LONG-FORM MEMBER QUESTION

DEPUTY MINISTER HELEN ANGUS

&

CINDY VEINOT, PROVINCIAL CONTROLLER

PENSION ASSET ACCOUNTING

QUESTION

- My question is about pension plans and how Ontario accounts for them in its Public Accounts – specifically, for the Ontario Teacher's Pension Plan and the OPSEU Pension Plan.
- We all know the importance of pensions for workers, and so questions around pensions tend to raise interest.
- I'm not an accountant so to me, what's not as clear, is why we are discussing pensions in relation to Public Accounts.
- The Ontario Teacher's Pension Plan and the Ontario Public Service Employee's Union Pension Plan are being included as assets in the Public Accounts.
- Why is that, and why are we discussing these pension plans in particular?
- And if you could maybe speak about what evidence and processes were used to support the decision made by the government, I would welcome that as well.

Commented [DM(1]: ??

ANSWER

Deputy Minister Angus Introduction

- Thank you for the question. I'll turn it over in just a moment to our Provincial Controller Cindy Veinot, who can provide more details.
- But let me first say that the government continues to move forward and present the province's finances fairly and accurately in accordance with Canadian Public Sector Accounting Standards.
- To provide a bit of context to Cindy's answer, let me provide a quick overview of the issue of pension asset accounting in the Public Accounts.
- Back when the government released the 2015-16 Public Accounts, there was a disagreement between the Office of the Auditor General and the province's professional accounting staff on this issue. The conversation centred on the appropriate application of the Public Sector Accounting Standards in the reflection of the Ontario Teacher's Pension Plan and the OPSEU Pension Plan in the Public Accounts.
- These pension plans are jointly-sponsored – meaning there is shared management and risk by both the government as the employer, and the bargaining agent for the members of the respective plans. In these cases, the bargaining agent is the Ontario Teachers' Federation for one plan, and the Ontario Public Service Employees' Union in the other.
- The Auditor General's position was that a full valuation allowance on the government's share of the plan on the province's two jointly-sponsored pension plans must be provided. A valuation means they were effectively written down to zero.
- That interpretation was a break from the accounting practices that the government has been using in Public Accounts since 2001, and so the government was not prepared to make that change without first considering it fully and seeking external expertise on the matter.

- To allow for the release of the release of the Public Accounts, a time-limited regulation on the accounting treatment for those pension plans was passed in September 2016.
- This regulation allowed officials from the Treasury Board Secretariat and the Ministry of Finance to sign the Statement of Responsibility for the 2015-16 Public Accounts, while we reviewed the question of how to account for these pension plans.
- The government then sought wide-ranging advice on how to move forward, including convening an independent Pension Asset Expert Advisory Panel, getting advice from external consultants, and conducting further research and analysis internally.
- This is a key part of our role as public servants – to conduct our due diligence and provide our best advice based on our professional judgment.
- Based on this research, during the 2016-17 fiscal year, it was confirmed by the government that the Public Sector Accounting Standards do not require a valuation allowance for either of the pension plans the Auditor General had identified.
- This determination was based on the panel report and the opinions from our external consultants, as well as our own review of the accounting standards.
- The decision not take a valuation allowance was consistent with the accounting treatment that Ontario has used consistently since 2001. The 2015-16 Public Accounts were adjusted to reflect that decision in order to ensure year-over-year comparisons of Public Accounts were possible.
- So I think that provides some high-level context, and now I'll pass it over to Provincial Controller Veinot who can go into more detail.

Cindy Veinot, Provincial Controller

- Thank you, Deputy Angus, for that overview. You hit the main points, so I'll get into some of the details.

