following:

Section 8.01 Unless the sponsors 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.

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. There has been no instance where the arbitration provisions have been invoked by the parties since the FMP was established. OTPP's internal legal counsel, has indicated 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. 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' 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).

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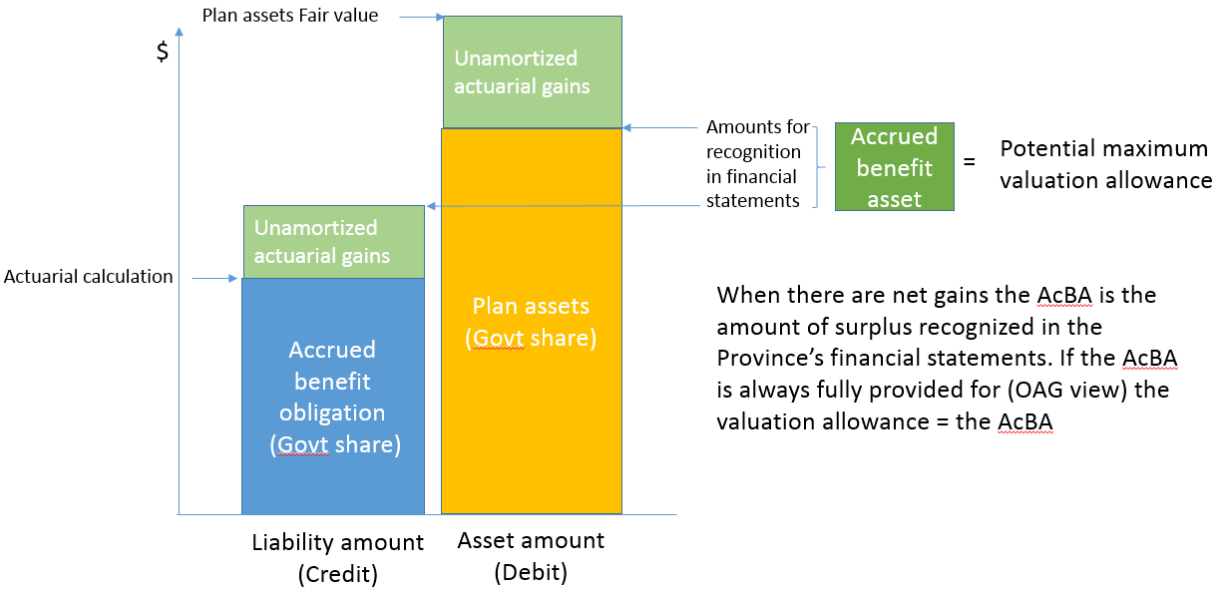
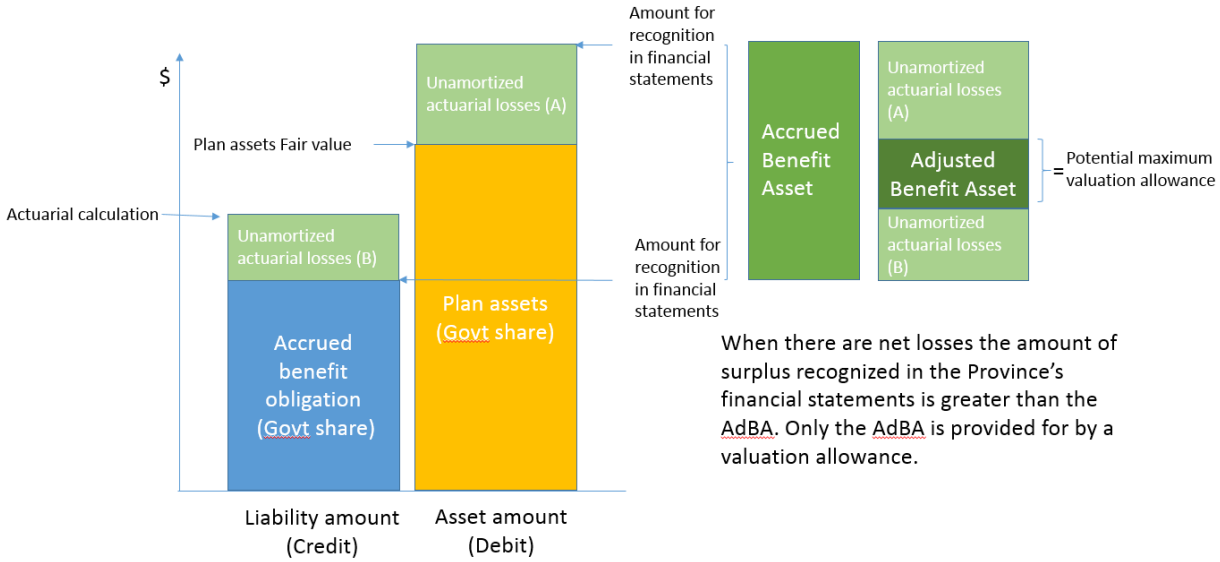
Appendix C – Overview of a Valuation Allowance on Pension Assets

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



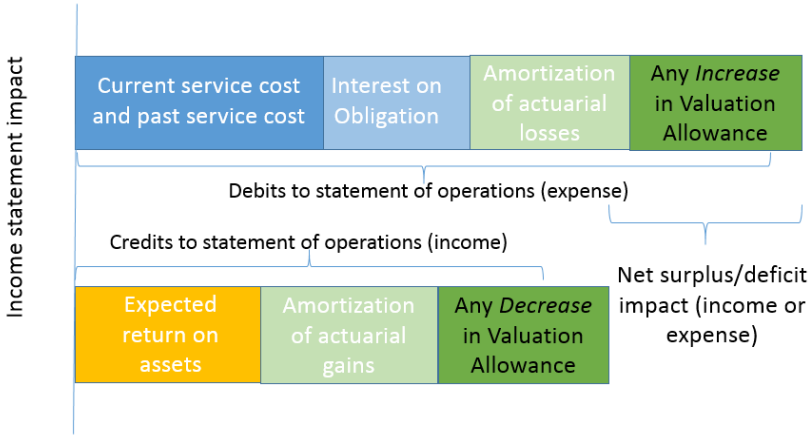
An Adjusted Benefit Asset (AdBA) is required when there are unamortized losses



Components of Expense

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

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



Changes in the Accrued Benefit Asset

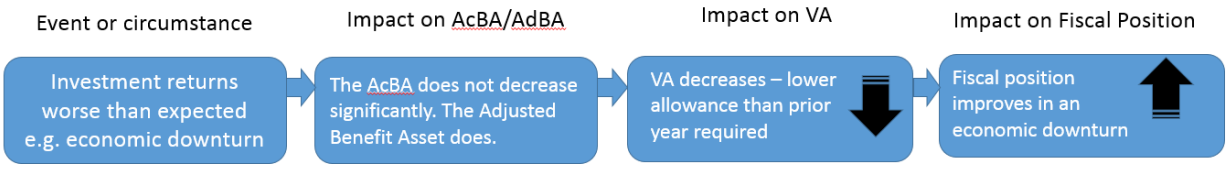
Changes in the AcBA may occur for a number of reasons. Where changes result in an increase in the AcBA without expectation of future benefit, such changes would result in a change in the valuation allowance (VA) to effectively reduce the AcBA to zero. In this situation, the following impacts on the statement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

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

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

Changes in the Accrued Benefit Asset

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



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

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

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

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

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

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

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Appendix D – Summary of different valuation methodologies for pension valuations

The following table summarizes the main similarities and differences in assumptions and methodologies used for i) OTPP's funding valuation, ii) the financial statements of OTPP, prepared under CPA Canada Handbook – Accounting Part IV and iii) actuarial valuation of the Province's share of OTPP prepared for the province under Public Sector Accounting Standards.

Assumption/ methodology	Funding valuation (Going concern basis)	Accounting Part IV of the CPA Canada Handbook – (OTPP Financial statements)	Accounting PSAS – (Province Financial statements)
Purpose	To inform plan sponsors of the amount that needs to be contributed each year to adequately fund benefits and to provide information on the financial position of the plan as of the valuation date on a funding basis in accordance with the Pension Benefits Act, the Income Tax Act as well as generally accepted actuarial practice.	Financial statements [of pension plans] provide information about the pension plan including net assets available for benefits, pension obligations and the financial position of the plan as of the valuation date in accordance with Part IV of the CPA Canada Handbook (Part I of the CPA Canada Handbook (i.e. IFRS) is referred to where Part IV is silent).	Measure and report the obligation for employee retirement benefits, attribute the costs of those benefits to the periods in which the related services are rendered and to provide information on the financial position of the plan in accordance with PSAS.
Actuarial cost method	Modified aggregate method (level cost method)	Projected benefit method prorated on services	
Asset valuation	The actuary should select an asset valuation method that is consistent with the circumstances of the work. The value of assets may be, subject to specific requirements for different types of valuation, any of: • Their market value; • Their market value adjusted to	Fair value for all plan assets. Fair value is determined in accordance with IFRS 13, *Fair value measurement*.	PSAS allows choice regarding the valuing of plan assets at market-related value. Market -related values, are defined as either market values or amounts adjusted to market values over a period not to exceed five years, applied

	moderate volatility in investment returns; • The present value of their cash flows after the calculation date; and • Their value assuming a constant rate of return to maturity in the case of illiquid assets with fixed redemption values For funding valuation, the plan uses the actuarial value of assets which are the market value of assets adjusted for investment gains / losses spread over a period of 3 years.		consistently. The Province has chosen to value OTPP's plan assets by adjusting to market value over a period of 5 years in accordance with PSAS.
Discount rate	Best estimate less Margins for adverse deviations and expenses where appropriate. For funded plans, the best estimate may be either the expected investment return on the assets of the pension plan at the calculation date and the expected investment policy after that date, OR reflect the yields on fixed income investments, considering the expected future benefit payments of the pension plan and the circumstances of the work	Part IV notes that guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 Employee Benefits in Part I of the Handbook. OTPP follows Part I (IAS 19) which requires the use of government bonds when no deep market for high quality corporate bonds exists. Per their financial statements OTPP uses a discount rate based on	Not specified. However two methods are specifically acknowledged in PSAS – a) discount rates determined by reference to plan asset earnings and b) discount rates determined by reference to the government's cost of borrowing. [15] The Province of Ontario uses a discount rate for OTPP determined by reference to the expected long-term

[15] The Public Sector Accounting Board has formed an Employment Benefits Task Force to examine a number of aspects of the existing Public Sector Accounting Standard dealing with retirement benefits, including consideration of the discount rate. To date there have been no due process documents and no indication as to the direction of the PSAB in respect to discount rates.

	For the purpose of the funding valuation, the plan uses a discount rate which is based on market related rates averaged over a period of 36 months. The discount rate used in the most recent funding valuation for OTPP as at January 1, 2015 was 4.85%.	bonds issued by the Province of Ontario. As illustrated in Appendix E, this is inconsistent with other Provincial pension plans in Canada which use as a discount rate, the long-term rate of return on plan assets. The discount rate used by OTPP in their December 31, 2015 financial statements was 3.25%.	return on plan assets. The discount rate used by the Province to account for OTPP in their March 31, 2016 financial statements was 6.25%. This is the long-term rate of return on plan assets which is in accordance with PSAS.
Independent verification		OTPP's financial statements are audited by Deloitte LLP.	The Province's financial statements are audited by the OAG.
Underlying population data	All valuations use consistent underlying data of the population covered by the plan (membership data as at August 30 of the prior year projected to the valuation date is used].		
Inflation rate	All valuations treat inflation in a consistent manner (on a best estimate basis). Best estimate assumptions are derived based on the best estimate of future events. Best estimates of inflation by the Province may be different from those of the OTPP Board, even though they are both best estimate assumptions. In developing its best estimate assumptions, the Province references a broad range of available data, including the best estimate from the OTPP Board.		
Demographic assumptions	Valuations use consistent demographic assumptions (best estimate by the OTPP Board).		Under PSAS, the Province is not required to prescribe demographic assumptions.
Other economic assumptions	The OTPP Board develops its own salary escalation assumption to be used for both the funding and the Board's financial statement valuation. Economic assumptions other than the discount rate, inflation rate and salary assumptions are determined by the Board. These are the same for funding valuation and the Board's financial statement valuation.		The Province prescribes the future salary escalation rates. The Province develops this assumption by referencing the outcome of the most recent collective agreements as

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		well as compensation policies issued from time to time by the government and the historic increases granted.

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Appendix E - Comparison of the discount rates used by Provincial pension plans across Canada relative to the discount rate used by OTPP

Review of Discount Rates Across Jurisdictions

- In the inter-jurisdictional review of all funded provincial sponsored or joint sponsored plans which also have stand-alone plan financial statements:
  - the Ontario Teachers' Pension Plan (OTPP) is the only plan were the discount rate used in the plan's financial statements is more than 50 basis points below the discount rate used by the province.
  - OTPP stand-alone financial statements use the market rate of Provincial bonds.

- All other plans' financial statements (i.e. 23 plans across jurisdictions) use the long-term rate of return as the discount. The discount rate used by the plans' are lower than 50 basis points or less than the provinces' discount rate or at times higher than the provincial rate.

1

Plan's discount rate is lower than the provincial rate by more than 50 bps

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Teachers' Pension Plan (OTPP)	6.25%	LT return on plan assets	ON 1	3.25%	Market rate of Provincial Bonds

2

Plan's discount rate is lower by 50 bps or less (or higher than the provincial rate)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Ontario					
Ontario Public Service Employees Union Pension Plan (OPSEUPP)	6.25%	LT return on plan assets	ON 2	5.75%	LT return on plan assets
Healthcare of Ontario Pension Plan (HOOPP)	5.75%	LT return on plan assets	ON 3	5.65%	LT return on plan assets plus margin
Colleges of Applied Arts and Technology Pension Plan (CAATPP)	6.00%	LT return on plan assets	ON 4	5.70%	LT return on plan assets
Ontario Public Service Pension Plan (PSPP)	6.00%	LT return on plan assets	ON 5	5.95%	LT return on plan assets
Alberta					
Teachers' Post-1992 Pension Plan	6.80%	LT return on plan assets	AB 1	7.00%	LT return on plan assets
Universities Academic Pension Plan	6.00%	LT return on plan assets	AB 2	5.95%	LT return on plan assets

3

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Alberta (cont'd)					
Local Authorities Pension Plan	5.60%	LT return on plan assets	AB 3	5.60%	LT return on plan assets
Public Service Pension Plan	6.00%	LT return on plan assets	AB 4	6.00%	LT return on plan assets
Management Employees Pension Plan	6.10%	LT return on plan assets	AB 5	6.10%	LT return on plan assets
Provincial Judges and Master in Chambers Pension Plan	5.40%	LT return on plan assets	AB 6	5.80%	LT return on plan assets
Supplementary Retirement Plan for Public Service Managers	6.00%	LT return on plan assets	AB 7	6.00%	LT return on plan assets
Special Forces Pension Plan	5.90%	LT return on plan assets	AB 8	5.90%	LT return on plan assets

4

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Saskatchewan					
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	6.50%	LT return on plan assets	SK 1	6.50%	LT return on plan assets
British Columbia					
Public Service Pension Plan	6.50%	LT return on plan assets	BC 1	6.50%	LT return on plan assets
Municipal Pension Plan	6.50%	LT return on plan assets	BC 2	6.50%	LT return on plan assets
Teachers' Pension Plan	6.50%	LT return on plan assets	BC 3	6.50%	LT return on plan assets
College Pension Plan	6.50%	LT return on plan assets	BC 4	6.50%	LT return on plan assets

5

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Quebec					
Commission administrative des regimes de retraite et d'assurances	6.50%	LT return on plan assets less inflation	QC 1	6.40%	LT return on plan assets less inflation
Newfoundland					
Memorial University of Newfoundland Pension Plan	6.30%	LT return on plan assets	NF 1	5.80%	LT return on plan assets
Nova Scotia					
Nova Scotia Public Service Superannuation Plan (PSSP)	6.70%	LT return on plan assets	NS 1	6.15%	LT return on plan assets
Nova Scotia Teachers' Pension Plan (TPP)	6.75%	LT return on plan assets	NS 2	6.25%	LT return on plan assets

6

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
Manitoba					
Civil Service Superannuation Plan	6.00%	LT return on plan assets	MB 1	6.00%	LT return on plan assets plus inflation
Teachers Pension Plan	6.25%	LT return on plan assets	MB 2	6.00%	LT return on plan assets
New Brunswick					
Provincial Court Act and Provincial Court Judges Pension Act (JUDGE)	6.15%	LT return on plan assets		No individual financial statements	
Pension Plan for Management Employees of New Brunswick School Districts (Sch-Mgt)	6.05%	LT return on plan assets		No individual financial statements	
Pension Plan for General Labour, Trades and Services Employees of New Brunswick School Districts (GLTS)	6.05%	LT return on plan assets		No individual financial statements	
Pension Plan for Full-Time CUPE 2745 Employees fo New Brunswick School Districts (CUPE 2745)	6.05%	LT return on plan assets		No individual financial statements	

7

Plan's discount rate is higher than the provincial rate (or lower by 50 bps or less) (cont'd)

	Provincial Nominal Discount Rate	Basis of Provincial Nominal Discount Rate	PLAN REF#	Plan's Nominal Discount Rate	Basis of Plan's Nominal Discount Rate
New Brunswick					
NHMgt, NH-G&S, NH-N&P (i.e NH Nursing Home)	6.20%	LT return on plan assets		No individual financial statements	
CUPE Employees of New Brunswick Hospital (shared risk)	5.45%	LT return on plan assets		No individual financial statements	
Certain Bargaining Employees of New Brunswick (shared risk)	5.70%	LT return on plan assets		No individual financial statements	
Public Service Shared Risk Pension Plan	6.00%	LT return on plan assets		No individual financial statements	
New Brunswick Teachers' Pension Plan (shared risk)	6.15%	LT return on plan assets		No individual financial statements	

8

Appendix F – Comparison of definitions of a Joint Defined Benefit Plan and Government Partnership

The definition of a government partnership is provided in GOVERNMENT PARTNERSHIPS, Section PS 3060 paragraph .06. Section PS 3060 was introduced into the Public Sector Accounting (PSA) Handbook in October 1999.

The definition of a joint defined benefit plan is provided in the glossary to RETIREMENT BENEFITS, Section PS 3250. Section PS 3250 was introduced into the PSA Handbook subsequent to Section PS 3060 in September 2001.

Both standards use similar wording in the definitions of a government partnership and of a joint defined benefit plan illustrating the development of Section PS 3250 considered the content in Section PS 3060.

Below is a comparison of the two definitions as currently in the PSA Handbook (consistent wording between the two definitions are underlined):

	Definition of a government partnership (GP)	Definition of a joint defined benefit plan (JDBP)	Comparison
Introductory paragraph	A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:	A **joint defined benefit plan** is a contractual arrangement between the government and another sponsor or sponsors representing plan participants that has all of the following characteristics:	Consistent in concept with the wording in the GP definition being more general.
Criteria 1	(a) the partners co-operate toward achieving significant clearly defined common goals;	(a) the sponsors co-operate toward achieving the significant clearly defined common goal of providing retirement benefits in exchange for services rendered by the employees;	
Criteria 2	(b) the partners make a financial investment in the government partnership;	(b) funding contributions are shared mutually between the government and the plan members, represented by the non-government sponsor;	Consistent in concept with the definition of a GP focusing on investments in the partnership and the

			definition of a JDBP focusing on contributions into the plan.
Criteria 3	(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and	(c) the sponsors share control of decisions related to the administration of the retirement benefit plan and to the level of benefits and contributions on an ongoing basis; and	Consistent in concept with the wording in the GP definition being more general.
Criteria 4	(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership.	(d) the significant risks associated with the retirement benefit plan are shared on an equitable basis between the government and the plan members, represented by the non-government sponsor.	
Concluding paragraph	The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the	The contractual arrangement establishes that the sponsors have shared control over the retirement benefit plan, and ensures that neither party is in a position to control the plan unilaterally. Nevertheless, overall, there must be an equitable relationship between the funding by the government of the retirement benefit plan, the extent of control it is able to exercise over the plan and the risks and benefits that accrue to the government from the plan.	

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	government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]		

In addition to consistent wording, the concepts in the definitions of a government partnership and a JDBP are similar.

While similar in concept and wording, the definition of a JDBP is more specific than the general definition of a government partnership. GOVERNMENT PARTNERSHIPS, Section PS 3060 is a general standard for all types of government partnerships. Alternatively RETIREMENT BENEFITS, Section PS 3250 addresses specific types of employee retirement benefits including JDBPs.

There is one principle in the JDBP paragraphs in Section PS 3250. Paragraph .081 indicates "*When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]". This principle is consistent with the proportionate consolidation method included in Section PS 3060.

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Appendix G – History of Surplus Utilization for OTPP

The history of OTPP surplus utilization from 1990 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	Contributions by teachers increased by 1 percentage point (from 7.9% to 8.9%) effective January 1, 1990 per legislation.	Legislated an increase in matching contributions (from 7.9% to 8.9%) effective January 1, 1990 and responsibility to finance the initial unfunded liability through a series of special payments	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	$0

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			reduce the value of remaining special payments	
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	

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).

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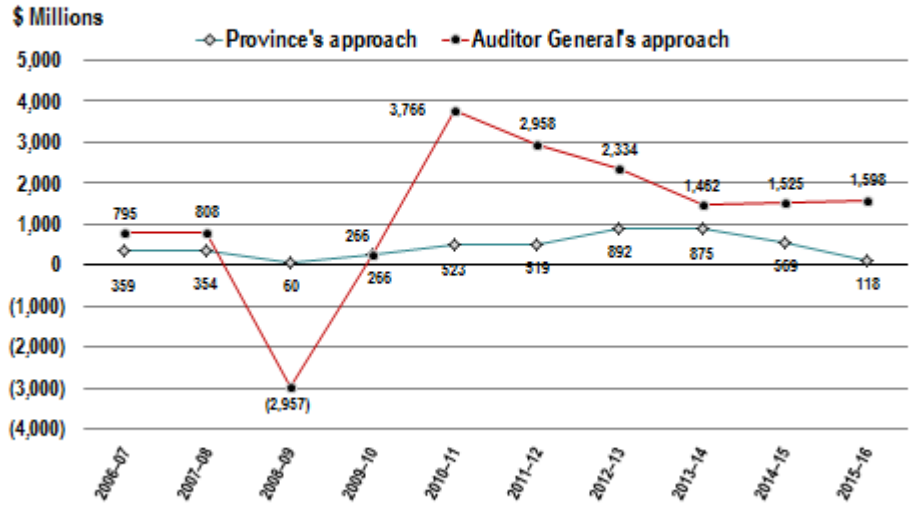
Appendix H - Illustrative impact of 100% valuation allowance on OTPP on key indicators for prior 10 years

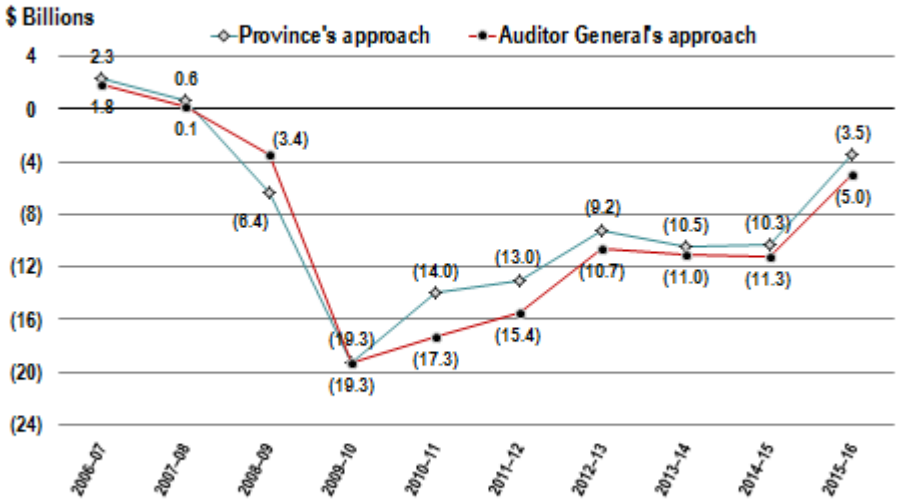
OTPP expense comparison — 10-year

Chart 1



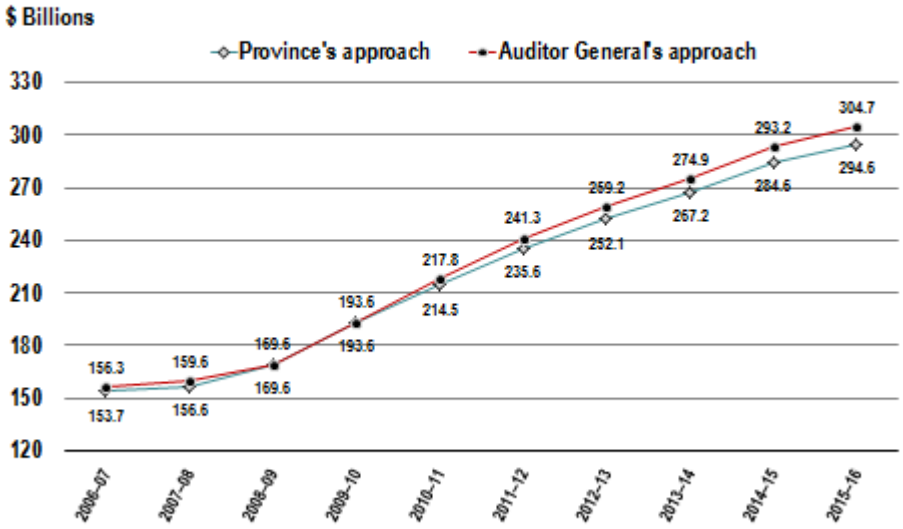
Surplus/(deficit) comparison — 10-year

Chart 2



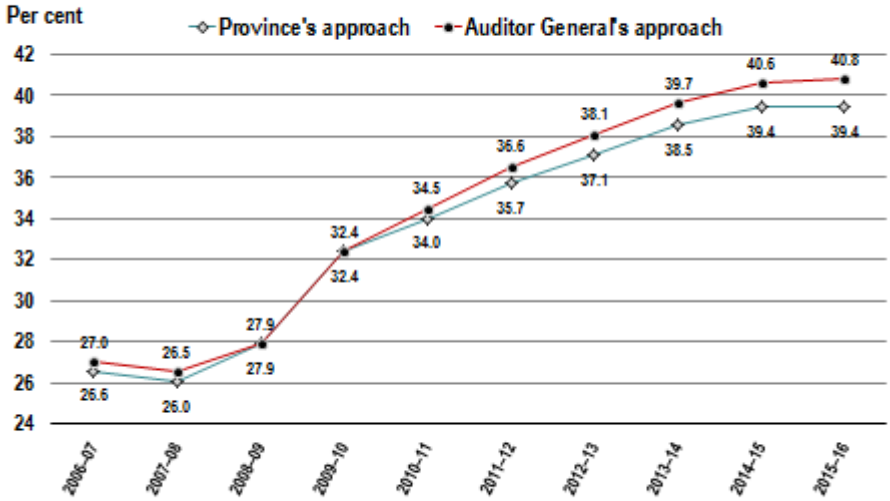
Net debt comparison — 10-year

Chart 3



Net debt-to-GDP comparison — 10-year

Chart 4



Appendix I – Analysis of the British Columbia pension plans in relation to OTPP (prepared by lawyers, Koskie Minsky)

BRITISH COLUMBIA PLANS

In British Columbia, the Municipal Pension Plan, the Colleges Pension Plan, the Teachers' Pension Plan and the Public Sector Pension Plan were all converted from employer sponsored pension plans to jointly sponsored plans in accordance with the Public Sector Pension Plans Act, S.B.C. 1999, c.44 (the PSPPA").

A. British Columbia Municipal Pension Plan (the "MPP")

The MPP is governed by:

(a) Municipal Pension Plan Joint Trust Agreement (consolidated), updated to September 30, 2015 (the "MPP Trust Agreement"); and

(b) Municipal Pension Plan Rules effective April 1, 2000 (current to November 19, 2015).

Under the MPP Trust Agreement, the following rules govern the Sponsors of the MPP and the Board of Trustees of that arrangement in regard to Plan surpluses:

The Board of Trustees may amend the MPP to utilize surpluses under section 11.5, provided that the conditions in 11.5(a) and (b) are met. These provisions permit the Board of Trustees to utilize Plan surpluses to improve Plan benefits for Plan members, provided that the surplus is sufficient to fund the benefit improvement "based on the open group of Plan Members and using a twenty-five year amortization schedule for the Plan actuarial excess to be used to fund the benefit improvement". Any benefit improvement made by the Board of Trustees cannot result in increased contribution rates nor can it create an unfunded liability. Any such improvement must also be consistent with the Trustees' fiduciary responsibilities. Within these parameters, however, the Board of Trustees of the MPP does have the authority to utilize Plan surpluses on an ongoing basis.

The MPP Partners may also amend the MPP using ongoing surpluses in accordance with section 11.3 of the MPP Trust Agreement. This section permits the Partners to direct the Board of Trustees to amend the Plan rules and requires the Board of Trustees to comply with that direction so long as three conditions are met: (a) the Partners first receive and consider the advice of the Board respecting the proposed amendment, (b) the proposed amendment is compliant with the Trustees' fiduciary responsibilities and (c) the proposed amendment will not result in the Plan failing to be funded in accordance with the PBSA going concern funding requirements. Significantly, the MPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the

event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Accordingly, under the MPP, both the Partners and the plan administrator may utilize Plan surpluses by amending the Plan terms in regard to either or both of contribution rates and benefits.

It should be noted that, during a Transitional Period, the use of actuarial gains in the MPP is prescribed by Appendix "B" to the MPP Joint Trust Agreement. During the Transitional Period, all gains must first be used to eliminate unfunded liabilities. Then, actuarial gains must be applied to both (a) reconfigure employer contribution rates and (b) make specified benefit improvements. Employer contribution rates are to be reconfigured by eliminating the 'doubling' feature of employer contribution rates applicable to employees in certain Plan membership categories once they reach either 45 or 50 years of age (depending on the employment category). The transitional provisions prescribe the new base rates for each of the 5 categories of members in the BC, but also stipulate that employer contribution rates for two of the five categories will be increased beyond those base rates to reflect the differential current service cost for those two groups. The surplus implications of the reconfiguration of employer contribution rates are not predictable, and depend, at least in part, on the relationship between the 'base rates' under the transitional provisions and the actual rates being paid by employers at the time of the reconfiguration. Once the employer contribution rates are reconfigured and the specified benefit improvements are made, then 50% of any additional actuarial excesses must be used to fund a contribution rate stabilization reserve, and the balance of the actuarial excess must be transferred to the Inflation Adjustment Account to an aggregate total of $1 billion. The contribution rate stabilization reserve is intended to be shared on an equal (50/50) basis between Plan members and employers in order to maintain or reduce future contribution rates. Until such time as the objectives identified for the Transitional Period are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

B. British Columbia Public Service Pension Plan (''PSPP")

The PSPP Joint Trust Agreement contains provisions regarding the authority of the Partners and the Board of Trustees to utilize ongoing surpluses that are equivalent to the provisions cited above with respect to the MPP. Accordingly, under the PSPP, both the Partners and the Board of Trustees have the authority, in the circumstances and subject to the conditions described in relation to the MPP, to utilize ongoing surpluses to reduce contributions or improve Plan Member benefits.

In this regard, section 10.3(c) of the PSPP Joint Trust Agreement expressly provides the Board of Trustees[16] with the authority to apply ongoing surpluses (the term used in the PSPP Joint Trust Agreement is "surplus assets") in one or more of the following manners:

1. transfer all or portions of surplus assets to the reserve established within the Pension Fund for stabilising contribution rates;

2. transfer all or portion of the surplus assets to the Inflation Adjustment Account;

3. apply all or a portion of the surplus assets to an equal reduction or elimination of Employer and Plan Member contributions to the Basic Account for a period of time;

4. apply all or a portion of the surplus assets to fund changes to the PSPP's benefit provisions provided that any change to benefits does not result in contribution rate increases, does not create or increase an unfunded liability, is consistent with the Trustees' fiduciary obligations and does not conflict the requirement (in s. 13.5) that, upon the termination and wind-up of the PSPP any remaining assets are to be equally shared between the employees and the employers.

At the same time, as is the case for the MPP, the Partners have the authority, pursuant to s.11.3 of the PSPP Joint Trust Agreement, to direct the Board of Trustees to amend the PSPP Plan rules and change either or both of the PSPP's contribution rates or benefits so long as the Partners have received and considered the advice of the Board respecting both the cost and administrative impact of any proposed amendments, the amendment is not inconsistent with the Trustees' fiduciary responsibilities or any funding policy adopted by the board and the proposed amendment will not result in the PSPP failing to be funded in accordance with British Columbia's Pension Benefits Standards Act. Significantly, the PSPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the MPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

Section 15.4 of the PSPP Joint Trust Agreement provides that certain benefit improvements must be made using Plan surpluses that are identified in actuarial valuations dated March 31, 2001 and March 31, 2002. Unlike with respect to the MPP, the PSPP does not appear to have an indefinite 'Transitional Process' that commits all ongoing surpluses until the Transitional objectives are accomplished. Rather, the PSPP Trustees and Partners have had discretionary authority with respect

[16] It is noteworthy that s. 14(c) of the PSPP Joint Trust Agreement stipulates that the Trustees are not acting in a fiduciary capacity when they make decisions that apply ongoing surpluses, and may take account of the financial and other interests of the party that appointed them.

to ongoing PSPP surpluses

C. British Columbia Teachers Pension Plan ("TPP")

The TPP is governed by:

(a) a Joint Trust Agreement made as of April 2, 2001 between Her Majesty the Queen in right of the Province of British Columbia as represented by the Minister of Finance and Corporate Relations (the "Government") and the British Columbia Teachers' Federation ("BCTF");

(b) the TPP Rules.

The Joint Trust Agreement contains provisions permitting both the Partners and the TPP Board of Trustees to amend the Plan rules using ongoing Plan surpluses (section 11 of the Joint Trust Agreement). These provisions are the equivalent of the MPP Joint Trust Agreement provisions regarding the same matters, as described above. In particular, it is significant that the TPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution for either Partner in the event that the they cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses.

As well, Appendix "B" to the TPP Joint Trust Agreement adopts special funding rules for a "Transitional Period" during which the Board of Trustees is directed to use surpluses to achieve specified contribution and benefit improvement outcomes. The transitional objectives for the TPP are not the same as for the MPP, although they entail both contribution rate changes and benefit improvements. In the case of the TPP, however, the transitional provisions build in a 4% reduction in the employer contribution rate from its July 1, 2010 level. As with the MPP, the Transitional Period is of indefinite duration, and only ends when the transitional objectives have been satisfied. During the transitional period, all ongoing surpluses are committed to the transitional objectives and no ongoing surpluses are available for discretionary reductions in contributions or surplus withdrawals.

D. British Columbia Colleges Pension Plan ("CPP")

The CPP is governed by:

(c) the CPP Joint Trust Agreement made April 4, 2011; and

(d) the CPP rules, effective June 22, 2012 (current to April 1, 2016).

The CPP Joint Trust Agreement allocates powers and authorities with respect to ongoing surpluses in the

same way as the other BC Plans.

The Partners have the authority (s.14 (2) of the Joint trust Agreement) to direct the Board to amend the Plan rules, and the Plan Board is required to amend those rules, provided that the Partners "first receive and consider the advice of the Board respecting both the cost and the administrative impact of implementing the proposed amendment" and the proposed amendment is not inconsistent with applicable law or the Trustees' fiduciary responsibilities. Significantly, the CPP constating documents contain no right of recourse to arbitration or other final and binding dispute resolution in the event that the CPP Partners cannot agree on surplus utilization. This contrasts with the OTPP Partners' Agreement, which does provide for third party determinations of differences arising between Partners with respect to surplus uses

Pursuant to subsection 14(4) of the CPP Joint Trust Agreement, the Board of Trustees is also permitted to amend the Plan rules and to utilize Plan surpluses so long as there is no resulting increased in contribution rates, there is no creation of, or increase in, an unfunded liability and the proposed amendment is consistent with the Trustees' fiduciary responsibilities. As with the other BC Plans, the Board of Trustees must use a twenty-five year period for the amortization of the Plan surplus.

Unlike the MPP, TPP and PSPP, the CPP Joint Trust Agreement has no transitional provisions that direct the Board of Trustees as to the application of ongoing surpluses during a transitional period.

III. SUMMARY AND CONCLUSIONS

A. Ontario Plans

OTPP - The governance arrangements with respect to the OTPP provide that the Partners that sponsor that arrangement, being the Minister of Education and the OTF, may utilize ongoing surpluses as they believe appropriate, subject only to the Ontario Pension Benefits Act, R.S.O.
1990, c.P.8 (the "Ontario PBA"). The Board of Directors of the OTPP, being the OTPP administrator for purposes of the PBA, has no authority with respect to the use of Plan surpluses. The OTPP Partners' Agreement anticipates that the Partners will, on a triennial basis, review the results of a preliminary actuarial valuation and determine whether and how they wish to adjust Plan benefits or contribution rates in view of any existing funding deficiencies or ongoing surpluses. The Partners are obliged to bargain in good faith with each other with respect to the disposition of ongoing surpluses, and may have recourse to mediation and final and binding arbitration should they not reach an agreement on their own. An arbitration panel may apply ongoing surpluses to improve benefits or reduce contributions, subject to the limitations set out in section 92 of the Partners Agreement.

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B. BC Plans

Ongoing Surpluses - All of the BC Plans follow the same pattern with respect to the authority to use ongoing surpluses. In the normal course, the Boards of Trustees of the BC Plans, unlike their Ontario counterparts, are permitted to utilize ongoing surpluses through the amendment of the Plan rules governing contributions and benefits, so long as the amendment of the Plan rules does not result in an increased contribution rate for employees or employers, does not create or increase an unfunded liability in the Plan and is otherwise compliant with applicable legislation and the Trustees' fiduciary obligations.

At the same time, each of the BC Plans also permits the Plan Partners to utilize ongoing surpluses by directing the Board of Trustees to amend the Plan rules. The Partners may so direct the Board of Trustees after receiving advice from the Board with respect to the costs of any Plan amendment and the administrative implications of such an amendment, and so long as the proposed amendment is compliant with law and with the Trustees' fiduciary obligations. However, unlike for the OTPP, the BC Plans' constating documents provide neither Partner with a right of recourse to a third party for a final and binding determination concerning surplus utilization.

Transitional Period- In addition, three of the four BC Plans we have reviewed (MPP, TPP and, for only two years, the PSPP) contain special rules governing the utilization of ongoing surpluses during a "Transitional Period". In these cases, the Transitional rules require that ongoing surpluses that emerge during the Transitional Period are to be used to restructure the employer contribution obligation and improve benefits. In the cases of the MPP and TPP, the Transitional Periods do not come to an end until all of the intended uses of ongoing surplus during the Transitional Period have been fulfilled. We are not currently aware as to whether the Transitional Periods for the MPP and the TPP remain ongoing, or have terminated. Until such time as the objectives identified for the Transitional Periods are fulfilled, there is no discretion left to either the Partners or the Board of Trustees to utilize ongoing MPP surpluses.

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Appendix J – Summary of OTPP Funding Rate Assumptions and Provincial Discount Rates vs. Actual Performance

Ontario Teacher's Pension Plan
Rate Comparison

	OTPP Annual Performance	OTPP Filed Discount Rate *	Province Economic Assumption for Nominal Return
2005	17.2%	6.48%	7.00%
2006	13.2%		7.00%
2007	4.5%		6.75%
2008	-18.0%	5.65%	6.75%
2009	13.0%	5.00%	6.75%
2010	14.3%		6.75%
2011	11.2%	5.40%	6.75%
2012	13.0%	5.30%	6.75%
2013	10.9%		6.75%
2014	11.8%	4.95%	6.75%
2015	13.0%	4.85%	6.50%
2016	n/a	n/a	6.25%

* The plan does not file a valuation annually. Under the Pension Benefits Act, plans must file at least every three years

Ontario Teacher's Pension Plan
Plan Performance

2015	13.0%
2014	11.8%
4 - Year	12.2%
10- year	8.2%
Inception	10.3%

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Perpetuity Request.rtf

From: Petsche, Nadine (TBS) []
To: uros.karadzic@ca.ey.com [uros.karadzic@ca.ey.com]
CC: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
Subject: Perpetuity Request
Date: Monday, June 05, 2017 21:47:31

Hi Uros.

I was hoping that you might have a few minutes to chat tomorrow regarding the AG's request to run the asset ceiling test under a perpetuity assumption.

Thanks,

Nadine

Please note.rtf

From: Petsche, Nadine (TBS) []
To: matthew Colley [mcolley@deloitte.ca]; Raymond, Martin (CA - Montreal) [maraymond@deloitte.ca]
Subject: Please note
Date: Sunday, September 11, 2016 19:40:59

Matt/Martin,
We are expecting to receive a copy of a draft legal opinion later today which we hope will be finalized by tomorrow am. I will send you a copy once it is received and would appreciate it if you could review it provide feedback or concerns. Thanks. Nadine

Position Paper V1 to cv.docx.rtf

From: Petsche, Nadine (TBS) []
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
Subject: Position Paper V1 to cv.docx
Date: Thursday, September 22, 2016 19:12:38
Attachment 1: Position Paper V1 to cv.docx
Attachment 2: AG OPCD Deloitte Meeting Sept 21 16 Pensions DRAFT to CV.doc

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Position Paper V1 to cv.pdf

Draft Position Paper on Accounting for Joint Defined Benefit Plans
in the Province's 2015-16 Public Accounts (September 22, 2016)
Accounting Policy and Financial Reporting

Executive Summary

During the course of the audit of the 2015-16 consolidated financial statements for the Province, the Auditor General asked if the reported pension assets for OTPP and OPSEUPP might be impaired in accordance with PS3250 and requested an actuarial valuation.
Subsequent to being provided with the results of the actuarial assessment, the Office of the Auditor General communicated issues with the accounting treatment for the assets on the Province's books, in effect, challenging the Province's interpretation of PSAB standards which had been in place for the past 15 years.

According to the Auditor General's interpretation of PS 3250, the entire balance of $10.6 billion of pension assets related to OTPP and OPSEUPP would have to be written off of the Province's balance sheet as an error, and on a go forward basis, only the value of negotiated and agreed to benefits to the government through reduced contributions could be reported on the Province's financial statements, to the extent that the supporting agreements were in place as at fiscal yearend.

Based on input from an external audit opinion and management's knowledge of the frameworks in place for the pension plans, the province should retain past practice with regards to reporting the Province's share of the pension assets on the consolidated financial statements of the Province, and apply PS 3250 paras .050 - .059 as relevant to the substance of a joint defined benefit plan.

Furthermore, the Province should continue to work with the Auditor General and the Public Sector Accounting Board to work towards enhanced accounting guidance which more explicitly addresses expectations with regards to joint benefit pension plans and the application of the principle of substance over form with regards to such plans.

I. Background

i. Historical practice

The Province has reported an accrued pension asset for OTPP and OPSEUPP since 2001-02 Public Accounts. The accrued pension asset positions have been gradually growing since that time. As of March 31, 2016, the Province will reporting a net pension asset position of $10.1 billion for OTPP (excluding RCA) and $420[1] million for OPSEUPP.

ii. 2015/16 Public Accounts Reporting

Identification of potential accounting issues and areas of audit focus for the following year's audit are typically communicated through the Audit Findings Report for the prior

[1] Excludes consolidation agency adjustments for pension contributions reported as an expense by the government controlled organizations included in the government reporting entity.

year's audit. Per **Attachment 1**, the Audit Finding Report for the 2014-15 Public Accounts Audit (Page 4) makes reference to the AG's planned review of economic assumptions, excluding any reference to the Province's reporting for the defined pension assets.

The Auditor General's 2015 Annual Report (Attachment 2) also excludes any reference to any concerns regarding the Province's accounting for pensions, and the only reference to pension in Chapter 2 is in regards to PSAB's project on Employee Future Benefits.

As more detailed audit plans were developed, the Office of the Auditor General shared a copy of the draft Audit Planning Report in February, 2016 (**Attachment 3**) which reflected a focus on economic assumption in relation to pension related reporting on the Province's books (i.e. inflation, salary escalation rates, management's best estimates of return).

During subsequent audit planning discussions between the Office of the Provincial Controller and the Office of the Auditor General, no mention was made to any concerns with the accounting treatment of the pension assets related to OTPP or OPSEUPP. In June, 2016 the OAG audit staff started to enquire about the OTPP and OPSEUPP assets being reported on the Province's books. The OAG advises via email correspondence that the matter had not previously been identified as an issue (See June 14th email, **Attachment 4**).

In mid-June, the OAG staff requested that OPCD undertake an actuarial assessment to determine if asset impairment existed on the pension assets being reported on the Province's books (see **Attachment 5**). The correspondence did not include any reference to para. 059 in PS 3250 which we have subsequently learned is a focus of the Auditor General (i.e. unilateral right to withdraw surplus), nor were any questions raised regarding any agreements that the Province might have in place with OTF as at March 31, 2016.