- The government has chosen to continue to recognize pension assets from the two pension plans under discussion based on advice we received from external experts and from our own research and analysis on the Public Sector Accounting Standards.
- The Treasury Board Secretariat uses external expertise to supplement our own resources on complex accounting and reporting matters like this one. External advisors are engaged to provide advice and guidance to supplement our internal analysis.
- One example of this is the establishment of the Pension Asset Expert Advisory Panel during the 2015-16 fiscal year.
- This Panel was made up of four members, who were tasked with providing independent advice and recommendations to the government on the application of Public Sector Accounting Standards to Ontario's net pension assets.
- The four members of the Panel included accounting and legal experts, as well as pension experts that specialize in jointly-sponsored pension plans, actuarial modelling for pension plans, and Public Sector Accounting Standards.
- The panel also provided advice on how to value net pension assets reported on the province's books, taking into account future decisions which might be made by the plan's sponsors.
- When the government announced it would be establishing the panel, it laid out the mandate very clearly, which included considering four things:
  - First, whether the government as a joint sponsor could be considered to have control of the plan, which is a necessary condition to recognizing pension plans as assets;
  - Second, the requirement regarding control with respect to recognizing a pension asset for other pension plans;
  - Third, the appropriate valuation techniques to measure a pension asset that take into considering future decision-making authority by plan sponsors; and.

  - Fourth, to provide recommendations to the Employee Future Benefits Task Force of the Public Sector Accounting Board regarding issues that should be considered in its review of the retirement and post-employment benefits standards.
- The government asked that this advice be provided by the end of 2016 so that it could be shared with the Office of the Auditor General and with the public.
- The President of the Treasury Board received this report and shared it with the Office of the Auditor General, as well as making the report public in early 2017.
- The panel determined that the province's share of the net pension assets of both pension plans should be recognized in Ontario's financial statements, including Public Accounts.
- The government accepted the independent panel's recommendations and thus indicated its plans to account for these pension plans as government assets in the 2016-17 Public Accounts.
- With the expiration of the time-limited regulation, we also adjusted the 2015-16 Public Accounts to follow this recommendation.

Findings of the Panel

- Let me dig in to the findings of the panel just a little bit here, in the interest of clarifying the government's decision to list these pension plans as assets.
- The panel needed to determine whether the government could be considered to have control of the plan as a joint sponsor, a determination they made based on the governance and the terms of the plans, and how best to follow Public Sector Accounting Standards.
- Based on the research that the panel conducted, it concluded that an asset existed for the Ontario Teacher's Pension Plan and the OPSEU Pension Plan because the accounting surplus in the plans have a future economic benefit both to the government and the employee sponsors.

- This future economic benefit can be realized by reducing the contributions the government makes to the plans, freeing cash for other purposes that would otherwise be required to make contributions.
- The panel also concluded that the government controls access to that accounting surplus because it shares control of the surplus with the employee sponsors. In the case of the OPSEU Pension Plan with OPSEU, and in the case of the Ontario Teacher's Pension Plan with the Ontario Teacher's Federation.

Ontario Teacher's Pension Plan

- In the case of the Ontario Teacher's Pension Plan, sponsors must agree with how the surplus funds will be used.
- However, if they do not agree, there is a process included in the pension plan itself that helps both sponsors reach a decision.
- The only condition in the Ontario Teacher's Pension Plan for accessing that extra money is that it must be shared equitably between the sponsors.
- Historically, this has meant a 50/50 split of the surplus over time.

OPSEU Pension Plan

- In the OPSEU Pension Plan, funding surpluses are allocated 50/50, and each sponsor is allowed to use the allocation they receive either to improve benefits for members of the pension plan or to reduce contributions as each sponsor determines appropriate.
- These agreements indicate that the government can reasonably determine that it would be able to reduce the contributions to the pension plans in order to free up cash for other purposes.

Reducing Contributions to Pension Plans versus Removing Assets from Plans

- Another important point to make is that there are different rules for directly taking assets out of the plans compared to reducing contributions to the plan.

- Directly taking assets out of the plan requires permission from members of the plan or approval of the joint sponsor, as well as outside approval from the Financial Services Commission of Ontario.
- To reduce pension contributions, however, only requires that the plan sponsors agree to reduce contributions, and does not require any approvals from external parties.
- It is important to note that the government is not seeking to remove assets directly from the pension plans.
- Because of the existing surplus, some of the funds that would be contributed to the plans could reasonably be used in other ways without affecting the status of the pension plans.
- This issue is whether the government could expect to be able to reduce contributions to these plans, thus freeing up that funding for other purposes that the question of accounting for them as assets rests.