- Following a competitive tendering process, in response to the OAG's request, an external firm was engaged to assess the applicability of the asset ceiling test for Ontario's 2015-16 financial statements.
- On August 19th, copies of the reports summarizing the results of the external firm's assessments for OTPP and OPSEUPP were shared with the Office of the Auditor General, including supporting documentation which had been reviewed by the external firm. (See **Attachment 6a** and **6b**)
- On August 26th, OPCD received an email from the OAG containing some follow up questions related to the external firm's analysis, including for the first time a reference to para .059 in PSAS 3250. (See **Attachment 7**)
- On September 1st, OPCD and the external firm met with representatives of OAG to review the results of their additional analysis and explain rational for the responses to the OAG's questions. (**see Attachment 8** – Responses to OAG Questions). During this discussion, OPCD enquired twice whether the OAG would require a legal opinion in relation to the work they were doing to which no requirement was identified. During the same meeting, staff made reference to the fact that British Columbia does not report any pension assets on its books.
- On September 6th, OPCD provided the OAG with additional background on how the ON plans were different than those in British Columbia. (**see Attachment 9**)
- On September 6th, OPCD received a response from the OAG which focused on legal rights. (See **Attachment 10**) Based on the responses to OPCD's questions during the meeting on September 1st, this new position was a surprise.
- Since September 6th, TBS and MOF representatives, including some discussions involving external advisors, has dialogued with the OAG in an effort to better understand the Auditor General's interpretation of the PSAB standard.

- A decision was made to build upon the Statement of Work already in place with the external firm to expand upon its advisory services with the intention of providing an accounting opinion. On September XX, the external firm completed its reported and provided it to TBS. The results of the report were used to inform the accounting policy for joint defined benefit based plans for purposes of the Province's consolidated financial reports.

iii. Impact on 2015-16 Public Accounts Audit Process

- As noted above, challenges raised by the Auditor General with regards to the Province's historical reporting of pension assets for the joint defined benefit plans arose very late in the audit.
- The AG did not clearly communicate any specific challenges to the Province's accounting treatment for the OTPP and OPSEUPP assets until very late in the audit process.
- As a result of the nature and timing of the concerns raised by the AG, TBS and MOF management were challenged to obtain sufficient, appropriate evidence to support their a potential change in the Province's historical practice which had received a clean audit opinion for the prior 15 years.
- While the AG advised that she had already received an accounting opinion(s) supporting her interpretation, TBS management undertook to acquire legal and accounting opinions on a timely basis to help inform judgment on the most appropriate basis to report the OTPP and OPSEUPP asset balance under PSAB.
- Obtaining external advice required working closely with external advisors and internal stakeholders to ensure a common and robust understanding of the facts to inform management's decision on the most appropriate basis of reporting to reflect the underlying economic substance of the Province's activities and financial position.
- Without adequate support to inform an opinion, Management would not be able to sign off on the Management Letter of Representation attesting to their judgment that the financial statements were prepared in accordance with PSAB, nor the Statement of Responsibility in the Province's Annual Report which contains similar attestation.

iv. External Advisor's Report

In collaboration with Income Security & Pension Policy (MOF), Pension Policy Unit (TBS), MOF engaged external actuaries to work on both the OTPP and OPSEUPP assessments. OPCD engaged an external firm to review the value of the pension assets reported on the Province's March 31, 2016 consolidated financial statements under PS 3250.

Based on a review of relevant documentation, the external review supported the reported asset values on the books as reflecting Province's expectation to benefit from the accrued benefit asset reported for both OTPP and OPSEUPP, either through withdrawing surplus or taking a contribution holiday in the future based on current funding management policy (FMP) of OTPP and OPSEUPP.

Based on the results of the initial analysis (Aug. 19), and subsequent support provided by Deloitte in response to the AG's August 26th follow-up questions, the Province's past accounting treatment appeared to be supported.

v. Auditor General's written position

In response to a request from TBS, the AG provided a written summary of her position which reflected input/advice that she had received from her own advisors and other sources. The letter (**Attachment 11**) stated that the AG's interpretation would require both a unilateral right to access the surplus by the Province, and that irrevocable written agreements be in place as at year-end in order for an asset to be reported on the province's books. Her letter stated that she would expect for 100% of the asset to be written off of the Province's balance sheet as at March 31, 2016.

vi. Meetings between TBS, MOF and the AG

Following receipt of the AG's letter, a meeting was held on September 14th which included staff from TBS, MOF, the OAG and representatives from the external advisory firm to allow the external advisors to better understand the AG's position as input to providing their accounting advisory services.

On September 15th, the Deputy Ministers of TBS and MOF had an audit closing meeting with the Auditor General to bring closure to all matters related to the 2015-16 Public Accounts audit, notwithstanding the pension asset ceiling matter for OTPP and OPSEUPP. During the meeting, the proposal was made to adopt legislated accounting as a solution to addressing the AG's position which would allow for the same impact to be reported as desired by the AG, and for management to sign off on the Management Letter of Representation and Statement of Responsibility. Initially, the Auditor General accepted this proposal but subsequently rejected it and said she would issue a qualified audit opinion.

Since that time, TBS continues to provide the external audit firm with access to materials and persons necessary to complete their work, and has also engaged a second firm to provide accounting advisory services on this matter.

vii. External Accounting Opinion

On Sept XX, the report of the external firm was received with XXXXX

Key considerations in the external firm's report include:

viii. Management's Responsibility

It remains management's responsibility to apply its discretion in deciding whether to accept the opinion of the external advisor. In this particular case, and after serious consideration, TBS and MOF management have decided that XXX.

For the 2015-16 Public Accounts, a valuation allowance is not required for both OTPP and OPSEUPP. The Province will continue to monitor and assess whether the accrued pension asset may become impaired in the future.

Commented [np1]: Legal terms being reviewed by LSB (unilateral access to 'surplus' pool).

Attachments: TBD

Original request from AG in June re: actuarial

Deloitte initial report

Follow up questions

Follow up answers

Note to OAG on BC comparative

Response from AG on relevance of legal access

AG written position

Deloitte's opinion

Attachment X

Below are some extracts from the PS3250 which are relevant for calculating the limit on carrying amount of accrued benefit asset (the asset ceiling test) and the joint defined benefit which are relevant to the analysis and position taken for financial statement preparation.

Limit on the carrying amount of an accrued benefit asset

.050 *An accrued benefit asset should be presented on a government's statement of financial position net of any valuation allowance. When a defined benefit plan gives rise to an accrued benefit asset, a government should recognize a valuation allowance for any excess of the adjusted benefit asset over the expected future benefit. A change in valuation allowance should be recognized in the statement of operations for the period in which the change occurs.* [SEPT. 2001]

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

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

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

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

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

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

a. the present value of its expected future accruals for service for the current number of active employees, less the present value of required employee contributions and

minimum contributions the government is required to make regardless of any surplus; and

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

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

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

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

Joint defined benefit plans

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

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

benefit plan.

.081 *When a government participates in a joint defined benefit plan, the government's risk is limited to its portion of the plan. The government should account for its portion of the plan in accordance with the standards for defined benefit plans.* [SEPT. 2001]

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

Attachment X

List of documents reviewed

Funding management policy (FMP) of OTPP
Asset ceiling documentation from Allan Shapira (Aon) dated August 2, 2016
Actuarial valuation report of OTPP as at January 1, 2015 – funding purposes
Accounting standards PS3250 on post-employment benefits
Teachers' Pension Act
OTPP Partner's Agreement
Supporting document from OTPP to OPCD on accounting results, including the communication from Mercer on valuation results for different assumption basis – both documents dated Jan. 26, 2016

AG OPCD Deloitte Meeting Sept 21 16 Pensions DRAFT to CV.pdf

MEETING SUMMARY

TOPIC **OAG/Deloitte LLP/OPCD Discussion on Pension Asset Ceiling**

MEETING DATE(S): **September 21, 2016, 4:15 – 6:00 PM**

LOCATION: **7 Queen's Park,**
2nd Floor, Frost South, ADM Boardroom

ATTENDEES: Cindy Veinot (OPCD)
Nadine Petsche (OPCD)
Kerry Danyluk (Deloitte LLP)
Matthew Colley (Deloitte LLP)

Bonnie Lysyk (OAG)
Susan Klein (OAG)
Bill Pelow (OAG)
David Catarino (OAG)
Audelyn Budihardjo (OAG)
Benjamin Leung (OAG)

Note: This summary follows the order of the discussion between the Office of the Controller General, Deloitte LLP (external accounting advisors to OPCD), and staff of the Office of the Auditor General as at September 22, 2016.

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Discussion Highlights

Remarks by Auditor General/OAG

- Stated that she was here just to listen to what Deloitte has concluded
- In terms of reasonable expectations, a key here is whether the $4.3B has been looked at. Wanted to get additional details on the calculation of this amount
- Referenced the OTPP's financial statements and different result vs. surplus. (OPCD and Deloitte LLP pointed out that the OTPP's financial statements are prepared on a different basis – IFRS- and use different assumptions. Discussed the fact that the $4.3M in value from the recent decision regarding indexation was calculated on a funding basis. Bonnie suggested that we putting forth a position that the funding source as the same value that should be reported for accounting purposes (to be used as a proxy for the asset value). Delotitte reiterated that it would not be suggesting a value in its opinion letter, and reminded that AG that for funding purposes, values are typically more conservative. OPCD remarked that the AG's comments did not reflect our position or what we were putting forth which is that no valuation allowance is necessary.
- The AG commented that the buildup of the pension asset is because of a difference between the discount rates used between the Plan and the government. (see discussion above regarding purpose of discount rates.)
- The AG suggested that the government was following a different approach to discount rates than other governments which explained the difference between the OTPP's rates and the government. OPCD referenced research analysis that had been shared with the OAG which showed that ON's practice is consistent with most other Senior governments in Canada with regards to using management's best estimates on return, and that in fact, it is the OTPP which is an outlier in using a rate 'other than the sponsor's' rate (management's best estimate of return) for its financial statements. It is this difference in OTPP's practice which accounts for the big difference between what the OTPP reports and what ON reports.
- The AG said that government would have to be comfortable commenting that they have entitlement to the $10.6 B of the teacher's retirement fund (that the asset is supposed to mean something).
- The OAG commented, in relation to the $4.3B benefit, that the accounting valuation doesn't respond at all because the f/s reflect 100% indexation (w.r.t. share the pain).
- The AG asked Deloitte to explain how the pension asset met the definition of an asset. Deloitte responded that there is no need to look to PS1000, since PS 3250 was developed within PSAB's conceptual framework which recognizes assets.
- The AG commented that she doesn't feel that uncertainty is ok, and that there were no agreements in place as at March 31/16. She observed that the asset was increased due to differences between the OTPP's and ON's rates. It is an accounting issue – PSAB allows different rates, but PS3250 requires that you have to see 'what is behind the asset'. It is more than just about applying PS 3250.
- The AG mentioned the BC example, stating that it was not a different situation and that it was the same scenario. She also mentioned a situation in QC where the assets had to be written down.
- The AG said that the value of the asset would need to be documented to really support the value. Would be looking for a document prepared between the OTF and the government (an agreement as at XXX), but none of this is documented to support the asset. Need documented, concrete evidence.
- Commented that the situation could change, and that the value could change not because nobody knew but because they didn't want to tell the AG until 3 months after year end.
- She suggested that perhaps Deloitte LLP didn't have all of the information that they needed to inform their decision, implying that the government was withholding information that they needed to complete a robust analysis.
- She said she appreciated that Deloitte LLP had looked at the situation, but wondered aloud why nothing

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Discussion Highlights

is in front of her regarding the Province's position if we are all comfortable at out.

- The AG said that there may be some aspects worth looking at – an analytical review of the pension expense and how it impacts the fiscal plan. She said that for the most part that governments use the funds' rates of return. OPCD contradicted the AG's remarks and reminded the AG of our analysis which had been shared with her office which stated that the government's use the estimated rate of retune and the plans are for the most part using their sponsors' rates (that it is OTPP which is different)
- The AG said that there is a need to look behind the scenes at the negotiations between the OTF and the Ministry. She said that rates get tweaked with an objective of the impact on the bottom line, and that this is history on how it has played its way out over the past 10 years.
- She said that she would have expected a provincial position paper from the government.
- She feels that she has a strong position and doesn't agree with the position being taken.
- She wants proof for the asset value being reported.
- She referenced 2 faxes being received the night before a meeting that she was supposed to take into consideration w.r.t. asset values. (OPCD asked to clarify which faxes she was referring to. AG said it was the July and Aug docs related to the $4.3B, and that if we were suggesting that as the value of our asset that we should have provided more than that. OPCD reminded the AG that the docs were provided in response to a request she made in a telephone call earlier in the day but she didn't recall making such a request. OPCD also advised that the documents weren't intended to reflect our position of the asset value.)
- The AG commented on the Province's legal opinion (internal) as not being solid. Deloitte also stated that the legal letter will not confirm that there is a unilateral right to access an asset for surplus withdrawals (as would be relevant under para.059 only).
- The AG reiterated what she would need to see to report an asset is an 'irrevocable agreement in place as at March 31st'.
- She commented that the FMP is just an agreement to negotiate, and that negotiations are the next level up.
- She commented that there were also opportunities to improve our pension disclosure as the pension assets are current reported as a reduction to our pension liabilities.
- The AG made it clear that if the government would not change the financial statements in accordance with her view, that her messaging would be different than if we were to agree that the write-down of $10.6 B was an error. The AG reminded OPCD of her solution of recording the full impact to accumulated deficit over 15/16 and 16/17.
- With regards to her messaging, she said that she would say how over the past 10 years the government's deficits have been understated by XXX.
- The AG asked again how the asset would be used in the future. Her staff asked how the balance would be expected to decline in the future? They suggested that it will only continue to increase in value and that is why it has to be addressed. With regards to questions on future reduced contributions and the amount of share the pain contributions reflected in the actuarial valuations (~$1M), Deloitte clarified for the AG that it only relates to the teachers who have retired since 2009, and that prior to 2008 the plan was fully indexed. The previous negotiations lowered the benefit obligation to teachers but introduced the share the pain payments for funding purposes. For accounting purposes, the obligation has continued to be calculated at 100%.
- The AG asked how the taxpayers will ever see the benefit of the asset and suggested that the government's accounting was being used to manipulate the accounting, that it had grown from $200M to $10.6 B over the past 10 years.
- With regards to OPCD's observations that the AG's approach being susceptible to manipulation of the bottom line each year by having an agreement in place (which would be contrary to the spirit of the standard which addresses long term liabilities), the AG commented that she would be fine

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Discussion Highlights

with that. She 'wouldn't disagree with being able to take the amount in the agreement back into revenue when there is an agreement at year end'. (Note that this would mean that the AG's approach would report the $4.3B indexation amount as revenue in 16/17).

- When asked for her position, Susan Klein, the Deputy AG, commented that she supports Bonnie's position on the mater, stating that they could take the intention of the standard as requiring that there is an agreement in place as at year end.

OPCD and Deloitte LLP comments

- Acknowledged and thanked the AG for her feedback on the Statement of Facts that Deloitte's had sent earlier in the week.
- Commented that certain parts of PS 3250 don't necessarily fit together
- Reiterated understanding that the AG was looking for there to be an agreement at year-end for which there was none
- With regards to the concept of a Joint Defined Benefit Plan(JDBP), it was observed that the rules were written for a liability situation (similar to the rest of the handbook) as opposed to assets, with a focus on risks
- Within PS 3250, the guidance says that JDBPs should follow the rest of the rules for defined benefit plans (e.g. para 50 – 59)
- With regards to the test for legal enforceability, Kerry does not see this as the applicable test when one is assessing benefits expected from contribution reductions
- Relevant parameters are para .052 which deals with uncertainties and the ability to use the surplus for either a contribution holiday or a reduction
- $4.6B from the funding basis. Using funding source to pay is the same.
- Kerry acknowledged that unlike a sole sourced plan, other parties do need to agree and in this regard, the TPA deals with matching contributions, but it is less clear about the applicability of surpluses. There is more judgement involved w.r.t. assessing uncertainty but not enough to suggest that there needs to be a full valuation allowance.
- With regards to testing for expectations and minimum contributions, there is a diversity of practice (whether should test every 3 years, every 15 years)
- Kerry pointed out that the government can negotiate a reduction and contemplates to share in surplus
- In terms of framing the thought process, it is important that the government feels good enough about the design of the plan to develop a reasonable expectation (para 55) to support the asset
- Kerry commented on the $10.6 B vs. $4.3 B (savings of what the government would have to pay anyway)
- Kerry commented that she wouldn't be able to take the rest to an opinion level
- Bonnie w.r.t. $4.3 billion – is it a reasonable explanation that ON could expect a benefit from the asset in its entirely over the fullness of time
- The funding position of the plan will determine how quickly the province will be able to utilize the asset. (once full indexation has been restored and out of the restoration zone). In terms of the $4.3B value for indexation – Cindy clarified for the AG that it represented the present value of payments you would have to make in the future (in perpetuity, until the end of the plan and the last teacher retires.) Deloitte clarified for the AG that the calculations are related to teachers retiring after 2009, and that the amounts could expect to get larger as more of those teachers retire. (This comment was made in response to the OAG's remarks regarding the amount reflected in the actuarial valuation where >$1M payments were made in relation to the fund in relation to indexation and questioning on how the $4.3B was calculated.)
- With regards to OTPP's financial statements, the AG
- With regards to the difference between a sole sponsored PP vs. a JDBP, with a SS plan, there was some discussion with regards to the expectation of reduced contributions. Reference was made to the Zones that would impact the ability of the government to expect a reduction in future contributions.

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Discussion Highlights

- Deloitte restated its position that no agreement needs to be in place as at year end, but rather what is looked to is the framework that is in place and the reasonable expectation (looking at past history from the day that the plan has been in place. There is an expectation/contemplation that inflation protection will eventually be restored and that the government will benefit from reduced contributions.
- Deloitte and OPCD restated that the $4.3B that the AG kept referring to could NOT be crosswalked to the accounting numbers because it is calculated based on funding.
- OPCD commented that the $10.6B in reported asset value was also net of a $9 B unamortized gain balance which demonstrates that actual returns have actually exceeded management's best estimate of return.

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Public Accounts meeting 5_30pm .rtf

From: Petsche, Nadine (TBS) []
To: kdanyluk@deloitte.ca [kdanyluk@deloitte.ca]; Colley, Matthew (CA - Toronto) (mcolley@deloitte.ca) [mcolley@deloitte.ca]
CC: Veinot, Cindy (TBS) [Cindy.Veinot@ontario.ca]; Chen, Raymond (TBS) [Raymond.Chen@ontario.ca]
Subject: Public Accounts meeting 5:30pm
Date: Thursday, September 22, 2016 13:31:03

Hi Kerry and Matt.
As discussed, you are invited to discuss your findings on PS 3250 this afternoon at 5:30. Location details are provided below. We will provide your names to security.

Whitney Block Rm 6420, 99 Wellesley St W, Toronto, ON M7A 1A1

Nadine

Public Sector Pension and Non-Pension Benefit Advice _ TBS-OTB-OPCD-22.rtf

From: Warburton, Cara (CA - Toronto) [cawarburton@deloitte.ca]
To: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
CC: Raymond, Martin (CA - Montreal) [maraymond@deloitte.ca]; Colley, Matthew (CA - Toronto) [mcolley@deloitte.ca]
Subject: Public Sector Pension and Non-Pension Benefit Advice | TBS-OTB-OPCD-22
Date: Wednesday, December 06, 2017 11:40:07
Attachment 1: image003.png
Attachment 2: letter attached

Thank you very much for notifying us of this contract decision. Please can we book a debrief meeting to receive feedback on our response.

Thanks

Cara

--

Cara Warburton

Senior Manager | Public Sector

22 Adelaide Street West, Suite 200, Toronto, ON, M5H 0A9, Canada

D: (416) 601 5763 | M: (647) 300 9400

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letter attached.pdf

From: Virani, Shyrose (TBS) [Shyrose.Virani@ontario.ca]
To: CA Ontario Online Bidding (CA) [onlinebidding@deloitte.ca]
Subject: letter attached
Date: Wednesday, November 29, 2017 10:50:26
Attachment 1: 20171129094441568.pdf

Public pension plans research.rtf

From: Christina Chan [Christina.Chan@ca.ey.com]
To: Petsche, Nadine (TBS) [Nadine.Petsche@ontario.ca]
CC: Uros Karadzic [uros.karadzic@ca.ey.com]; Shayan Jafrani [Shayan.Jafrani@ca.ey.com]
Subject: Public pension plans research
Date: Friday, April 21, 2017 13:42:51
Attachment 1: image002.jpg
Attachment 2: Public pension plans - comparison summary.xlsx

Hi Nadine,

As requested, we have completed our research on the public pension plans in British Columbia and Alberta for purposes of comparing reporting with the CAAT/HOOPP plans in Ontario. This email serves as a commentary to the file attached.

The summary file is set up with the key “criteria checklist” that we believe would simplify and assist with the comparison. We appreciate your offer to have your team research other plans. The file includes the plans in Manitoba and Saskatchewan that we have identified for your team to consider. We suggest that extracting the key plan information and summarizing it in the template as we have done for Alberta and BC plans would be most helpful in determining if the plans are comparable to CAAT/HOOPP. If a meeting with your team that will be doing the research will help clarify the task, please let us know.

We have focused on public sector plans in British Columbia, Alberta, Manitoba and Saskatchewan given the following considerations:

- Federal plans are not comparable as they are generally solely sponsored by the Federal government

- Public sector plans in the Eastern provinces (New Brunswick, Newfoundland, Nova Scotia, P.E.I.) were excluded due to the changing nature of the plans with the conversion to shared risk model in these provinces–

For British Columbia and Alberta, we considered the plans for which the provinces reported an obligation on a defined benefit basis. We excluded plans which are relatively small or plans with limited information available. Our analysis is based on the review of plan texts, funding policies, governance documentation and financial statements, as available on the government and pension plan websites.

Key observations

With the exception of the Alberta Teachers' Plan, all the public plans in British Columbia and Alberta we have researched appear to be comparable to CAAT/HOOPP:

- In particular, the Alberta UAPP appears to be most comparable as it also has a similar governance structure. The plan appears to have both employer and employee legal sponsors. Further, according to the sponsorship agreement (post 1992), the province is not a legal sponsor and does not appear to have direct control over benefit/contribution levels, similar to CAAT/HOOPP. The plan is accounted for on a joint defined benefit plan basis. The plan is currently in a deficit position at 31 March 2016.

- The respective boards of the other Alberta plans (PSPP, MEPP and LAPP) have control of the benefit/contributions levels. Alberta is listed as a "participating employer" for the MEPP and PSPP. We note that although the plans are contributory, they do not have a legal employee sponsor. Similar to the CAAT/HOOPP, other employers participating in the plans appear to apply defined contribution (DC) reporting. The plans are accounted for on a joint defined benefit plan basis. The plans are currently in deficit positions at 31 March 2016.

- For the BC plans, the province is clearly a legal sponsor of the plans, unlike CAAT/HOOPP. However, the province does not have the same degree of control over benefits and/or contribution levels as Ontario would have over OTPP or OPSEUPP. Rather, the respective boards have some authority to change benefits/contribution levels without the province's consent. The plans are accounted for on a joint defined benefit plan basis. A valuation allowance is applied to impair any balance sheet asset (where applicable), similar to Ontario's treatment of CAAT/HOOPP.

- The Province of Alberta is a legal sponsor of the Teachers Plan. It is unclear whether they have decision making authority on contribution/benefit levels.

Based on the observations above, the current defined benefit reporting of CAAT/HOOPP applied by the Province of Ontario is not inconsistent with the reporting of comparable pension plans in Alberta and British Columbia.

Let us know if you would like to further discuss.

Regards,

Christina

Christina Chan, ASA | People Advisory Services | Manager

Ernst & Young LLP
Ernst & Young Tower, 222 Bay Street, P. O. Box 251, Toronto, ON M5K 1J7 Canada
Phone: +1 416 943 3121 | Cell Phone: +1 647 834 6683
EY/Comm: 1622451 | Christina.Chan@ca.ey.com
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image002.pdf

EY

Public pension plans - comparison summary.pdf

Public Pension Plans Comparison

Province	Ontario				British Columbia			
Plan	**OTPP**	**OPSEUPP**	**CAAT**	**HOOPP**	**CPP**	**MPP**	**PSPP**	**TPP**
Is the Plan reported as a joint defined benefit plan?	Y	Y	Y	Y	Y	Y	Y	Y
Is an obligation reported?	Y	Y	Y	Y	Y	Y	Y	Y
Is the plan in an asset position, prior to valuation allowance?	Y	Y	Y	Y	Y	Y	Y	N
Is the asset impaired?	N	N	Y	Y	Y	Y	Y	n/a
Control over contributions levels:								
Province	Y	Y	-	-	Y	Y	Y	Y
Employee sponsors	Y	Y	-	-	Y	Y	Y	Y
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board	Y	Y	Y	Y
Control over benefit levels:								
Province	Y	Y	-	-	Y	Y	Y	Y
Employee sponsors	Y	Y	-	-	Y	Y	Y	Y
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board	Y	Y	Y	Y
Notes								
					Each board of trustees may amend the plan (contribution and benefit level) related to utilizing surplus, with certain restrictions (e.g. not creating an unfunded liability)			
Legal sponsors								
Province (directly)	ON	ON	n/a	n/a	BC	BC	BC	BC
Other Employers	n/a	n/a	CEC	OHA	Post-Secondary Employer's Assoc.	n/a	n/a	n/a
Employees	OTF	OPSEU	OPSEU, OCASA	ONA, CUPE, OPSEU, SEIU	Employee's Union	Union of BC Municipalities; Municipal Employees' Pension Committee	BCGSEU; Professional Employees Assoc.; Union of Psychiatric Nurses	BC Teacher's Federation

Public Pension Plans Comparison

Province	Ontario				Alberta				
Plan	**OTPP**	**OPSEUPP**	**CAAT**	**HOOPP**	**LAPP**	**PSPP**	**MEPP**	**Teachers**	**UAPP**
Is the Plan reported as a joint defined benefit plan?	Y	Y	Y	Y	Y	Y	Y	Y	Y
Is an obligation reported?	Y	Y	Y	Y	Y	Y	Y	Y	Y
Is the plan in an asset position, prior to valuation allowance?	Y	Y	Y	Y	N	N	N	N	N
Is the asset impaired?	N	N	Y	Y	n/a	n/a	n/a	n/a	n/a
Control over contributions levels:									
Province	Y	Y	-	-	-	-	-		-
Employee sponsors	Y	Y	-	-	-	-	-	Unclear	-
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board	LAPP Board	PSP Board	MEPP Board	Board	UAPP Board
Control over benefit levels:									
Province	Y	Y	-	-	-	-	-		-
Employee sponsors	Y	Y	-	-	-	-	-	Unclear	-
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board	LAPP Board	PSP Board	MEPP Board		UAPP Board
Notes									
					(relate to post-1992 obligations only; pre-1992 obligations are under special arrangements/old plan)				
					Alberta College of Art and Design reports its share on a DC basis for its audited financial statement			50/50 cost sharing; contributions rates are set by board to account for any new deficiency	The plan ceased to be a statutory plan under the PPPA in 2001 and since registered under EPPA
Legal sponsors									
Province (directly)	ON	ON	n/a	n/a				AB	n/a
Other Employers	n/a	n/a	CEC	OHA	Various participating employers, not including the Government of Alberta	Various participating employers, including the Government of Alberta	Various participating employers, including the Government of Alberta	Other private schools participating employers)	Governors of universities (5 parties)
Employees	OTF	OPSEU	OPSEU, OCASA	ONA, CUPE, OPSEU, SEIU	n/a	n/a	n/a	Alberta Teachers' Association	Academic Staff Associations

Public Pension Plans Comparison

Province	Ontario				Manitoba					Saskatchewan
Plan	**OTPP**	**OPSEUPP**	**CAAT**	**HOOPP**	**CSSP**	**TPP**	**UMPP**	**UWPP**	**BURP**	**SHEPP**
Is the Plan reported as a joint defined benefit plan?	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Is an obligation reported?	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Is the plan in an asset position, prior to valuation allowance?	Y	Y	Y	Y	N	N	n/a	n/a	n/a	
Is the asset impaired?	N	N	Y	Y	N	N	n/a	n/a	n/a	
Control over contributions levels:										
Province	Y	Y	-	-						
Employee sponsors	Y	Y	-	-						
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board						
Control over benefit levels:										
Province	Y	Y	-	-						
Employee sponsors	Y	Y	-	-						
Plan boards / other parties	-	-	Sponsor's committee	HOOPP Board						
Notes										
							report in aggreage as "post-secondary education plans" for province's financial statement			
Legal sponsors										
Province (directly)	ON	ON	n/a	n/a						
Other Employers	n/a	n/a	CEC	OHA						
Employees	OTF	OPSEU	OPSEU, OCASA	ONA, CUPE, OPSEU, SEIU						

minister request.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: minister request
Date: Friday, October 21, 2016 17:00:17

Lucy,

The minister has asked for a flow chart to help explain to the public in easy to follow presentation (flowchart?) how the AG's approach to determining pension expense impacts the fiscal plan. Specifically, he would like to be able to explain how a pension surplus becomes a pension expense because of the AG's different interpretation.

Apparently this is an urgent request that we have to complete by end of weekend. Wondering if you have any ideas or can help? Maybe you have something off the shelf? Not great odds I guess.

Thanks.

Nadine

miscellanous (Pension Asset Ceiling).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: miscellanous (Pension Asset Ceiling)
Date: Friday, September 16, 2016 21:46:52
Attachment 1: image001.png
Attachment 2: image002.png
Attachment 3: Financial Statements 2000.pdf
Attachment 4: Pension Discount Rate Analysis for AG.xlsx
Attachment 5: Summary (overview) to pwc sept 16.docx
Attachment 6: Scanned from a Xerox multifunction device.pdf

Hi Lucy.

Just sending along additional items related to the pension file.

1) Notes below regarding Province's perspective (see below), including an overview attachment

2) Copy of the AG's issues note reflecting her position

3) Copy of government partnership guidance (PS 3060)which may have applicability to JSPPs like the situation involving OTF

I think that will be all for now w.r.t. materials. Thanks. Nadine

From the Province's perspective…

The Province continues to believe that the assets are appropriately stated in accordance with PSAB for the following reasons:

· The assets result from the excess of the contributions and asset returns over the projected benefit obligations. Given there have been no issues raised with respect to either the contributions or the asset returns, our analysis focuses on the impact of the projected benefit obligation.

· The project benefit obligation has been estimated using a discount rate based on the expected return on assets as permitted by PSAB (see paragraph .44 below). That method has been consistently applied by the Province since at least 2000.

· OTPP also used a discount rate based on the expected return on assets until 1999, at which point it changed its policy to use a rate based on high yield corporate bonds. We have attached the OTPP's year 2000 financial statements for ease of reference.

PS3250

.042 *Actuarial assumptions should be based on the government's best estimates of expected long-term experience and short-term forecasts.* [SEPT. 2001]

.043 One commonly used approach that meets this standard is the use of streamed rate assumptions. Under the streamed rate approach, the short-term forecast of fund asset earnings, for example, would reflect the rates of return that assets currently held in the fund will earn until their maturity. As those assets mature, assumptions about their expected earnings on reinvestment would move to the expected long-term rate. Similarly, there would be streamed rate assumptions for salary increases.

.020 The retirement benefits interest expense is the net of:

(a) the interest cost on the accrued benefit obligation determined by applying the discount rate determined at the beginning of the period in accordance with paragraph PS 3250.044 to the average value of the accrued benefit obligation for the period; and

(b) the expected return on plan assets for a defined benefit plan, determined by applying the assumed rate of return on plan assets to the average market-related value of assets for the period.

.044 The actuarial assumptions underlying the valuation of the retirement benefit liability and expense would be internally consistent. For example, **when a government determines its discount rates by reference to its plan asset earnings, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the short-term forecast of rates of return**

on assets currently held in the fund. When a government determines its discount rates by reference to its cost of borrowing, the assumptions used to determine the short-term forecast incorporated in the discount rates would be consistent with the specific rates of interest and the periods committed to by the government on the amounts borrowed.

· Though 3250.044 indicates one option is to use discount rates by reference to the cost of borrowing, based on our jurisdictional scan of the other provinces' financial statements, we have not found any jurisdictions that use the government borrowing rate to value their pension obligations for plans that are funded by plan assets.

· We have included our analysis for your reference.

OTTP

OTTP prepares its financial statements in accordance with Part IV of the CPA Handbook. Section 4600 in part IV provides guidance on accounting for investments and pension obligations. For all other items, a pension plan chooses to follow IFRS or ASPE. OTTP has chosen to follow IFRS.

For the recording of the pension obligation, the guidance in Section 4600 is as follows:

22 *A pension plan shall measure the pension obligation required by paragraph* 4600.12*(g) in accordance with paragraph* 4600.05*(v). For this purpose,* ***a pension plan may measure the pension obligation at the defined benefit obligation amount determined by the plan's sponsor.***

.23 Guidance on determining the defined benefit obligation can be found in EMPLOYEE FUTURE BENEFITS, Section 3462, in Part II of the Handbook, and in IAS 19 *Employee Benefits* in Part I of the Handbook.

4600.12(g) is the requirement to distinguish the pension obligation in the statement of

financial position and 4600.05(v) is the definition of a pension obligation of a defined benefit pension plan, which states the following, “A pension obligation of a defined benefit pension plan is the actuarial present value of accrued pension benefits determined by applying best estimate assumptions and the projected benefit method prorated on services.”

As noted, pension plans have a considerable amount of choice in determining how to account for their pension obligations – the amount as determined by the plan sponsor, using the guidance in ASPE, or using the guidance in IFRS.

OTTP has chosen to use the guidance in IFRS (IAS 19) and includes the following in its financial statements (December 2015 year end):

“The discount rate is based on market rates, as at the valuation date, of bonds issued by the Province

of Ontario, which have characteristics similar to the Plan’s liabilities. The discount rate was determined by applying a weighted average discount rate that reflects the estimated timing and amount of benefit payments. The inflation rate is the geometric difference between the yield on Government of Canada long-term nominal bonds and Government of Canada real-return bonds. The salary escalation rate incorporates the inflation rate assumption and long-term expectation of growth in real wages”.

We have included the guidance in from IAS 19 below for comparison:

<u>IAS 19</u>

83 The rate used to discount post-employment benefit obligations (both funded and

unfunded) shall be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. For currencies for which there is no deep market in such high quality corporate bonds, the market yields (at the end of the reporting period) on government bonds denominated in that currency shall be used. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations.

86 In some cases, there may be no deep market in bonds with a sufficiently long maturity to match the estimated maturity of all the benefit payments. In such cases, an entity uses current market rates of the appropriate term to discount shorter-term payments, and estimates the discount rate for longer maturities by extrapolating current market rates along the yield curve. The total present value of a defined benefit obligation is unlikely to be particularly sensitive to the discount rate applied to the portion of benefits that is payable beyond the final maturity of the available corporate or government bonds.

· OTTP is an outlier in using a discount rate based on the guidance in IAS 19 based on our review of the stand-alone financial statements of the provincially sponsored plans. We have attached our preliminary analysis (see above).

· With regards to any perception that the reported asset might be “fictitious”, we point out that the funding valuations completed by OTTP and submitted to FSCO have also demonstrate that the plan is overfunded. Based on the guidance provided to the members of the plan on the OTTP’s website, the surplus in the plan at March 31, 2016 (at 100%) is $13.1 billion. The difference between the $10 billion asset and the 50% of the $13.1 billion, or $6.5 billion is primarily based on the discount rate used. The preparation of the funding valuation is based on prescribed requirement and is not an accounting valuation. Nonetheless, it speaks to the fact that the plan, on a funding basis, has a surplus.

In summary, we don’t believe that an adjustment is warranted to the reported pension asset on the CFS on the basis that:

· The discount rates used to value the projected benefit obligation are consistent with the requirements of PSAB.

· The AG has reviewed the discount rate each year and based on the understanding of those involved in the current year and historically, has never raised a concern with the rates used.

· The asset recorded on the pension’s books is not fictitious and is supported by the OTPP’s own calculations and public disclosures.

image001.pdf

PDF

image002.pdf

Pension Discount Rate Analysis for AG.

Financial Statements 2000.pdf

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of the Ontario Teachers' Pension Plan have been prepared by management, which is responsible for the integrity and fairness of the data presented, including the many amounts which must, of necessity, be based on estimates and judgements. The accounting policies followed in the preparation of these consolidated financial statements conform with Canadian generally accepted accounting principles. Financial information presented throughout the annual report is consistent with the consolidated financial statements.

Systems of internal control and supporting procedures are maintained to provide assurance that transactions are authorized, assets are safeguarded and proper records maintained. These controls include quality standards in hiring and training of employees, a code of conduct, the establishment of an organizational structure that provides a well-defined division of responsibilities and accountability for performance, and the communication of policies and guidelines through the organization. Internal controls are reviewed and evaluated by internal audit programs which are subject to scrutiny by the external auditors.

Ultimate responsibility for the consolidated financial statements rests with the Board of Directors. The board is assisted in its responsibilities by the Audit and Actuarial Committee, consisting of five directors who are not officers or employees of the plan administrator. In addition, the committee reviews the recommendations of the internal and external auditors for improvements in internal control and the action of management to implement such recommendations. In carrying out its duties and responsibilities, the committee meets regularly with management and with both the external and internal auditors to review the scope and timing of their respective audits, to review their findings and to satisfy itself that their responsibilities have been properly discharged. This committee reviews the consolidated financial statements and recommends them for approval by the board.

The plan's external auditors, Deloitte & Touche LLP, have conducted an independent examination of the consolidated financial statements in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary to express the opinion in their Report to the Administrator. The external auditors have full and unrestricted access to the Audit and Actuarial Committee to discuss their audit and related findings as to the integrity of the plan's financial reporting and the adequacy of internal control systems.

CLAUDE LAMOUREUX
PRESIDENT AND CHIEF EXECUTIVE OFFICER

ANDREW JONES
VICE-PRESIDENT, FINANCE

FEBRUARY 14, 2001

AUDITORS' REPORT TO THE ADMINISTRATOR

We have audited the consolidated statement of net assets available for benefits and accrued pension benefits and surplus of the Ontario Teachers' Pension Plan as at December 31, 2000 and the consolidated statements of changes in net assets available for benefits, changes in accrued pension benefits and changes in surplus for the year then ended. These consolidated financial statements are the responsibility of the Plan's administrator. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the net assets available for benefits and accrued pension benefits and surplus of the Plan as at December 31, 2000 and the changes in its net assets available for benefits, changes in accrued pension benefits and changes in surplus for the year then ended in accordance with Canadian generally accepted accounting principles.

CHARTERED ACCOUNTANTS
TORONTO, CANADA

FEBRUARY 14, 2001

ACTUARIES' OPINION

William M. Mercer Limited was retained by the Ontario Teachers' Pension Plan Board (the "Board") to perform an actuarial valuation of the assets and the going concern liabilities of the Ontario Teachers' Pension Plan (the "Plan") as at December 31, 2000, for inclusion in the Plan's consolidated financial statements. As part of the valuation, we examined the Plan's recent experience with respect to the non-economic assumptions and presented our findings to the Board.

The valuation of the Plan's actuarial liabilities was based on:

- membership data provided by the Ontario Teachers' Pension Plan Board as at December 31, 1999;
- methods prescribed by the Canadian Institute of Chartered Accountants for pension plan financial statements;
- real and nominal interest rates on long term Canada bonds at the end of 2000;
- assumptions about future events (for example, future rates of inflation and future retirement rates) which have been communicated to us as the Board's best estimate of these events;
- information obtained from the Ontario Ministry of Labour and published reports on negotiated wage settlements in the 1999/2000 and 2000/01 school years; and
- an estimate of the salary grid increase for the 2000/01 school year based on the information above, along with input from the Partners.

The objective of the consolidated financial statements is to fairly present the financial position of the Plan on December 31, 2000 as a going concern. This is different from the statutory valuation [the actuarial valuation required by the *Teachers' Pension Act* and the *Pension Benefits Act [Ontario]*], which uses actuarial methods prescribed by the *Teachers' Pension Act* and cautious assumptions about future events to establish a prudent level for future contributions.

While the actuarial assumptions used to estimate liabilities for the Plan's consolidated financial statements represent the Board's best estimate of future events and market conditions at the end of 2000, and while in our opinion these assumptions are reasonable, the Plan's future experience will inevitably differ, perhaps significantly, from the actuarial assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations, and will affect the financial position of the Plan, and the contributions required to fund it, at that time.

We have tested the data for reasonableness and consistency, and we believe it to be sufficient and reliable for the purposes of the valuation. We also believe that the methods employed in the valuation and the assumptions are, in aggregate, appropriate for the purposes of the valuation. Our opinions have been given, and our valuation has been performed, in accordance with accepted actuarial practice.

LESTER J. WONG, F.C.I.A.

MALCOLM P. HAMILTON, F.C.I.A.

FEBRUARY 14, 2001

CONSOLIDATED STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED PENSION BENEFITS AND SURPLUS

AS AT DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
NET ASSETS AVAILABLE FOR BENEFITS		
Assets		
Investments (note 3)	**$85,117**	$73,872
Receivable from the Province of Ontario (note 4)	**1,251**	1,252
Receivable from brokers	**37**	210
Cash	**40**	42
Fixed assets	**8**	8
	86,453	75,384
Liabilities		
Investment-related liabilities (note 3a)	**13,074**	6,780
Due to brokers	**166**	230
Accounts payable and accrued liabilities	**92**	71
	13,332	7,081
Net assets available for benefits	**73,121**	68,303
Actuarial asset value adjustment (note 1e)	**(4,341)**	(8,316)
Actuarial value of net assets available for benefits	**$68,780**	$59,987
ACCRUED PENSION BENEFITS AND SURPLUS		
Accrued pension benefits (note 5)	**$58,556**	$52,105
Surplus	**10,224**	7,882
Accrued pension benefits and surplus	**$68,780**	$59,987

ON BEHALF OF THE BOARD

CHAIR

BOARD MEMBER

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999
Net assets available for benefits, beginning of year	**$68,303**	$59,171
Investment operations		
Investment income (note 7)	**6,211**	10,121
Investment expenses (note 12a)	**(100)**	(91)
Net investment operations	**6,111**	10,030
Member service operations		
Contributions (note 10)	**1,281**	1,413
Benefits (note 11)	**(2,541)**	(2,278)
Member service expenses (note 12b)	**(33)**	(33)
Net member service operations	**(1,293)**	(898)
Increase in net assets	**4,818**	9,132
Net assets available for benefits, end of year	**$73,121**	$68,303

CONSOLIDATED STATEMENT OF CHANGES IN ACCRUED PENSION BENEFITS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
Accrued pension benefits, beginning of year	**$52,105**	$49,626
Increase in accrued pension benefits		
Interest on accrued pension benefits	**3,478**	3,493
Benefits accrued	**1,359**	1,301
Changes in actuarial assumptions (note 5a)	**3,893**	766
	8,730	5,560
Decrease in accrued pension benefits		
Benefits paid (note 11)	**2,541**	2,278
Experience (losses) gains (note 5b)	**(262)**	803
	2,279	3,081
Net increase in accrued pension benefits	**6,451**	2,479
Accrued pension benefits, end of year	**$58,556**	$52,105

CONSOLIDATED STATEMENT OF CHANGES IN SURPLUS

FOR THE YEAR ENDED DECEMBER 31, 2000

($ Millions)	**2000**	1999 restated (note 2)
Surplus, beginning of year	**$7,882**	$4,381
Increase in net assets available for benefits	**4,818**	9,132
Change in actuarial asset value adjustment (note 1e)	**3,975**	(3,152)
Increase in actuarial value of net assets available for benefits	**8,793**	5,980
Net increase in accrued pension benefits	**(6,451)**	(2,479)
Surplus, end of year	**$10,224**	$7,882

FOR THE YEAR ENDED DECEMBER 31, 2000

DESCRIPTION OF PLAN

The following description of the Ontario Teachers' Pension Plan (the Plan) is a summary only. For more complete information, reference should be made to the *Teachers' Pension Act* (the TPA) as amended.

(a) General The Plan is governed by the TPA. It is a contributory defined benefit pension plan co-sponsored by the Partners who are the Province of Ontario (the Province) and Plan members, represented by the Ontario Teachers' Federation (the OTF). The terms of the Plan are set out in the *Partners' Agreement.*

The Plan is registered with the Financial Services Commission of Ontario and with the *Income Tax Act (Canada)* (registration number 0345785) as a Registered Pension Plan not subject to income taxes.

The Plan is administered and the investments are managed by the Ontario Teachers' Pension Plan Board (the Board). Under the TPA, the Board is constituted as a corporation without share capital to which the *Corporations Act (Ontario)* does not apply.

(b) Funding Plan benefits are funded by contributions and investment earnings. Contributions are made by active members of the Plan and matched by the Province and designated private schools and organizations. The determination of the value of the benefits and required contributions is made on the basis of periodic actuarial valuations (note 9).

(c) Retirement pensions A retirement pension is available based on the number of years of credited service, the average of the best five annual salaries and the age of the member at retirement. A member is eligible for a reduced retirement pension from age 55. An unreduced retirement pension is available at age 65 or at any age if the member has 35 years' credit or if the sum of a member's age and qualifying service equals 90. An early retirement window covering the period between June 1, 1998 and December 31, 2002 is currently provided, during which time a member can retire with an unreduced pension if the sum of the member's age and qualifying service equals 85 rather than 90.

(d) Disability pensions A disability pension is available at any age to a disabled member with a minimum of 10 years of credited service. The type of disability pension is determined by the extent of the disability.

(e) Death benefits Death benefits are available on the death of an active member and may be available on the death of a retired member. The benefit may take the form of a survivor pension, lump sum payment or both.

(f) Escalation of benefits Pension benefits are adjusted annually for inflation at 100 percent of the Consumer Price Index, subject to a limit of 8 percent in any one year with any excess carried forward.