Main Findings of the Panel Regarding Control

- The Panel arrived at two main findings, based on what I've just outlined. The findings support accounting for these pension plans as assets in the province's Public Accounts:

    1) First, there is no requirement under Public Sector Accounting Standards that any formal agreement must exist between the joint sponsors regarding the timing or amount of a reduction in contributions to record an asset. This is because the existing agreements in place between the parties support the recognition of an expected benefit.

    2) Second, unilateral control is not required to allow the government to recognize the pension plan surplus as an asset. Joint control, with each party having the ability to deny the actions of the other sponsor,

only provides evidence of shared control, not a lack of control. Thus, joint control supports the recognition of an asset.

- Based on the recognition of these plans as assets, showing the pension plans as assets in the Public Accounts is a faithful representation of the province's financial position.
- It would therefore be misleading not to recognize the province's share of the Ontario Teacher's Pension Plan and the OPSEU Pension Plan as assets in the Public Accounts.

Independent External Analysis

- While the independent panel supported the government's position on these pension plans, the government also sought out further advice.
- The government sought opinions from two leaders in accounting practice – Deloitte LLP and EY.
- Deloitte provided an opinion on aspects of the province's accounting as of March 31, 2016 for the Ontario Teacher's Pension Plan.
- The opinion, which was dated October 2, 2016, concluded that it was permissible to recognize a pension asset under Public Sector Accounting Standards, even though the province did not have a unilateral right to reduce contributions.
- The opinion provided from Deloitte did not address the value at which the asset should be recorded.
- A further consideration that needed to be addressed is at what value is the pension asset being reported, and does it overstate the future benefit that can be drawn from lower contributions.
- If the province's share of the plan assets exceed what can be expected as future benefit, then the asset must be have a valuation allowance applied to it to bring it to an appropriate level.
- An analysis was completed by EY as to whether any valuation allowance is required to be recorded for both pension plans.

Commented [DM(2]: Language? Can/should the opinion be read into the record?

- As of March 31, 2017, EY confirmed that no valuation allowance was required for either plan.

Decision to Take Advice

- After significant deliberation, including consideration of the expert panel, Deloitte's opinion, and EY's opinion, Ontario confirmed that the accounting for these plans prior to the 2015-16 fiscal year was appropriate.
- The government's position on recording these pension plans as assets is in line with Public Sector Accounting Standards for pension asset accounting.
- Based on extensive consideration, the government determined that the appropriate accounting for the 2016-17 financial statements should include these pension assets.
- Consistency in accounting is important because it allows people to make year-over-year comparisons. When changes are made, the government is transparent and open about the changes.
- In the case of pension assets, we have been open and transparent about the way the government arrived at the decision to continue listing the pension plans as assets in the Public Accounts.
- In addition to following the expert advice going forward, in order to make sure that comparisons are able to be made year-over-year in the Public Accounts, the 2015-16 financial statements were restated to reflect the pension surpluses as assets.

Conclusion

- In closing, I want to reiterate that while the province respectfully disagrees with the Office of the Auditor General's interpretations of the Public Sector Accounting Standards on this issue, we are open to continuing to discuss it in the hopes of finding a resolution.

- Public Sector Accounting Standards do not say that the government must have unilateral control over the jointly-sponsored pension plans to record them as an asset.
- Because there are ways to access the value of these pension plans, including reducing employer and employee contributions, and because the surplus was built on previous actions taken by the government and employees, as well as investment income, it should be recorded as an asset.
- In following the advice of the independent panel and the organizations engaged to provide additional outside analysis, there is the added benefit of the government following the accounting treatment that Ontario has consistently used since 2001 which makes year-over-year comparisons possible.
- We stand by our extensive research and analysis. We take our duty to provide the most fair and accurate Public Accounts very seriously, and in accounting for pension assets we are always guided by that duty.