(g) Retirement Compensation Arrangement The Retirement Compensation Arrangement (RCA) has been created by agreement between the Partners as a supplementary plan to provide the members of the Plan with benefits that, due to limitations imposed by the *Income Tax Act (Canada)* and its regulations, cannot be provided under the Registered Pension Plan. Because the RCA is a separate trust, the net assets available for benefits and accrued benefits of the RCA are not included in these financial statements (note 13).

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

These financial statements present the financial position and the results of operations of the Plan and are prepared in accordance with Canadian generally accepted accounting principles.

The financial statements of wholly-owned subsidiary companies are consolidated as part of the Plan's financial statements.

Certain comparative figures have been reclassified to conform with the current year's presentation.

(b) Investments and investment-related assets and liabilities

Fair Value Investments and investment-related assets and liabilities are stated at fair value. Fair value is an estimate of the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Where ascertainable, fair values are based on public market prices or quotations from investment dealers. Where public market prices or quotations are not ascertainable, fair values are derived using methods such as discounted cash flows, earnings multiples, appraisals, prevailing market rates for instruments with similar characteristics and other pricing models, as appropriate.

Trade date reporting Purchases and sales of investments and derivative contracts are recorded as of the trade date (the date upon which the substantial risks and rewards have been transferred).

Investment income Dividend income is recognized based on ex-dividend date and interest income and real estate operating income is recognized on the accrual basis as earned. Investment income also includes realized and unrealized gains and losses.

(c) Foreign currency translation

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rates prevailing on the year-end date. Income and expenses are translated into Canadian dollars at the exchange rates prevailing on the dates of the transactions. The realized and unrealized gains and losses arising from these translations are included in investment income.

(d) Accrued pension benefits

The value of accrued pension benefits and changes therein during the year are based on an actuarial valuation prepared by an independent firm of actuaries. The valuation is made as at the start of the year and then extrapolated to year-end. It uses the projected benefit method prorated on service and management's best estimate, as at valuation date, of various economic and non-economic assumptions (note 5).

(e) Actuarial asset value adjustment

The actuarial value of net assets available for benefits is determined by reference to market trends consistent with assumptions underlying the valuation of accrued pension benefits. The adjustment represents the difference between the actual and management's best estimate of return on the Plan's equity investments (including real estate and commodities) amortized over five years. Fixed income securities are valued at fair value on a basis consistent with the discount rate used to value the Plan's accrued pension benefits.

The year-over-year change in the actuarial asset value adjustment is reflected in the Consolidated Statement of Changes in Surplus.

(f) Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions that primarily affect the reported values of assets and liabilities, related income and expenses and related disclosures.

2. CHANGES IN ACCOUNTING POLICY– ACCRUED PENSION BENEFITS

Consistent with a new Canadian Institute of Chartered Accountants standard on Employee Future Benefits, the Board changed its method of determining the best estimate assumptions used in valuing the accrued pension benefits. The Board now uses a market interest rate to discount the accrued pension benefits, in order to arrive at the fair value of the Plan's liabilities. In prior years, the Board used a rate which reflected management's best estimate of the expected long-term asset rate of return.

With this change to the determination of the discount rate, the method for calculating the actuarial asset value adjustment has also been modified. In prior years, the adjustment represented the difference between the actual and management's best estimate of return on all Plan assets, amortized over five years. The actuarial asset value now values fixed income securities at fair value, consistent with the measurement of the Plan's liabilities at fair value. For the Plan's equity investments, an actuarial asset value adjustment is calculated as the difference between the actual and management's best estimate of return on the Plan's equity assets, amortized over five years.

The changes in accounting policy referred to above have been applied retroactively in the financial statements and have the following impact on 1999 figures previously reported:

($ Millions)	1999 Reported	1999 Restated
Net assets available for benefits	$68,303	$68,303
Actuarial asset value adjustment	(7,264)	(8,316)
Actuarial value of net assets available for benefits	$61,039	$59,987
Accrued pension benefits – opening	$48,636	$49,626
Changes during the year	3,469	2,479
Accrued pension benefits – closing	52,105	52,105
Surplus, beginning of year	5,747	4,381
Increase in net assets available for benefits	9,132	9,132
Change in actuarial asset value adjustment (note 1e)	(2,476)	(3,152)
Increase in actuarial value of assets available for benefits	6,656	5,980
Net increase in accrued pension benefits	(3,469)	(2,479)
Surplus, end of year	8,934	7,882
Accrued benefits and surplus	$61,039	$59,987

3. INVESTMENTS

The Plan invests directly or through derivatives in fixed income, equities and inflation-sensitive investments in accordance with its policy of asset diversification. The purpose of such diversification is to minimize the likelihood of an overall reduction in surplus and maximize the opportunity for gains across the investment portfolio.

(a) Investments[1] before allocating the effect of derivative contracts and investment-related receivables and liabilities

The schedule below summarizes the Plan's investments, including net accrued interest and dividends of $388 million (1999 – $454 million), before allocating the effect of derivative contracts and investment-related receivables and liabilities, as at December 31:

($ Millions)	2000		1999	
	Fair Value	**Cost**	Fair Value	Cost
Fixed income				
Debentures	**$15,715**	**$12,205**	$16,328	$12,991
Bonds	**13,218**	**12,696**	13,303	13,198
Money market securities	**4,273**	**4,238**	2,153	2,153
Alternative investments[2]	**2,162**	**1,720**	1,326	1,166
	35,368	**30,859**	33,110	29,508
Equities				
Publicly traded				
Canadian	**13,487**	**9,618**	17,125	11,195
United States	**1,885**	**1,565**	516	559
Non–North American	**6,415**	**5,455**	8,149	5,591
Non–Publicly traded				
Canadian	**1,110**	**856**	464	446
United States	**769**	**671**	699	510
Non–North American	**1,196**	**1,188**	984	852
	24,862	**19,353**	27,937	19,153
Inflation-sensitive investments				
Real estate (note 6)	**10,393**	**9,711**	3,508	3,220
Real rate products				
Canadian	**5,822**	**5,054**	4,656	4,349
United States	**4,424**	**4,190**	391	404
	20,639	**18,955**	8,555	7,973
	80,869	**69,167**	69,602	56,634
Investment-related receivables				
Securities purchased under agreements to resell	**1,948**	**1,946**	992	990
Derivative-related, net	**2,300**	**493**	3,278	409
Investments	**85,117**	**71,606**	73,872	58,033
Investment-related liabilities				
Securities sold under agreements to repurchase	**(3,578)**	**(3,572)**	(2,883)	(2,879)
Securities sold but not yet purchased	**(1,592)**	**(1,606)**	(973)	(992)
Real estate (note 6)	**(4,192)**	**(4,002)**	(693)	(710)
Derivative-related, net	**(3,712)**	**(1,199)**	(2,231)	(2,294)
Net investments (note 3c)	**$72,043**	**$61,227**	$67,092	$51,158

(1) For additional details, refer to the Schedule of Investments for our holdings over $50 million on page 45.

(2) Comprised of hedge funds, managed futures accounts and fund of funds programs.

(b) Derivative contracts

Derivative contracts are financial contracts, the value of which is derived from the value of underlying assets, indices, interest rates or currency rates. Derivative contracts are transacted either in the over-the-counter market or on regulated exchanges. The Plan utilizes derivatives to manage its asset mix, as well as its exposure to interest rates, foreign currencies, and credit. Derivatives are also utilized for trading purposes in a manner consistent with the Plan's investment objectives.

Notional amounts of derivative contracts serve as the basis upon which the returns from, and the fair value of, the contracts are determined.

The following schedule summarizes the Plan's derivative contracts as at December 31:

($ Millions)	**2000**		1999	
	Notional	**Fair Value**	Notional	Fair Value
Asset conversion				
Interest rate swaps	**$6,353**	**$(933)**	$ 6,091	$(763)
Equity and commodity swaps	**17,436**	**(215)**	13,719	3,257
		(1,148)		2,494
Interest rate management				
Interest rate swaps	**1,330**	**4**	1,104	1
Futures	**6,962**	**(1)**	4,238	(1)
Exchange traded options				
Purchased	**2,509**	**5**	3,041	4
Written	**2,644**	**(4)**	3,771	(4)
Over-the-counter options				
Purchased	**40**	**1**	97	3
Written	**100**	**(1)**	169	(4)
		4		(1)
Foreign currency management				
Currency swaps	**499**	**(10)**	553	10
Forwards	**13,347**	**24**	13,567	343
Futures	**708**	**1**	—	—
		15		353
Trading				
Interest rate swaps	**2,427**	**(7)**	2,836	28
Volatility swaps	**967**	**34**	66	1
Futures	**18,484**	**(17)**	13,715	(161)
Forwards	**5,899**	**175**	3,791	53
Exchange traded options				
Purchased	**454**	**14**	313	22
Written	**816**	**(5)**	441	(32)
Over-the-counter options				
Purchased	**1,964**	**38**	2,062	43
Written	**1,153**	**(22)**	1,042	(19)
		210		(65)
		(919)		2,781
Less: Net cash collateral received under derivative contracts		**(493)**		(1,734)
Net fair value of derivative contracts		**$(1,412)**		$1,047

The net fair value of derivative contracts as at December 31 on page 33 are represented by:

($ Millions)	**2000**	1999
Derivative-related receivables	**$2,562**	$4,755
Cash collateral paid under derivative contracts	**428**	324
Derivative-related liabilities	**(3,481)**	(1,974)
Cash collateral received under derivative contracts	**(921)**	(2,058)
	$(1,412)	$1,047

Securities with a fair value of $320 million (1999 – $246 million) have been deposited with various financial institutions as margin to effect derivatives transactions.

The derivative contracts on page 33 mature within one year except for the following, which have a weighted average maturity (in years) of:

	2000		1999	
	Notional *($ millions)*	**Maturity *(years)***	Notional *($ millions)*	Maturity *(years)*
Asset conversion				
Interest rate swaps	**$6,119**	**8.4**	$5,487	6.6
Equity and commodity swaps	**2,468**	**1.4**	5,155	1.6
Interest rate management				
Interest rate swaps	**1,004**	**8.2**	993	4.4
Over-the-counter options	**140**	**1.9**	—	—
Foreign currency management				
Currency swaps	**493**	**5.7**	553	7.1
Forwards	**182**	**1.5**	57	2.2
Trading				
Interest rate swaps	**2,155**	**5.1**	2,536	5.1
Volatility swaps	**221**	**3.2**	66	3.1
Over-the-counter options	**83**	**1.6**	102	2.1
Forwards	**23**	**1.4**	—	—

(c) Investment asset mix

The Plan has established a long-term asset-mix policy of approximately 60 percent equities, 18 percent fixed income and 22 percent inflation-sensitive investments.

The Plan's investments, after allocating the effect of derivative contracts and investment-related receivables and liabilities, as at December 31 are summarized below:

	2000		1999	
	Effective Net Investments at Fair Value *($ millions)*	**Asset Mix *%***	Effective Net Investments at Fair Value *($ millions)*	Asset Mix *%*
Fixed income				
Bonds	**$10,771**	**15%**	$14,926	22%
Money market and equivalents	**2,548**	**3**	2,378	4
	13,319	**18**	17,304	26
Equities				
Canadian	**17,739**	**25**	19,885	30
United States	**10,119**	**14**	8,191	12
Non–North American	**13,022**	**18**	13,568	20
	40,880	**57**	41,644	62
Inflation-sensitive investments				
Commodities	**2,098**	**3**	1,090	2
Real estate (note 6)	**6,201**	**9**	2,815	4
Real rate products	**9,545**	**13**	4,239	6
	17,844	**25**	8,144	12
Total net investments	**$72,043**	**100%**	$67,092	100%

(d) Interest rate risk

The value of the Plan's assets is affected by short-term changes in nominal interest rates and equity markets. Pension liabilities are exposed to long-term market interest rates as well as expectations for salary escalation.

The Plan's primary exposure is to a decline in the long-term real rate of return which may result in higher contribution rates required to meet pension obligations. As at December 31, 2000, holding the inflation and salary escalation assumptions constant, a 1 percent decrease in the assumed real long-term rates of return would result in an increase in the pension liabilities of approximately 13 percent (1999 – 16 percent).

After giving effect to the derivative contracts and investment-related receivables and liabilities discussed in note 3b, a 1 percent increase in nominal interest rates would result in a decline in the value of the fixed income securities of 6.6 percent (1999 – 7.7 percent).

(e) Credit risk

At December 31, 2000, the Plan's most significant concentration of credit risk is with the Government of Canada and the Province of Ontario. This concentration relates primarily to the holding of $14.5 billion of Government of Canada-issued securities and $15.7 billion of non-marketable Province of Ontario Debentures, a receivable from the Province of $1.3 billion and future provincial funding requirements of the Plan.

The Plan limits derivative contract credit risk by dealing principally with counterparties that have a credit rating of A or higher, and by utilizing an internal credit limit monitoring process, as well as through the use of credit mitigation techniques such as master netting arrangements and obtaining collateral where appropriate.

(f) Foreign currency risk

Foreign currency exposure arises from the Plan's holdings of foreign currency-denominated investments and related derivative contracts.

The Plan uses a currency overlay program to hedge a portion of its asset-mix policy allocation to U.S. and Non-North American equities. The Plan also takes trading positions in foreign currencies with the objective of adding incremental returns. The Plan's net foreign currency exposure in Canadian dollars after giving effect to the related policy hedge, as at December 31, is as follows:

($ Millions)	**2000**			1999
	Foreign Currency Exposure	**Net Foreign Currency Hedge**	**Net Foreign Currency Exposure**	Net Foreign Currency Exposure
United States Dollar	**$12,021**	**$5,389**	**$6,632**	$4,854
Euro	**5,920**	**2,528**	**3,392**	2,245
British Pound Sterling	**3,370**	**1,405**	**1,965**	1,537
Swiss Franc	**1,561**	**483**	**1,078**	252
Japanese Yen	**2,489**	**1,774**	**715**	1,280
Other	**2,165**	**187**	**1,978**	1,532
	$27,526	**$11,766**	**$15,760**	$11,700

(g) Securities lending

The Plan lends securities as a means of generating incremental income or supporting other investment strategies. As at December 31, 2000, the Plan's investments included loaned securities with a fair value of $3,402 million (1999 – $3,280 million). The fair value of collateral in respect of these loans was $3,590 million (1999 – $3,444 million).

4. RECEIVABLE FROM THE PROVINCE OF ONTARIO

The receivable from the Province consists of required matching contributions and interest thereon.

($ Millions)	**2000**	1999
Contributions receivable	**$1,194**	$1,194
Accrued interest receivable	**57**	58
	$1,251	$1,252

The receivable from the Province consists of $636 million to be received in 2001 and $615 million to be received in 2002.

5. ACCRUED PENSION BENEFITS

(a) Actuarial assumptions

The actuarial assumptions used in determining the value of accrued pension benefits of $58.6 billion (1999 – $52.1 billion), reflect management's best estimate of future economic events and involve both economic and non-economic assumptions. The non-economic assumptions include considerations such as mortality, withdrawal rates and retirement rates. The primary economic assumptions include the discount rate, salary escalation rate and the inflation rate. As discussed in note 2, the discount rate is now set at the market rate, as at the valuation date, of debt obligations with characteristics similar to the Plan's liabilities. The inflation rate is the difference between the yield on federal long-term nominal bonds and federal real return bonds. The salary escalation rate incorporates the inflation rate assumption and long-term expectation of growth in real wages. A summary of the primary economic assumptions, as at December 31, is as follows:

	2000	1999
Discount rate	**6.25%**	6.75%
Salary escalation rate	**3.20%**	3.25%
Inflation rate	**2.20%**	2.25%

The main economic assumptions were changed as a result of changes in capital markets during 2000. These changes resulted in a net increase in the value of accrued pension benefits of $3,297 million. In addition, a change was made to the assumed post-retirement mortality rates to better reflect the Plan's experience. This change increased the value of accrued pension benefits by a further $596 million. In 1999, changes to the actuarial assumptions resulted in a net increase in the value of accrued pension benefits of $766 million.

(b) Experience gains and losses

An experience loss of $262 million (1999 – gain of $803 million), arising from differences between the actuarial method and assumptions and actual results, relates primarily to current experience for members' salary and inflation rates.

6. INVESTMENT IN REAL ESTATE

(a) Acquisition of Cadillac Fairview Corporation ("CFC")

On March 17, 2000, pursuant to a plan of arrangement, the Plan acquired the remaining 78.2 percent of the common shares that it did not previously own of CFC, a fully integrated commercial real estate operating company, and $100 million of CFC convertible debentures for total consideration of $2,355 million.

The fair value of CFC's net assets acquired is summarized below:

($ Millions)	
Real estate properties	$5,730
Other assets	403
	6,133
Debt on real estate properties	(2,892)
Other liabilities	(324)
Net assets of CFC	2,917
Less: Investment in CFC previously held	(562)
Total consideration	**$2,355**

(b) Investment in Real Estate

The Plan's investment in real estate, which is comprised of real estate–related investments that are either owned or managed on behalf of the Plan by The Cadillac Fairview Corporation Limited, as at December 31, is as follows:

($ Millions)	**2000**		1999	
	Fair Value	**Cost**	Fair Value	Cost
Assets				
Real estate properties	**$9,635**	**$8,901**	$2,454	$2,411
Investments	**526**	**577**	485	498
Other assets	**232**	**233**	7	7
Investment in CFC	**—**	**—**	562	304
Total assets	**10,393**	**9,711**	3,508	3,220
Liabilities				
Debt on real estate properties	**3,833**	**3,694**	693	710
Other liabilities	**359**	**308**	—	—
Total liabilities	**4,192**	**4,002**	693	710
Net investment in real estate	**$6,201**	**$5,709**	$2,815	$2,510

(c) Real Estate Income[1]

The Plan's real estate income for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Revenue		
Rental	**$1,140**	$263
Investment	**41**	24
	1,181	287
Expenses		
Property operating	**447**	101
Interest	**242**	41
Management	**42**	7
Other	**23**	—
	754	149
Operating income	**427**	138
Realized gain (loss)	**14**	(16)
Unrealized gain	**187**	190
Net income	**$628**	$312

(1) Operating income, on a fair value basis, excludes a charge for depreciation and amortization.

7. INVESTMENT INCOME

(a) Investment income, before allocating the effect of derivative contracts

Investment income, before allocating the effect of derivative contracts and before allocating the realized and unrealized net gains/losses, for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Fixed income interest		
Debentures (net of interest incurred on swap contracts of $1,039 million; 1999 – $753 million)	**$386**	$762
Money market securities	**197**	104
Bonds	**720**	633
	1,303	1,499
Equity dividend income		
Canadian equity	**222**	271
United States equity	**13**	13
Non–North American equity	**234**	241
	469	525
Inflation-sensitive investments		
Real estate operating income (note 6c)	**427**	138
Real rate products interest income		
Canadian	**189**	152
United States	**92**	14
	708	304
	2,480	2,328
Net gain on investments [1]	**3,731**	7,793
	$6,211	$10,121

(1) Includes net unrealized gains (losses) of $(4,145) million (1999 – $1,075 million).

(b) Investment income

Investment income by asset class, after allocating the effect of the derivative contracts and net gains, including foreign currency losses of $71 million (1999 – $1,106 million gain), for the year ended December 31, is as follows:

($ Millions)	**2000**	1999
Fixed income	**$1,689**	$(347)
Canadian equity	**2,523**	4,475
United States equity	**316**	1,559
Non–North American equity	**(694)**	3,697
Inflation-sensitive investments	**2,377**	737
	$6,211	$10,121

8. INVESTMENT RETURNS AND RELATED BENCHMARK RETURNS

Investment returns and related benchmark returns by investment asset class for the year ended December 31 are as follows:

	2000		1999	
	Investment Returns	**Investment Benchmark Returns**	Investment Returns	Investment Benchmark Returns
Fixed income	**15.6%**	**13.7%**	2.0%	2.8%
Canadian equity	**13.5**	**7.4**	30.4	32.0
United States equity	**(4.1)**	**(5.5)**	12.7	14.1
Non–North American equity	**(8.5)**	**(13.5)**	27.7	21.6
Inflation-sensitive investments	**19.9**	**18.0**	12.0	9.8
Total Plan	**9.3%**	**5.3%**	17.4%	17.6%

Investment returns have been calculated in accordance with the acceptable methods set forth by the Association for Investment Management and Research and the Pension Investment Association of Canada.

The Plan identifies benchmarks to evaluate the performance of the investment management process. The performance of each asset class is measured against a benchmark that simulates the results of the markets in which the managers invest, except that the inflation-sensitive investments composite benchmark includes real estate which is measured against an inflation-related benchmark.

The total return of the Plan is measured against a Canadian dollar denominated composite benchmark produced by aggregating Canadian dollar equivalent returns from each of the policy asset class benchmarks, using the Plan's asset mix policy weights. The total return incorporates the Plan's tactical asset allocation decisions.

9. FUNDING POLICY

Statutory actuarial valuations are prepared periodically in accordance with the *Teachers' Pension Act* to determine the funding requirements of the Plan. Active members are currently required to contribute 7.3 percent of the portion of their salaries covered by the Canada Pension Plan and 8.9 percent of salaries above this level. Aggregate member contributions are matched by the Province and other employers.

The actuarial assumptions and methods used to determine statutory pension liabilities are different than those used to calculate the amounts disclosed in these financial statements. The statutory valuations use a more conservative approach than the valuations used in these financial statements (note 5) and also take into account benefits to be earned and contributions to be made after the valuation date.

The initial statutory valuation of the Plan, prepared by William M. Mercer Limited as at January 1, 1990 disclosed an unfunded liability of $7.8 billion which was the amount by which the Plan's liabilities exceeded its assets. This liability was the responsibility of the Province and was to be paid off with interest by a series of special payments over a 40 year period, which began January 1, 1990. Subsequent statutory valuations have treated the present value of the remaining special payments as an asset.

The statutory valuation as at January 1, 1998 disclosed the present value of special payments to be $8.45 billion, with an actuarial gain of $6.78 billion. Pursuant to the *Partners' Agreement* between the Ontario Teachers' Federation (OTF) and the Province, the Partners entered into negotiations to decide how to utilize the gain. Pursuant to the agreement reached on April 18, 1998, the Partners agreed to share the 1998 actuarial gain of $6.78 billion and future gains in the following sequence:

(i) $2.24 billion would be spent on improving benefits;
(ii) special payments on the pre-1990 unfunded liability would be eliminated at an estimated cost of $8.45 billion; and
(iii) a further $8.45 billion less the $2.24 billion would be spent on improved benefits or member contribution rate reductions, subject to the Province's consent prior to April 1, 2001; or held in a contingency reserve as determined by the OTF.

As a result, $2.24 billion of the gain was used to improve benefits under the Plan, and the remaining $4.54 billion of the gain was used to eliminate the obligation of the Province to make special payments after November 30, 2008. These changes consumed the actuarial gain. The present value of the remaining special payments after application of gains was $3.91 billion as at January 1, 1998.

The statutory valuation as at January 1, 1999 disclosed the present value of the remaining special payments to be $3.65 billion with an actuarial gain of $3.52 billion. Pursuant to the 1998 agreement noted above, all of this gain was used to eliminate the obligation of the Province to make special payments after April 1999.

The statutory valuation as at January 1, 2001 disclosed an actuarial gain of $6.78 billion (2000 – $4.54 billion).

10. CONTRIBUTIONS

($ Millions)	**2000**	1999
Members		
Current service	**$604**	$612
Optional credit	**11**	8
	615	620
Province of Ontario		
Current service	**601**	592
Interest	**42**	43
Optional credit	**5**	11
Special payments (note 9)	**—**	128
	648	774
Other employers	**9**	9
Transfer from other pension plans	**9**	10
	18	19
	$1,281	$1,413

11. BENEFITS

($ Millions)	**2000**	1999
Retirement pensions	**$2,215**	$2,016
Disability pensions	**31**	30
Death benefits	**102**	93
Refunds	**18**	16
Commuted value transfers	**164**	108
Transfers to other plans	**11**	15
	$2,541	$2,278

12. ADMINISTRATIVE EXPENSES

(a) Investment expenses

($ Millions)	**2000**	1999
Salaries and benefits	**$40.5**	$31.8
External investment management fees	**34.3**	34.8
Custodial fees	**6.6**	6.4
Premises and equipment	**6.6**	6.5
Professional consulting services	**5.0**	4.3
Information services	**3.7**	3.6
Communication and travel	**2.1**	1.8
Statutory audit fees	**0.3**	0.3
Other	**1.0**	1.1
	$100.1	**$90.6**

(b) Member service expenses

($ Millions)	**2000**	1999
Salaries and benefits	**$20.9**	$21.2
Premises and equipment	**6.2**	6.1
Professional and consulting services	**2.4**	2.2
Communication and travel	**2.1**	1.9
Board and committee remuneration	**0.2**	0.2
Statutory audit fees	**0.2**	0.2
Other	**0.7**	0.8
	$32.7	$32.6

(c) Executive compensation

The compensation table represents full disclosure of base salary, annual bonus, long-term incentives and other compensation earned in 1998, 1999 and 2000 by the Chief Executive Officer and the four other most highly compensated executives.

Name and Principal Position	Year	Base Salary	Annual Bonus[1]	Long-term Incentive Plan[3]	Group Term Life Insurance	Other Compensation
Claude Lamoureux	2000	$389,169	$504,500	$790,100	$1,119	$9,600[4]
President & CEO	1999	357,637	196,100	131,900	1,033	9,600
	1998	349,077	177,600	0	964	9,600
Robert Bertram	2000	$302,800	$404,000	$627,000	$ 870	$13,962[5]
Executive V.P. Investments	1999	276,309	102,600	101,800	798	13,343
	1998	269,053	63,200	0	777	13,209
Neil Petroff	2000	$196,130	$338,500	$451,900	$ 561	$ 0
Sr. V.P. International Equity Indexes, Fixed Income & Foreign Exchange	1999	175,444	202,800	51,400	507	0
	1998	170,606	124,700	0	490	0
Morgan McCague	2000	$186,384	$323,800	$460,000	$ 533	$ 0[6]
Sr. V.P. Quantitative Investments	1999	164,863	188,000	53,200	476	3,218
	1998	155,037	162,900	0	448	3,009
Allan Reesor	2000	$237,976	$319,200[2]	$280,100	$ 682	$ 4,808[6]
Executive V.P., Member Services and C.I.O.	1999	195,619	100,900	40,797	564	3,792
	1998	188,736	94,400	59,600	545	3,654

[1] Bonuses for investment professionals are based on a combination of total fund, asset class, and individual performance, measured in dollars of value added. Performance versus benchmark is measured over four annual performance periods.

Bonuses for other executive staff are based on achievement of annual corporate and divisional objectives.

[2] Includes deferred annual incentive for 1999.

[3] The investment long-term incentive program was restructured in 1999 following a review of competitive market practices. The new program continues to be based on four-year performance periods. Initial grants are adjusted by the four-year total fund rate of return and by a performance modifier, based on total fund dollar value-added over a composite benchmark.

[4] Automobile allowance.

[5] Includes an automobile allowance of $8,000 per annum plus unused vacation cashout.

[6] Unused vacation cashout.

13. RETIREMENT COMPENSATION ARRANGEMENT

The Retirement Compensation Arrangement (RCA) is established pursuant to an agreement between the Province of Ontario and the Ontario Teachers' Federation (the Partners), to provide to the members of the Plan certain benefits that would have been provided under the Registered Pension Plan, but for amendments made to the *Income Tax Act (Canada)* and its Regulations that restrict benefits that may be provided under a registered plan for periods of service after 1991 and for certain periods before 1992 that are credited after 1991.

The RCA is administered under a trust separate from the assets of the Registered Pension Plan. The Board has been appointed by the Partners to act as the trustee of the RCA.

Because the RCA is a separate trust, the net assets available for benefits and the value of accrued benefits and deficiency, referred to below, have not been included in the accompanying financial statements of the Registered Pension Plan on pages 26 to 28.

The RCA is funded on a pay-as-you-go basis from a portion of the contributions made to the Board by teachers, the Province of Ontario and designated private schools and organizations. The portion is based on a rate determined periodically by the Board's independent actuary in a manner that is expected to be sufficient to pay the benefits over the next 12 months. Due to the funding policy adopted by the Partners, the assets will continue to be substantially less than the liabilities.

In addition, since it is difficult to predict the benefits expected to be paid over the next 12 months, it is possible that the assets may be insufficient to pay the benefits. In such a case, the payment of benefits will be temporarily suspended and the contributions raised in order to fund the payments that are due under the RCA.

A summary of the balance sheet for the RCA as at December 31 is as follows:

($ Thousands)	**2000**	1999
Net assets available for benefits		
Assets	**$2,200**	$1,799
Liabilities	**(408)**	(655)
	$1,792	$1,144
Accrued benefits and deficiency		
Accrued benefits	**$305,900**	$238,768
Deficiency	**(304,108)**	(237,624)
	$1,792	$1,144

The actuarial assumptions used in determining the value of accrued benefits are consistent with the assumptions used in the Plan except that the assumed discount rate has been adjusted to reflect the impact of the 50 percent refundable tax under the RCA.

The estimate of the value of accrued benefits is highly sensitive to salary increases, both actual and assumed. Any changes to the salary assumptions will have a significant impact on the liabilities for future benefits. In addition, significant uncertainty exists in projecting the liabilities of the RCA due to changes in the number of future participants as well as changes to the income tax regulations relating to pensions.

14. COMMITMENTS

The Plan has committed to enter into investment transactions, which will be funded over the next several years in accordance with the terms and conditions agreed to. As at December 31, 2000, these commitments totalled $2,824 million (1999 – $1,634 million).

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

FIXED INCOME

($ Millions)

Type	Year of Maturity	Coupon (%)	Fair Value	Cost
Government of Canada bonds	2001–2029	4.50–13.00	$9,516	$9,467
Canadian corporate bonds	2001–2049	0.00–16.00	1,988	1,997
Canadian treasury bills	2001–2002	5.41–5.97	1,839	1,819
Commercial paper	2001	5.71–5.93	549	548
International corporate bonds	2003–2012	5.74–10.00	317	305
Provincial bonds	2002–2016	5.50–9.75	267	270
Foreign denominated Canadian bonds	2001–2085	4.40–13.00	213	220
Term deposits	2001	5.50–5.70	133	133
Discount instruments	2001	5.47–5.80	113	111
Securities purchased under agreements to resell	2001	2.00–6.30	1,948	1,946
Securities sold under agreements to repurchase	2001	5.75–6.45	(3,578)	(3,572)

PROVINCE OF ONTARIO DEBENTURES

($ Millions)

Maturity Date	Coupon (%)	Fair Value	Cost
2001 to 2006	9.00–15.00	$6,186	$5,170
2007 to 2012	10.00–16.00	9,155	6,661
Total debentures net of accrued interest		15,341	11,831
Accrued interest		374	374
Total		$15,715	$12,205

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

CORPORATE SHARES

(Millions)

Security Name	Shares	Fair Value $
Nortel Networks Corporation	37.8	1,823.9
Nexen Inc.	21.4	791.4
Royal Bank of Canada	9.4	476.7
Toronto-Dominion Bank, The	8.4	366.4
Encal Energy Ltd.	31.1	331.6
Bank of Montreal	4.2	328.4
BCE Inc.	7.6	328.1
Bank of Nova Scotia, The	7.5	326.1
Manulife Financial Corporation	6.8	317.8
AT&T Canada Inc.	6.9	299.7
Maple Leaf Foods Inc.	37.9	299.2
Enron Corp.	2.2	279.1
Canadian Imperial Bank of Commerce	5.7	263.3
Sun Life Financial Services of Canada Inc.	6.2	248.7
Alcan Aluminium Limited	4.7	242.4
Canadian Pacific Limited	5.5	234.5
Petro-Canada	5.1	194.1
WestJet Airlines Ltd.	8.3	192.8
Alberta Energy Company Ltd.	2.6	184.9
Celestica Inc.	2.2	177.3
Talisman Energy Inc.	2.8	155.6
Bombardier Inc.	6.3	146.7
Barrick Gold Corporation	5.9	145.3
Thomson Corporation, The	2.5	144.8
Suncor Energy Inc.	3.6	136.1
Gulf Canada Resources Limited	17.8	135.9
Canadian National Railway Company	3.1	135.5
TELUS Corporation	2.9	117.9
TransCanada PipeLines Limited	6.6	112.9
HSBC Holdings	5.0	110.2
Total Fina SA	0.6	109.3
Ballard Power Systems Inc.	1.1	103.3
Canadian Natural Resources Limited	2.4	101.6
Enbridge Inc.	2.3	101.2
Shaw Communications Inc.	2.9	99.0
Potash Corporation of Saskatchewan Inc.	0.8	97.1
Abitibi-Consolidated Inc.	7.0	95.9
ENI SpA	9.7	93.2
United Dominion Industries Limited	5.1	91.0
Imperial Oil Limited	2.3	89.6
Power Corporation of Canada	2.4	89.1
Akzo Nobel NV	1.1	86.7
Inco Limited	3.2	86.4
ING Groep NV	0.7	86.4
Research In Motion Limited	0.7	85.5
BAE Systems PLC	9.9	84.8
NewPower Holdings, Inc. (Warrants)	5.7	83.2

CORPORATE SHARES

(Millions)

Security Name	Shares	Fair Value $
XTRA Corporation	1.1	81.7
Veba AG	0.9	80.8
Placer Dome Inc.	5.5	79.2
Clarica Life Insurance Company	1.9	78.4
C-MAC Industries Inc.	1.2	77.4
Anderson Exploration Ltd.	2.3	77.4
BioChem Pharma Inc.	1.6	76.7
Hitachi Ltd.	5.6	75.2
Kirby Corporation	2.3	73.6
Bayer AG	0.9	73.5
Telefonos de Mexico SA	1.1	73.3
Westcoast Energy Inc.	2.0	73.2
Magna International Inc.	1.2	72.6
Loblaw Companies Limited	1.4	70.4
Seagram Company Ltd., The	0.9	70.3
Zurich Financial Services Group, The	0.1	69.8
National Bank of Canada	2.6	69.5
Power Financial Corporation	2.0	69.1
Telecom Italia SpA	5.8	68.4
Matsushita Electric Works, Ltd.	1.9	67.6
Telefonica, SA	1.5	65.5
NOVA Chemicals Corporation	2.3	65.0
Shell Transport & Trading Company	5.1	63.3
Novartis AG	0.02	61.9
Portugal Telecom SA	4.5	61.5
Unilever PLC	4.8	61.4
Aventis SA	0.5	59.4
TransAlta Corporation	2.7	59.3
Lindsay Manufacturing Co.	1.7	58.9
Nokia OYJ	0.9	58.1
Mackenzie Financial Corporation	2.1	57.3
George Weston Limited	0.7	56.2
Daiichi Pharmaceutical Co., Ltd.	1.2	55.7
Rogers Communications Inc.	2.2	55.2
Deutsche Bank AG	0.4	54.6
Australia & New Zealand Banking Group Limited	4.5	54.1
Trizec Hahn Corporation	2.3	53.4
Allied Irish Banks plc	3.1	53.3
Jardine Strategic Holdings PLC	12.2	53.2
Wolters Kluwer	1.3	52.4
Cheung Kong (Holding) Ltd.	2.7	52.3
Quebecor World Inc.	1.4	51.3
Shell Canada Limited	1.3	50.4
Royal Bank of Scotland Group	1.4	50.1
Alcatel	0.6	50.1

Note: For a complete list of companies, please see our website at **www.otpp.com.**

CONVERTIBLE AND EXCHANGEABLE DEBENTURES

(Millions)

Security Name	Par Value ($)	Fair Value ($)
Power Financial Corporation 8.0% Due April 30, 2014	85.5	529.8
PDFB Investments Inc. 3.25% Due March 12, 2018	89.1	254.6

INVESTMENTS OVER $50 MILLION

AS AT DECEMBER 31, 2000

REAL ESTATE PORTFOLIO

Property	Total Square Footage	Effective % Ownership
	(in thousands)	
Canadian Regional Shopping Centres		
Cataraqui Town Centre, Kingston	580	50%
Champlain Place, Dieppe	729	100%
Chinook Centre, Calgary	1,056	100%
Don Mills Shopping Centre, Toronto	420	100%
Eastgate Square, Hamilton	578	100%
Erin Mills Town Centre, Mississauga	759	50%
Fairview Mall, Toronto	883	50%
Fairview Park Mall, Kitchener	746	100%
Fairview Pointe Claire, Montreal	1,044	50%
Georgian Mall, Barrie	533	100%
Hillcrest Mall, Richmond Hill	558	100%
Intercity Shopping Centre, Thunder Bay	455	100%
Le Carrefour Laval, Montreal	1,183	100%
Les Galeries D'Anjou, Montreal	1,011	50%
Les Promenades St. Bruno, Montreal	1,036	100%
Lime Ridge Mall, Hamilton	827	100%
Market Mall, Calgary	754	50%
Markville Shopping Centre, Markham	954	100%
Masonville Place, London	684	100%
McAllister Place, St. John	471	100%
Midtown Plaza/Village, Saskatoon	687	100%
New Sudbury Centre, Sudbury	496	100%
Pacific Centre, Vancouver	1,348	50%*
Polo Park Mall, Winnipeg	1,197	100%
Regent Mall, Fredericton	446	100%
Richmond Centre, Vancouver	488	100%
Rideau Centre, Ottawa	692	31%
Sherway Gardens, Toronto	979	100%
Southland Mall, Regina	423	100%
The Promenade, Toronto	693	50%
Toronto Eaton Centre, Toronto	1,559	100%
Victoria Eaton Centre, Victoria	406	100%
Woodbine Centre, Toronto	682	60%

Property	Total Square Footage	Effective % Ownership
	(in thousands)	
Canadian Office Properties		
1 Queen Street East and 20 Richmond Street East, Toronto	503	50%
Granville Square, Vancouver	398	100%
Pacific Centre Office Complex, Vancouver	1,537	50%*
Shell Centre, Calgary	681	50%
Toronto Dominion Centre Office Complex, Toronto	4,437	50%*
Toronto Eaton Centre Office Complex, Toronto	1,899	100%
Waterfront Centre, Vancouver	395	100%
Yonge Corporate Centre, Toronto	661	50%
US Regional Shopping Centers		
Broward Mall, Fort Lauderdale, Florida	1,000	100%
Dover Mall, Dover, Delaware	834	100%
Galleria at White Plains, White Plains, New York	885	100%
Golden East Crossing, Rocky Mount, North Carolina	584	100%
Gwinnett Place, Duluth, Georgia	1,249	33%
Kitsap Mall, Silverdale, Washington	715	49%
Lakewood Center, Lakewood, California	2,044	49%
Los Cerritos Center, Cerritos, California	1,302	49%
Northpark Mall, Ridgeland, Mississippi	958	100%
Redmond Town Center, Redmond, Washington	1,119	49%
Stonewood Mall, Downey, California	929	49%
The Esplanade, Kenner, Louisiana	911	100%
Town Centre at Cobb, Kennesaw, Georgia	1,273	33%
Washington Square, Tigard, Oregon	1,239	49%

* Ownership increased to 100% subsequent to year end

PRIVATE COMPANIES AND PARTNERSHIPS

Absolute Return Fund Ltd.
Apaquogue Limited
ARC Canadian Energy Venture Fund
BC European Capital V
BC European Capital VI
BC European Capital VII
CACF Limited
DLJ Merchant Banking Partners II, L.P.
Exxel Capital Partners V, L.P.
Friedrich Grohe AG
Hicks, Muse, Tate & Furst Latin America Fund, L.P.
Magnatrax Corp.
Maple Leaf Sports & Entertainment
Maple Partners Financial Group
Morgan Stanley Real Estate Fund III International L.P.
Newcastle Capital Management Inc.
Providence Equity Partners Fund II, L.P.
Providence Equity Partners Fund III, L.P.
Schroder Asian Properties L.P.
Shoppers Drug Mart Inc.
The Macerich Company
The Third Hermes UK Focus Fund
Trimac Corporation

ELEVEN-YEAR REVIEW

FOR THE YEAR ENDED DECEMBER 31

($ Millions)	**2000**	1999	1998	1997	1996	1995	1994	1993	1992	1991	1990
CHANGE IN NET ASSETS											
Income											
Investment income	**6,211**	10,121	5,137	7,246	7,436	5,656	528	5,907	2,145	3,843	1,031
Contributions											
Members/transfers	**624**	630	612	591	620	636	732	689	711	651	559
Province of Ontario	**657**	655	653	649	673	669	704	712	740	663	587
– special payments	**—**	128	492	456	152	—	—	—	438	270	187
Total Income	**7,492**	11,534	6,894	8,942	8,881	6,961	1,964	7,308	4,034	5,427	2,364
Expenditures											
Benefits paid	**2,541**	2,278	2,103	1,802	1,520	1,261	1,130	1,001	921	829	760
Investment expenses	**100**	91	67	59	40	30	25	20	14	7	1
Member service expenses	**33**	33	32	31	29	27	26	24	23	18	19
Distribution of gain	**—**	—	—	—	—	—	—	325	—	—	—
Total Expenditures	**2,674**	2,402	2,202	1,892	1,589	1,318	1,181	1,370	958	854	780
INCREASE IN NET ASSETS	**4,818**	9,132	4,692	7,050	7,292	5,643	783	5,938	3,076	4,573	1,584
NET ASSETS											
Fixed income	**13,319**	17,304	11,476	10,276	10,622	12,509	11,409	17,569	19,007	19,199	18,129
Equities – Canadian	**17,739**	19,885	17,613	19,433	17,367	12,218	9,943	7,510	3,217	2,618	520
– Foreign	**23,141**	21,759	24,015	19,955	16,005	12,287	10,714	7,035	3,253	1,796	807
Inflation-sensitive investments											
– Commodities	**2,098**	1,090	401	126	—	—	—	—	—	—	—
– Real Estate	**6,201**	2,815	1,582	1,561	1,272	925	694	608	451	180	—
– Real Rate Products	**9,545**	4,239	3,019	1,597	1,066	1,064	653	548	457	16	—
Net Investments	**72,043**	67,092	58,106	52,948	46,332	39,003	33,413	33,270	26,385	23,809	19,456
Receivable from											
Province of Ontario	**1,251**	1,252	1,233	1,262	1,286	1,308	1,338	1,362	1,323	1,190	945
Other assets	**13,159**	7,040	5,391	8,537	3,293	1,586	622	36	72	10	—
Total assets	**86,453**	75,384	64,730	62,747	50,911	41,897	35,373	34,668	27,780	25,009	20,401
Liabilities	**(13,332)**	(7,081)	(5,559)	(8,268)	(3,482)	(1,760)	(879)	(957)	(7)	(312)	(277)
Net Assets	**73,121**	68,303	59,171	54,479	47,429	40,137	34,494	33,711	27,773	24,697	20,124
Smoothing reserve	**(4,341)**	(8,316)	(4,788)	(5,578)	(4,416)	(1,907)	(252)	(2,947)	(414)	(883)	709
Actuarial value of net assets	**68,780**	59,987	54,383	48,901	43,013	38,230	34,242	30,764	27,359	23,814	20,833
Accrued pension benefits	**58,556**	52,105	48,636	44,457	41,833	38,744	36,848	33,998	30,781	27,479	24,391
Surplus (Deficiency)	**10,224**	7,882	5,747	4,444	1,180	(514)	(2,606)	(3,234)	(3,422)	(3,665)	(3,558)
PERFORMANCE (%)											
Rate of return	**9.3**	17.4	9.9	15.6	19.0	16.9	1.7	21.7	8.9	19.6	5.6
Benchmark	**5.3**	17.6	11.9	15.6	18.1	17.2	(0.3)	20.5	8.0	15.4	(7.8)
Long-term goal	**7.7**	7.1	5.5	5.2	6.7	6.2	4.7	6.2	6.6	8.3	9.5

CORPORATE DIRECTORY

President & Chief Executive Officer
Claude Lamoureux

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Robert Bertram, Executive Vice-President

Active Equities
Brian Gibson, Senior Vice-President

Relationship Investing
Roy Graydon, Vice-President

International Equity Indexes, Fixed Income & Foreign Exchange
Neil Petroff, Senior Vice-President

Fixed Income
Sean Rogister, Vice-President

International Equity Indexes
Barbara Trott, Vice-President

Quantitative Investments
Morgan McCague, Senior Vice-President

Canadian Core Portfolios
Marcus Dancer, Vice-President

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Russ Bruch, Vice-President

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MIS Member Services
Phil Nichols, Vice-President

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Andrew Jones, Vice-President

Human Resources & Public Affairs
John Brennan, Vice-President

Internal Audit
Peter Maher, Vice-President

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Roger Barton, Vice-President, General Counsel & Secretary

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Peter Sharpe

Portfolio Operations
Brian Muzyk, Executive Vice-President & Chief Operating Officer

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Michael Kitt, Executive Vice-President

Architecture and Design
Rudy Adlaf, Senior Vice-President

Office Development
John Sullivan, Senior Vice-President

Project Management and Environmental Services
David Handley, Senior Vice-President

Investments
Andrea Stephen, Senior Vice-President

We welcome your comments and suggestions for this annual report, as well as other aspects of our communications program. Please call Lee Fullerton, Communications Manager, at 416-730-5347. e-mail: communications@otpp.com

Communications Department
Ontario Teachers' Pension Plan Board
5650 Yonge Street Toronto, Ontario M2M 4H5
Toll-free: 1-877-812-7989 Local: 416-228-5900
www.otpp.com

Pension Discount Rate Analysis for AG.pdf

Alberta

				Mar-15	
Teacher's Pre-1992 Pension Plan	No individual F/S			3.90%	
Teacher's Post-1992 Pension Plan	IFRS	7.25%	31-Aug-14	7.00%	Rate of return on invested assets
Public Service Management (Closed membership) Pension Plan	No individual F/S		http://www.r	3.90%	
Universities Academic Pension Plan	IFRS	6.25%	31-Dec-14	6.10%	Rate of return on invested assets
Local Authorities Pension Plan	IFRS	5.80%	31-Dec-14	5.80%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Public Service Pension Plan	IFRS	6.20%	31-Dec-14	6.20%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Members of the Legislative Assembly Pension Plan	No individual F/S		https://apsc.c	3.90%	
Management Employees Pension Plan	IFRS	6.40%	31-Dec-14	6.40%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Provincial Judges and Master in Chambers Pension Plan	IFRS	5.80%	31-Mar-13	5.75%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Supplementary Retirement Plan for Public Service Managers	IFRS	6.20%	31-Dec-14	6.20%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Special Forces Pension Plan	IFRS	6.30%	31-Dec-14	6.30%	The discount rate is based on the average from a consistent modeled investment return, net of investment expenses, and an additive for diversification and rebalancing.
Average for 11 plans				5.59%	

Saskatchewan

				Mar-15	
Saskatchewan Healthcare Employees' Pension Plan (SHEPP)	IFRS	6.80%	31-Dec-14	6.80%	Discount rate based upon the asset mix of the Fund
Teacher's Superannuation Plan	ASPE	3.40%	30-Jun-14	2.50%	In 2013, the discount rate methodology was changed to better reflect the Saskatchewan provincial bond yield curve to match the timing and amount of future expected benefit payments as well as the expected rate of return on assets assumption to 5% per annum up to 2030. The single discount rate was determined as a blend between the funded and unfunded portions of the Plan.
Public Service Superannuation Plan	IFRS	3.50%	31-Mar-14	2.40%	The discount rate is based on the Saskatchewan provincial bond yields with cash flows that match the timing and amount of expected benefit payments.
Others: 1) Judges, 2) Saskatchewan Transportation Company Employees Superannuation Plan, 3) Anti-TB League Employees Superannuation Plan, 4) Saskatchewan Pension Annuity Fund				4.38%	Not indicated - reviewed Saskatchewan Pension Annuity Fund
Average for 6 plans				3.09%	

British Columbia

				Mar-15	
Public Service Pension Plan	ASPE	6.50%	31-Mar-14	6.5	Annual investment return
Municipal Pension Plan	ASPE	6.50%	31-Dec-14	6.5	Annual investment return
Teachers' Pension Plan	ASPE	6.50%	31-Dec-14	6.5	Annual investment return
College Pension Plan	ASPE	6.50%	31-Aug-14	6.5	Annual investment return
Average for 4 plans				6.50%	

Quebec

				Mar-15	
Commission administrative des regimes de retraite et d'assurances (Plans administered by CARRA)	http://www.carra.gouv.qc.ca/pdf/rapport_annuel_2015.pdf	6.40%	31-Dec-14	6.50%	investment yield net of inflation
Pension Plan of the Universite du Quebec (PPUQ)				6.30%	investment yield net of inflation
Average for 2 plans				6.40%	

Newfoundland

				Mar-15	
Public Service Pension Plan	No individual F/S			6%	
Teachers' Pension Plan	No individual F/S			6.75%	
Memorial University of Newfoundland Pension Plan	IFRS	6.30%	31-Mar-14	6.30%	Fund's long-term expected return
Uniformed Services Pension Plan	No individual F/S			6.75%	
Members of the House of Assembly Pension Plan	No individual F/S			6.75%	
Provincial Court Judges' Pension Plan	No individual F/S			6.50%	
Average for 6 plans				6.51%	

Nova Scotia

				Mar-15	
Nova Scotia Public Service Superannuation Plan (PSSP)	IFRS	6.35%	31-Dec-14	6.75%	Total rate of return on assets
Nova Scotia Teachers' Pension Plan (TPP)	IFRS	6.40%	31-Dec-14	6.75%	Not indicated

Average for 2 plans (2014 - 1 plan)				6.75%	

Manitoba

				Mar-15	
Civil Service Superannuation Plan	ASPE	6.00%	31-Dec-14	6.00%	Real rate of return plus an inflation component
Teachers Pension Plan	ASPE	6.25%	31-Dec-14	6.50%	Net rate of return on plan assets
Average for 2 plans (2014 - 1 plan)				6.25%	

New Brunswick

				Mar-15	
Provincial Court Act and Provincial Court Judges Pension Act (JUDGE)	No individual F/S			6.35%	
Pension Plan for Management Employees of New Brunswick School Districts (Sch-Mgt)	No individual F/S			6.20%	
Pension Plan for General Labour, Trades and Services Employees of New Brunswick School Districts (GLTS)	No individual F/S			6.20%	
Pension Plan for Full-Time CUPE 2745 Employees fo New Brunswick School Districts (CUPE 2745)	No individual F/S			6.20%	
New Brunswick Teachers' Pension Plan Fund (NBTPP)	IFRS	Does not state	31-Dec-14		No pension obligation
Shared Risk Pension Plan for CUPE Employees of New Brunswick Hospitals	ASPE	Does not state	31-Dec-14		Rate of return on assets
Shared Risk Pension Plan for Certain Bargaining Employees of New Brunswick Hospitals	ASPE		31-Dec-14		Rate of return on assets
Public Service Shared Risk Plan Trust (PSSRP)	IFRS	Does not state	31-Dec-14		No pension obligation
Average for 4 plans				6.24%	

Summary (overview) to pwc sept 16.pdf

Statement of Facts and Assumptions

The Province of Ontario (Province) is a joint sponsor of the Ontario Teacher's Pension Plan (OTPP or the plan) and accounts for the Province's share of the plan (50%) as a defined benefit plan under PS 3250 when preparing the financial statements of the Province.

The Plan is a contributory defined benefit pension plan co-sponsored by the Province and Plan members, represented by Ontario Teachers' Federation (OTF) (the co-sponsors) and is governed by the Teacher's Pension Act – Ontario (TPA). The Plan is administered and the investments are managed by the Ontario Teachers' Pension Plan Board (the Board). Under the TPA, the Board is constituted as a corporation without share capital to which the *Corporations Act (Ontario)* does not apply. The TPA provides that the governing documents for the Plan are the pension plan established under Schedule 1 to the TPA, along with such other governing documents as may be created or adopted under the TPA or the text of the pension plan.

Section 5 of the TPA provides that the contributions of Ontario and contributing employers, on one hand, and active Plan members on the other hand, are to be approximately equal.

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

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

The following is a summary of the components of the plan

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

In recording the $10B asset, the Province has considered whether a valuation allowance should be factored into the analysis in order to ensure that the asset recorded reflects the expected future benefit from the plan that the Province can realize. Under Public Sector Accounting standards, the expected future benefit would be determined by examining the withdrawable surplus the Province can realize or through the reduction in future contributions (PS 3250.55).

In conducting its analysis, the Province has not considered any ability of the Province to withdraw surplus from the plan and has therefore focused on its ability to realize the recorded asset through a reduction of future contributions.

The FMP expressly anticipates the possibility of contribution holidays in two scenarios:

[1] Partners Agreement, section 110.

- Article IV (Temporary Improvements) of the FMP provides for temporary actions that can be taken by the partners when Plan assets are greater than current liabilities (subject to the restorations required in section 3.06 of the FMP having already been provided). Section 4.05 of the FMP provides that in such a scenario, the parties may reduce current contributions, provide temporary surplus distributions or provide a temporary benefit improvement.

- Article V (Permanent Improvements) of the FMP provides for permanent actions that can be taken when Plan assets exceed current liabilities by more than 10% of current liabilities. Section 5.05 provides for actions that can be taken in respect of the amount that assets exceed current liabilities plus the 10% margin noted previously. Such actions can include changes to current benefits, current contributions, or both.

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SECTION PS 3060
government partnerships

Additional Resources

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PURPOSE AND SCOPE

.01 This Section defines a government partnership and establishes standards on how to account for and report a government's interest in government partnerships in government financial

statements, [1] regardless of the structures and forms under which the government partnership activities take place. This Section does not deal with accounting by the government partnership itself.

.02 The standards are intended to apply to governments.

.03 This Section applies in situations where economic activities meet the definitions and criteria outlined in paragraph PS 3060.06 and paragraphs PS 3060.11-.28, even though such activities may not be referred to as government partnerships. However, this Section does not apply in situations where economic activities do not meet the definitions and criteria set out in those paragraphs even though they may sometimes be referred to as government partnerships. Accounting for such activities should be governed by their substance.

.04 For the purposes of this Section, an economic activity is not restricted to activities that generate a financial return, but extends to activities for the production and delivery of non-market goods and services that provide benefits to the community, such as law and order. That is, the partners may be motivated by factors other than the generation of financial return, such as the improvement of the welfare of their citizens.

.05 This Section does not apply to arrangements that are in and of themselves:

(a) Executory contracts such as leases and sale-leaseback transactions.

(b) Purchase / sale transactions such as outsourcing of services, management contracts and privatization. For guidance on how to account for revenues and expenses related to purchase / sale transactions, refer to FINANCIAL STATEMENT PRESENTATION, Section PS 1201.

(c) Transfers such as shared-cost arrangements and government programs. For guidance on how to account for government transfers, refer to GOVERNMENT TRANSFERS, Section PS 3410.

(d) Loans. For guidance on how to account for loans, refer to LOANS RECEIVABLE, Section PS 3050.

(e) Loan guarantees. For guidance on how to account for loan guarantees, refer to LOAN GUARANTEES, Section PS 3310.

DEFINITIONS

.06 The following definitions have been adopted for the purposes of this Section:

A **government partnership** is not a government organization but is a contractual arrangement [2] between the government and a party or parties outside of the government reporting entity [3] that has all of the following characteristics:

(a) the partners co-operate toward achieving significant clearly defined common goals; ?

(b) the partners make a financial investment in the government partnership; OTF ? Yes

(c) the partners share control of decisions related to the financial and operating policies of the government partnership on an ongoing basis; and Yes

(d) the partners share, on an equitable basis, the significant risks and benefits associated with the operations of the government partnership. Yes.

The contractual arrangement establishes that the parties have shared control over the government partnership, regardless of the difference in their ownership interest. Nevertheless, overall, there must be an equitable relationship between the financial investment of the government in the government partnership, the extent of control it is able to exercise over the activities of the government partnership, and the risks and benefits that accrue to the government from the government partnership. Government partnerships may be structured as operations under shared control, assets under shared control or organizations under shared control. [Former paragraph PS 3060.06 retained in Archived Pronouncements.]

.07 A **government business partnership** is a government partnership that has all of the following characteristics:

(a) it is a separate legal entity with the power to contract in its own name and that can sue and be sued;

(b) it has been delegated the financial and operational authority to carry on a business;

(c) it sells goods and services to individuals and organizations other than the partners as its principal activity; and

(d) it can, in the normal course of its operations, maintain its operations and meet its liabilities from revenues received from sources other than the partners.

.08 A **partner** is a party to a government partnership.

.09 **Proportionate consolidation** [4] is a basis of accounting for a government's interest in government partnerships, other than government business partnerships, whereby a government's pro rata share of each of the assets, liabilities, revenues and expenses that are subject to shared control, is combined on a line-by-line basis with similar items in the government's financial statements. ADDITIONAL AREAS OF CONSOLIDATION, paragraph PS 2510.06, provides details for applying the proportionate consolidation method.

.10 **Modified equity** is a basis of accounting for a government's interest in government business partnerships whereby the equity method of accounting is modified only to the extent that the government business partnership's accounting principles are not adjusted to conform with those of the government.

ELEMENTS THAT DEFINE A GOVERNMENT PARTNERSHIP

Contractual arrangement

.11 A distinctive characteristic common to all government partnerships is that two or more partners are bound by a contractual arrangement which establishes that the partners have shared control over the government partnership. This characteristic of shared control distinguishes a government's interest in a government partnership from investments in other activities in which the government may exercise control (see GOVERNMENT REPORTING ENTITY, Section PS 1300, BASIC PRINCIPLES OF CONSOLIDATION, Section PS 2500, ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510, and PORTFOLIO INVESTMENTS, Section PS 3041).

.12 Activities conducted with no formal contractual arrangement, but which meet the definition of a government partnership set out in paragraph PS 3060.06, are in substance government partnerships for the purposes of this Section.

.13 The contractual arrangement establishes shared control over the government partnership. Such a requirement ensures that no single partner is in a position to control the activities of the government partnership unilaterally. The arrangement identifies those decisions in areas essential to the goals of the government partnership that require the consent of all the partners and those decisions which may require the consent of a specified majority of partners.

.14 The contractual arrangement may be evidenced in a number of ways, for example, by a contract between the partners or minutes of discussions between the partners. In some cases, the arrangement is incorporated in the enabling legislation, articles or other by-laws of the government partnership. Whatever its form, the contractual arrangement is usually in writing and deals with such matters as:

(a) the activity, duration and reporting obligations of the government partnership;

(b) the appointment of the board of directors or equivalent governing body of the government partnership and the voting rights of the partners;

(c) the financial investments by the partners; and

(d) the sharing by the partners of the output, revenues, expenses or surpluses or deficits of the government partnership.

.15 In some cases, the contractual arrangement may designate a partner, or an outside party or parties, as the manager or operator of the government partnership. The manager does not control the government partnership, nor does the manager exercise shared control with the partners solely by virtue of his or her management role. Rather, the manager acts within the financial and operating policies that the partners have prescribed.

.16 A government may incorporate regulations in any contractual arrangement it enters into (e.g., level of service, level of maintenance of an asset that may be returned to it at the end of a set term). Governments regulate a variety of activities with which they have no ongoing operational involvement. As such, regulations in and of themselves do not constitute shared control.

Significant clearly defined common goals

.17 Common goals are those that all partners share. For example, a number of communities may join together to build and operate a landfill site or a recreational facility. The significant common goals of the communities involve service provision and sharing the costs and revenues associated with the operations of the facility, and so, the arrangement would qualify as a government partnership.

.18 On the other hand, a community may hire an individual or organization to operate a recreational facility for a fee. The significant goals of the government are to provide a service and cost savings, while the significant goal of the management organization is to earn revenues from the contract to manage the facility. While the significant goals of each party are mutually beneficial, they are not common to both parties to the contract, and so, the arrangement does not qualify as a government partnership.

Financial investment

.19 A financial investment may be in the form of assets and/or assuming responsibility for ongoing operating costs. The investment of financial assets and tangible capital assets in the government partnership would be accounted for in accordance with paragraphs PS 3060.41-.54. The value assigned to the responsibility for ongoing operating costs would be that determined in the contractual arrangement for the government partnership.

Shared control

.20 Shared control of a government partnership means that the partners make decisions related to the financial and operating activities of the government partnership on an ongoing basis based on the terms of the contractual arrangement; none of the partners is in a position to exercise unilateral control over the government partnership. When there is shared control, partners have an active ongoing interest or relationship in the arrangement other than as passive investors or as parties to a purchase / sale transaction. Shared control would exist, for example, when a joint board is established to oversee the provision of police or fire protection services for a number of local governments.

Shared risks and benefits

.21 In a government partnership, each partner is exposed to a share of the combined risks and shares in the benefits related to the common goals of the government partnership. In a government partnership, there must be an equitable sharing among the partners of the significant risks and benefits. For example, the government partners may operate a landfill site to provide a service to their constituents on a shared cost basis. The partners would generally share the operating and environmental risks, as well as the revenues associated with operating the landfill site.

.22 Risks and benefits would not be considered to be equitably shared in an arrangement where the government retains the full risk of owning an asset while allowing another party to receive the benefit of earning revenue from user fees derived from that asset. Risks and benefits would not be equitably shared when, for example, a government owned a highway that it allowed a private sector organization to operate and earn revenues from, based on the agreement and any necessary legislation.

FORMS AND STRUCTURES OF GOVERNMENT PARTNERSHIPS

Operations under shared control

.23 The operations of some government partnerships may involve the use of the assets and other resources of the partners, rather than the establishment of an organization or a financial structure that is separate from the partners themselves. In these circumstances, each partner may use its own assets for the purposes of the activities of the government partnership. The assets remain under the ownership and control of each partner. Each partner also incurs its own expenses and liabilities and raises its own financing, which represent its own obligations. The arrangement may provide a means by which the revenue from the sale of goods or services by the government partnership and any expenses incurred in common are shared among the partners.

.24 An example of operations under shared control is when two or more partners combine their resources and expertise for use in the operation of a landfill site. One partner may provide the land, others the equipment and others cash.

.25 In other cases, the activities of the government partnership may be carried out by the employees of one of the partners alongside the partner's similar activities. For example, provision of social services through a government partnership may involve one of the government partners being responsible for the staffing and administration of the program while all partners contribute ongoing funding.

Assets under shared control

.26 Some government partnerships involve the shared control, and often the shared ownership, by the partners of one or more assets invested in, or acquired for and dedicated to the purposes of, the government partnership. Assets under shared control are used to obtain benefits for the partners. Such a government partnership does not involve the establishment of a corporation or other organization, or a financial entity that is separate from the partners themselves. For example, several local governments may form a government partnership to acquire fire protection equipment to provide service to their constituents.

Organizations under shared control

.27 An organization under shared control is a type of government partnership which involves the establishment of a separate organization (e.g., a corporation) in which each partner has an interest. The organization operates similarly to other organizations, except that a contractual arrangement between the partners establishes shared control over the economic activities of the organization.

.28 In an organization under shared control, each partner usually contributes cash or other resources to the government partnership. The organization owns the assets of the government partnership and incurs liabilities and expenses. It may enter into contracts in its own name and raise financing for the purposes of the activities of the government partnership. For example, several local governments may operate a transit organization to provide transit services to their constituents.

ACCOUNTING FOR THE GOVERNMENT'S INTEREST

Government partnerships other than government business partnerships

.29 *Government financial statements should recognize the government's interest in government partnerships, except for government business partnerships, using the proportionate consolidation method.* [OCT. 1999]

.30 Governments may enter into government partnerships that are similar to governmental units [5] except for the extent of government control — the government shares control of the government partnership with its partners, while it controls the governmental unit. Governmental units are government organizations that carry out government activities that are integral to a government's operations in directly performing its executive function and are consolidated in the government's financial statements under GOVERNMENT REPORTING ENTITY, Section PS 1300. Government partnerships that carry out similar activities to governmental units would be accounted for using proportionate consolidation.

.31 Proportionate consolidation of such government partnerships provides financial statement users with the same sort of information about the financial position and results of operations of the government as would be available if the government managed the resources and operations through a governmental unit. Proportionate consolidation also reflects the level of activities (e.g., costs and revenues) on the government's statement of operations, the financial resources available, and the risks to which the government is exposed for such activities.

Government business partnerships

.32 *Government business partnerships should be accounted for by the modified equity method applied using the government's share of the government business partnership.* [OCT. 1999]

.33 Governments may enter into government business partnerships that are similar to government business enterprises [6] except for the extent of government control. Such government partnerships may also carry out similar activities to government business enterprises. A government business partnership differs from other government partnerships in its relationship to the government, and its objectives and operations. A government business partnership represents a financial asset of the government and given its autonomy, business-oriented objectives, and financial self-sufficiency, [7] equity accounting is appropriate. Consistent with

GOVERNMENT REPORTING ENTITY, Section PS 1300, for government business enterprises, the modified equity method is the most suitable form of equity accounting for government business partnerships.

.34 Accounting for government business partnerships by the modified equity method avoids commingling the budget and actual results of government business partnerships on a line-by-line basis with those of government activities having different objectives. It also avoids including the government's share of the gross debt of government business partnerships with the gross debt of other government organizations, as the government business partnerships are expected to repay that debt from their own revenues.

.35 The modified equity method supplemented with disclosure of condensed financial information gives financial statement users an informative accounting of the full nature and extent of the financial affairs and resources of those government business partnerships. It provides a measure of the impact that government business partnerships may have on a government's ability to discharge its liabilities or to provide financial resources for future operations.

Change in circumstances

.36 A change in circumstances over the life of a government partnership could affect either the valuation of the government's interest in the government partnership or in some cases, whether the arrangement would continue to be treated as a government partnership.

.37 In some cases, impairments in value of an asset invested in a government partnership or recognition of a contingent liability would require a write-down in the value of the government's reported interest in the government partnership.

.38 In other cases, the sharing of control, risks and benefits may change to such an extent as to cause an arrangement to no longer meet the definition of a government partnership. In such cases, the government's interest would be accounted for in accordance with GOVERNMENT REPORTING ENTITY, Section PS 1300, or other relevant Public Sector Accounting Standards or Guidelines. [8]

.39 The circumstances affecting a government business partnership may also change so that it no longer meets the definition of a government business partnership. Failure to meet any of the four elements of the government business partnership definition in paragraph PS 3060.07, would require such a change in status of the government business partnership.

.40 The alteration of an accounting treatment necessitated by events or transactions that reflect a difference in substance from those previously occurring is not considered to be a change in accounting policy or change in classification as described in ACCOUNTING CHANGES, Section PS 2120. Therefore, the change in accounting treatment would not be applied retroactively. Nevertheless, the change in accounting treatment, the underlying reasons for the change and the financial effect of the change would be disclosed.

ACCOUNTING FOR INVESTMENTS OF ASSETS

.41 *When a government invests assets in a government partnership and receives in exchange an interest in the government partnership, any loss* [9] *that occurs should be recognized at the time of the initial investment in the statement of operations.* [OCT. 1999]

.42 The existence of such a loss would usually provide evidence of a decline that is other than temporary, in the carrying value of the relevant assets retained by the government. It is also necessary for the government investing the assets to recognize the decline in value of the portion of the assets retained.

.43 *When a government invests assets in a government partnership and receives in exchange an interest in the government partnership, any gain* [10] *that occurs should be reported in the financial statements of the government as a deferred gain at the time of the initial investment only to the extent of the interests of the other non-related partners.* [OCT. 1999]

.44 The amount of the deferred gain is equal to the other partners' proportionate share of the difference between the fair value and net carrying amount of the asset.

.45 *When a government partnership other than a government business partnership is dissolved, any deferred gain related to the assets invested by the government should be recognized as revenue.* [OCT. 1999]

.46 For government partnerships other than government business partnerships, the deferred gain would not be amortized. It would only be realized at the time the government partnership is dissolved and the assets are distributed to the partners.

.47 *For government business partnerships, any deferred gain related to the assets invested by the government should be amortized to net operating results in a rational and systematic manner over the life of the invested assets. If the invested assets are non-depreciable, the deferred gain should be amortized to net operating results on a basis appropriate to the expected revenue or service to be obtained from their use by the government business partnership. When the invested assets are disposed of by the government business partnership to an independent third party, any unamortized portion of the deferred gain should be recognized as revenue.* [OCT. 1999]

.48 When the government invests assets in a government business partnership, the deferred gain would be amortized. As an asset is consumed over time by a government business partnership using it to generate cash inflows, deferred gains arising from the government's investment of assets in the government business partnership would become realized. Realization would occur because, by definition, government business partnerships are self-sustaining from revenues received from outside of the government business partnership. Deferred gains related to government business partnerships would also become realized when a government business partnership sells an asset invested by the government to an independent third party or when the government business partnership is dissolved.

Reporting tangible capital assets

.49 *When tangible capital assets are invested in a government partnership other than a government business partnership, the government should report those assets as follows:*

(a) the other non-related partners' share of assets invested by the government would be treated as disposals by the government; and

(b) the government's share of assets invested by the other non-related partners would be treated as purchases by the government in accordance with the relevant standards in FINANCIAL STATEMENT PRESENTATION, Section PS 1201*, and TANGIBLE CAPITAL ASSETS, Section* PS 3150. [OCT. 1999 •]

.50 Under FINANCIAL STATEMENT PRESENTATION, Section PS 1201, a government reports tangible capital assets as assets on the statement of financial position. TANGIBLE CAPITAL ASSETS, Section PS 3150, describes the accounting for the tangible capital assets of a government.

.51 The tangible capital assets of a government business partnership would be reflected in the government's financial statements in its one-line investment account (the "equity pickup"). The financial statements of a government business partnership would be prepared on the same basis as a private sector business. Under the modified equity method, the accounting policies of the government business partnership are not modified before determining the amount of the government's interest in the government business partnership. As a result, the government would not report the tangible capital assets of a government business partnership as described in paragraph PS 3060.49 and paragraphs PS 3060.53-.54.

(paragraph PS 3060.52 deleted)

Investments of tangible capital assets by the reporting government

.53 When a government invests an asset in a government partnership other than a government business partnership, the government would report the other non-related partners' proportionate share of an asset invested by the government as a disposal. In particular:

(a) Governments would account for the other partners' share of the net carrying amount of the asset as a disposal.

(b) Governments would recognize the net carrying amount in the statement of financial position, and would calculate deferred gains and losses based on the fair value less the net carrying amount of the assets.

Investments of tangible capital assets by the other partners

.54 When a non-related partner invests a tangible capital asset in a government partnership other than a government business partnership, the government would report its proportionate share

of that tangible capital asset as a purchase. In particular, governments would treat that amount as an increase in the tangible capital assets reported in the statement of financial position.

PRESENTATION AND DISCLOSURE

.55 *Government financial statements should disclose, in notes or schedules:*

(a) a description of the nature and purpose of government partnerships;

(b) a listing of government partnerships, including the government's share, separately identifying those that are accounted for using the proportionate consolidation method and those that are accounted for by the modified equity method; and

(c) condensed supplementary financial information relative to government partnerships. Such financial information should be provided separately for those government partnerships accounted for using proportionate consolidation and those accounted for using modified equity, on:

(i) the financial position and results of operations, including:

- *total assets and liabilities segregated by main classification;*
- *net assets or liabilities, separately displaying accumulated other comprehensive income;*
- *total revenues and expenses; and*
- *net operating results for the period, separately displaying other comprehensive income;*

(ii) the nature and amount of any adjustments to net assets or net operating results, as shown in the financial statements of the government partnerships, to arrive at the amount included in the government's statement of financial position or statement of operations; and

(iii) transactions and balances with organizations included in the government reporting entity. [OCT. 2006]

.56 *The government should disclose its share of any contingencies and contractual obligations of government partnerships and those contingencies that exist when the government is contingently liable for the liabilities of other parties to those government partnerships.* [OCT. 1999 •]

.57 *Deferred gains arising from the government's investment of assets in the government partnership should be reported with liabilities in the government's statement of financial position.* [OCT. 1999]

.58 Users of government financial statements need an appreciation of the magnitude of financial activities conducted by government partnerships and the effect of their operations on the government. This information would usually be presented on a combined basis.

.59 Separate disclosure of the government's share of any contingencies and contractual obligations of government partnerships would include, as appropriate:

(a) the government's share of any contingencies and contractual obligations of the government partnership; and

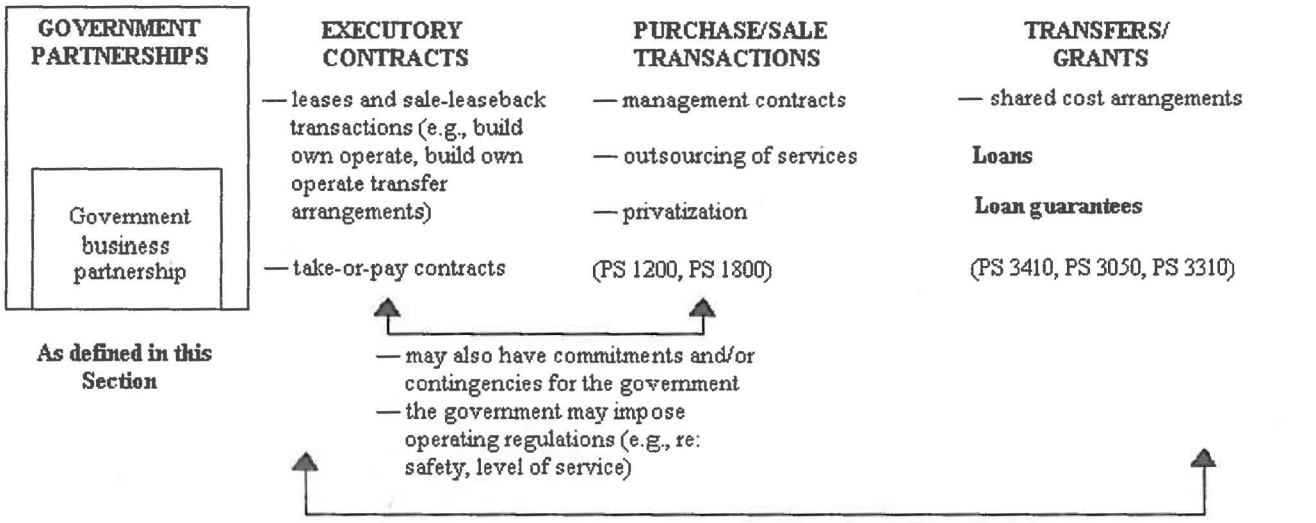
(b) the government's responsibility, if any, for the other partners' share of the contingencies of the government partnership.

If the government guarantees more than its proportionate share of a government partnership's liabilities, such a guarantee would be disclosed.

.60 The level of detail disclosed by governments should reflect the highly aggregated nature of financial statements. In deciding the level of detail to disclose, governments should consider the usefulness of the information to the reader in assessing the nature of, and the costs associated with, government partnerships.

APPENDIX A

TYPES OF GOVERNMENT CONTRACTUAL ARRANGEMENTS



These types of contractual arrangements are not government partnerships as defined in paragraph PS 3060.06.

Footnotes

1. The term "financial statements" refers to the summary financial statements published by a government that report on the financial position and changes in financial position of the government reporting entity.

2. A chart showing the various types of government contractual arrangements, including government partnerships, is included as Appendix A.

3. In arrangements where government employees jointly manage an employee benefit program (e.g., a pension plan) with the government, the employees are not considered to be parties outside of the financial reporting entity for the purposes of applying the definition of a government partnership.

4. Detailed guidance on the application of proportionate consolidation is set out in ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510.

5. Governmental units are defined in BASIC PRINCIPLES OF CONSOLIDATION, Section PS 2500.

6. GOVERNMENT REPORTING ENTITY, paragraph PS 1300.28, defines a government business enterprise.

7. GOVERNMENT REPORTING ENTITY, paragraph PS 1300.31, identifies factors for determining the financial self-sufficiency of a government business enterprise. Those factors would be considered when assessing the financial self-sufficiency of a government business partnership.

8. BASIC PRINCIPLES OF CONSOLIDATION, Section PS 2500, ADDITIONAL AREAS OF CONSOLIDATION, Section PS 2510, PORTFOLIO INVESTMENTS, Section PS 3041, and FINANCIAL INSTRUMENTS, Section PS 3450, may also provide relevant guidance in some cases where the arrangement no longer meets the definition of a government partnership.

9. A loss occurs when the fair value of the asset invested is less than its net carrying amount in the government's financial statements.

10. A gain occurs when the fair value of the asset invested is greater than its net carrying amount in the government's financial statements.

* Editorial change — January 2003, February 2007 and June 2011.

* Editorial change — September 2004.

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please review (last page).rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]
Subject: please review (last page)
Date: Thursday, September 22, 2016 10:25:48
Attachment 1: FMP_Temporary Plan Improvement Zone Discussion Deck.pdf

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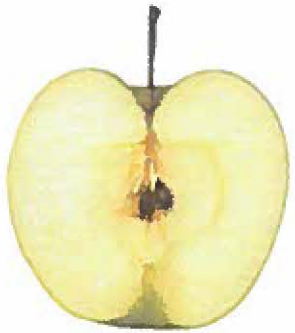
Hi Lucy.

Just forwarding a deck (we just became aware of) that demonstrates, based on scenario analysis, that the Province can expect to be in the temporary zone 30% of the time.

Talk to you later.

N

FMP_Temporary Plan Improvement Zone Discussion Deck.pdf



TEMPORARY PLAN IMPROVEMENTS

Draft for Discussion

March 19, 2014 (Sponsor's Task Force Meeting)

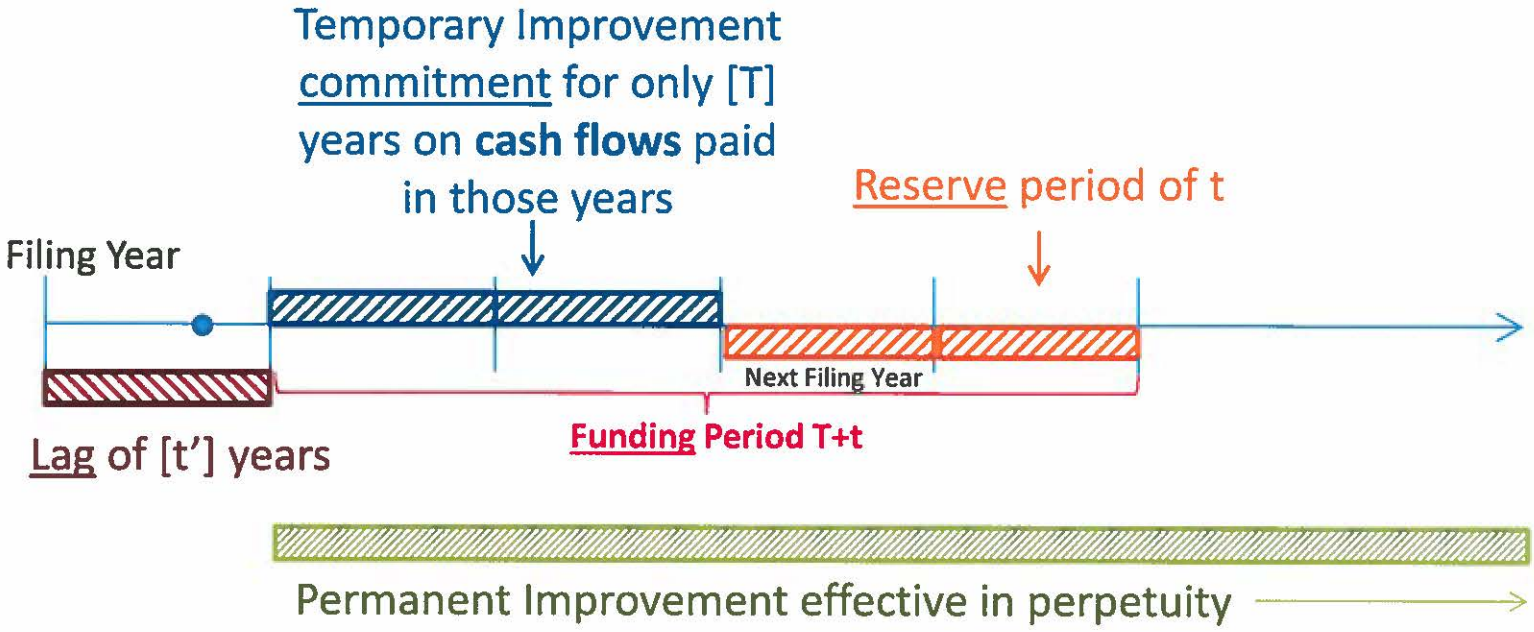
Funding Management Policy - Framework Description

TEMPORARY PLAN IMPROVEMENTS INCLUDE:

- Decrease to cash contribution paid
- Increase to benefits paid to pensioners in pay
- a combination of both

Temporary plan improvements are determined in a filed funding valuation. They are effective with a **lag** of [t'] years with a **commitment** of [T] years, **reserve** over t years and **funded** over a period of T+t. They impact only affected cash flows paid in years [t'] through [T].

Filing in temporary zone occurs if new temporary benefits schedule better than the current temporary benefits schedule.



Funding Management Policy - Framework Description

Valuation Basis

Assets = 110% of Liabilities valued at interest rates + 0.5%

Zone:	**Permanent Plan Improvements**
Mechanism:	Improve benefits as negotiated
Funding Risk:	Plan is essentially fully funded at Government of Canada long bond rates. Funding security is desired to ensure the Plan can support these benefits continually in the future. The impact of new teachers is important as they will create losses.

That is, Assets ~ 133% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1%

Zone:	**Temporary Plan Improvements**
Mechanism:	Improve benefits or lower contributions as negotiated[1]
Funding Risk:	Plan is well funded and can afford changes that temporarily provide a benefit enhancement (as long as it does not create a long term cost) and/or lower the contributions being paid into the plan.

[1] A funding reserve will be created to help support the temporary benefits

That is, Assets ~ 116% Liabilities valued at interest rates + 1.55%

Assets = Liabilities valued at interest rates + 1.55%

Zone:	**Fully Funded**
Mechanism:	Maintain Base Benefits and Contributions
Funding Risk:	Plan is adequately funded to provide base benefits supported by the base contributions. Given the volatility of market factors and the numerous assumptions in the funding valuation, "fully funded" is considered a range.

Zone:	**Additional Support Required From Current FMP Levers**
Mechanism:	Raise Contribution Rates and/or Invoke Conditional Inflation Protection as negotiated
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions. An increase to the contribution rate (within FMP maximum) and/or a decrease to the level of indexing being provided are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Zone:	**Additional Support Required From New/Additional Changes**
Mechanism:	Negotiate other plan changes
Funding Risk:	Plan is not considered adequately funded to provide base benefits supported by the base contributions and CIP is fully invoked and contribution rates are increased to maximum outlined in FMP. Plan changes are necessary to recoup the deficit. As the funding position improves, these plan changes will be reversed.

Next step is to review simulation results

TEMPORARY IMPROVEMENTS – Baseline FMP for Simulations

	Distribution Surplus	Surplus/Deficit split
Step 1:	Benefit Improvement (unlimited)	100%

	Distribution Deficit	Surplus/Deficit split
Step 1:	Raise Regular contribution up to 11%	100%

	Temporary Surplus	Surplus/Deficit split
Step 1:	Temporary Regular Contribution Reduction (regular CR no lower than 0%)	100%

Lag: 1 year, Commitment: 3 years, Reserve: 7 years, Funding Period: 10 years, Spread: 1.00%

	Restoration Surplus	Surplus/Deficit split
Step 1:	Lower Special to **1%**	100%
Step 2:	Restore Future Indexation Level to 100%	100%
Step 3:	Catch Up to 50% (both Post 2009-Pre 2014 and Post 2013 at 50%)	100%
Step 4:	Catch Up to 100% (both Post 2009-Pre 2014 and Post 2013 at 100%)	100%
Step 5:	Lower Special to 0%	100%

	Restoration Deficit	Surplus/Deficit split
Step 1:	Raise Special to **1%**	100%
Step 2:	Reduce Indexation Level (Post 2009-Pre 2014: 50%, Post 2013: 0%)	100%
Step 3:	Raise Special no threshold	100%

Note: FMP CR = 12%, Usable Surplus in Temporary zone is based on smooth assets and smooth liabilities

Brief Explanation of Metrics for Analysis

TEMPORARY PLAN IMPROVEMENTS METRICS for ANALYSIS:

- Probability in FMP Zone: Probability that OTPP will be in a particular FMP zone in the future
- Probability Temporary Benefits in pay: Probability that temporary benefits will be paid in the future and in which FMP Zone that will occur
- Probability Temporary Benefits in pay while in FMP Zone: What is the percentage of times a temporary benefits is in pay while in a particular FMP Zone

TEMPORARY IMPROVEMENT ZONE – POTENTIAL METRICS

# observations in each zone	Restoration Zone (Sp CR +CIP+add'l Sp CR)	Restoration Zone (Special CR)	Do Nothing Zone	Temporary Improvement Zone	Distribution Zone, usable surplus
Current (Starting FR 100%)	30%	2%	38%	0%	30%
Metrics					
Probability in FMP Zone (rounded)					
Baseline	32%	2%	27%	33%	6%
Probability in Temporary Benefits in pay (rounded)					
Baseline	0%	0%	9%	21%	3%
Probability Temporary Benefits in pay while in FMP Zone (rounded)					
Baseline	0%	0%	34%	63%	56%

Note: Starting FR= 100%

pw_.rtf

From: Petsche, Nadine (TBS) []
To: lucy.durocher@ca.pwc.com [lucy.durocher@ca.pwc.com]; Lucy Durocher (CA - ASR) (lucy.durocher@pwc.com) [lucy.durocher@pwc.com]
Subject: pw?
Date: Monday, January 23, 2017 22:16:08

Hi Lucy.

Sorry to bother you. Can you share the pw for the report? n

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); christina.chan@ca.ey.com; Shayan Jafrani; "Uros Karadzic"
Subject:	OTPP Recognition of accrued benefit asset
Start:	April 3, 2017 4:00:00 PM
End:	April 3, 2017 4:15:00 PM
Location:	Christina to call Nadine at 416 327 5 8027
Attachments:	OTPP Recognition of accrued benefit asset (EY 30 March 2017)np.docx

Hi Christina and Shayan.

Thanks for sharing the draft analysis on OTPP. I was hoping you might be available for a 15 minute call later today or tomorrow to discuss my comments (attached) and next steps.

Shyrose can help to set up a time to chat.

Thanks.

Nadine

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Any tax advice in this e-mail should be considered in the context of the tax services we are providing to you. Preliminary tax advice should not be relied upon and may be insufficient for US penalty protection. Tout conseil de fiscalité contenu dans le présent courriel doit être pris dans le contexte des services de fiscalité que nous vous offrons. Aucune décision ou position ne doit être prise à la lumière de conseils de fiscalité préliminaires, lesquels pourraient ne pas permettre d'éviter des pénalités aux États-Unis.

From:	Virani, Shyrose (TBS)
To:	Petsche, Nadine (TBS); Patel, Bharat (TBS); Fong, Pauline (TBS); Li, Wendy (TBS); Sun, Alicia (TBS); Ma, Patricia (TBS); Shayan Jafrani; christina.chan@ca.ey.com
Cc:	"Uros Karadzic"; Veinot, Cindy (TBS)
Subject:	OTPP Recognition of accrued benefit asset
Start:	May 10, 2017 3:00:00 PM
End:	May 10, 2017 3:30:00 PM
Location:	teleconference 416 246 7171 passcode 1474532#

Nadine to moderate

From:	Virani, Shyrose (TBS)
To:	Sekaly, Gabriel (EDU); Paul, Joshua (EDU); Killoch, Alex (MOF); Veinot, Cindy (TBS); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc:	Talwar, Garima (MOF); lucy.durocher@ca.pwc.com; "lucy.durocher@pwc.com"; Roberto, Nicole (EDU); Duffy, Paul (EDU); Tsang, Ingrid (MOF)
Subject:	pension
Start:	September 19, 2016 12:30:00 PM
End:	September 19, 2016 1:00:00 PM
Location:	teleconference 416-212-8014 passcode 1474532#, APFR Boardroom

From:	Virani, Shyrose (TBS)
To:	"uros.karadzic@ca.ey.com"; Veinot, Cindy (TBS); Donaldson, Mark (TBS); "sarah.anderton@ca.ey.com"
Cc:	Christina Chan
Subject:	Pension Asset - additional advice
Start:	June 25, 2018 12:30:00 PM
End:	June 25, 2018 1:00:00 PM
Location:	Teleconference 416 212 8013 passcode 4950903#, ADM"s boardroom

From:	Virani, Shyrose (TBS)
To:	christina.chan@ca.ey.com; Sun, Alicia (TBS); Patel, Bharat (TBS); Fong, Pauline (TBS); Ma, Patricia (TBS); Chan, Vanessa W. (TBS)
Cc:	"Gregory Winston"; "Uros Karadzic"
Subject:	Pension Planning
Start:	December 18, 2017 3:00:00 PM
End:	December 18, 2017 4:00:00 PM
Location:	TBS-R-7 Queen"s Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom

From:	Virani, Shyrose (TBS)
To:	christina.chan@ca.ey.com; Sun, Alicia (TBS); Patel, Bharat (TBS); Fong, Pauline (TBS); Ma, Patricia (TBS); Chan, Vanessa W. (TBS)
Cc:	"Gregory Winston"; "Uros Karadzic"
Subject:	Pension Planning
Start:	December 18, 2017 3:00:00 PM
End:	December 18, 2017 4:00:00 PM
Location:	TBS-R-7 Queen"s Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom

From:	Virani, Shyrose (TBS)
To:	Sekaly, Gabriel (EDU); Paul, Joshua (EDU); Killoch, Alex (MOF); Veinot, Cindy (TBS); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc:	Talwar, Garima (MOF); lucy.durocher@ca.pwc.com; "lucy.durocher@pwc.com"; Roberto, Nicole (EDU); Duffy, Paul (EDU); Tsang, Ingrid (MOF)
Subject:	pension
Start:	September 19, 2016 12:30:00 PM
End:	September 19, 2016 1:00:00 PM
Location:	teleconference 416-212-8014 passcode 1474532#, APFR Boardroom

From:	Virani, Shyrose (TBS)
To:	Sekaly, Gabriel (EDU); Paul, Joshua (EDU); Killoch, Alex (MOF); Veinot, Cindy (TBS); Petsche, Nadine (TBS); Pomykacz, Rob (MOF)
Cc:	Talwar, Garima (MOF); lucy.durocher@ca.pwc.com; Roberto, Nicole (EDU)
Subject:	pensions
Start:	September 20, 2016 3:00:00 PM
End:	September 20, 2016 3:30:00 PM
Location:	teleconference 416-212-8013 passcode 4950903#, ADM"s Boardroom

From:	Virani, Shyrose (TBS)
To:	Ma, Patricia (TBS); Chan, Vanessa W. (TBS); christina.chan@ca.ey.com; "Gregory Winston"
Subject:	PSPP HOOP and CAAT
Start:	January 19, 2018 10:30:00 AM
End:	January 19, 2018 11:30:00 AM
Location:	TBS-R-7 Queen"s Park Crescent-OTB.OPCD.FS.2ndFl.APFR.Boardroom, teleconference 416 212 8014 passcode 1474532#