TBS

Office of the Provincial Controller Division

Accounting for Pension Assets

Minister's Office Briefing

December, 2016

For Discussion Purposes Only

Background

- For accounting purposes, net pension assets arise when cumulative contributions exceed the cumulative reported pension expense
- During the 2015/16 Public Accounts audit, the AG questioned the Province's historical accounting for assets related to jointly sponsored pension plans, specifically the Ontario Teachers' Pension Plan (OTPP) and the OPSEU Pension Plan (OPSEUPP)
- According to the AG's interpretation of public sector accounting standards (PSAS), no assets should have been reported for these two plans as at March 31, 2016
- In order to reflect the impact of AG's interpretation of the accounting standards, the government used regulated accounting.
- The results of the Expert Advisory Panel on Pension Assets will be considered in confirming the Province's accounting treatment for net pension assets for 2016/17 and future years.

AG's Position

- In order for a net pension asset a jointly sponsored pension plan to be reported on the Province's books according to the Auditor General's interpretation of accounting standards, the following must be present:
  - a legally enforceable right to unilaterally access the asset
  - an agreement in place at year-end with the Co-Sponsor which addresses reduced future contributions
- The AG did not raise any issues or concerns with accounting for assets related to the HOOPP and CAATTPP asset which are not jointly sponsored pension plans and for which only CAATPP had a relatively minor reported asset in 2015/16

Reporting in the 2015-16 Public Accounts

- The Province disagrees with the Auditor General's interpretation of Public Sector Accounting Board (PSAB) standards
- The Province believes its share of accounting surpluses of joint defined benefit plans should be recognized as an asset.
- Reporting the assets would reflect the Province's expectation of benefit through reduced future contributions and the measurement of reported assets is supported by the results of a pension asset ceiling test which confirmed that the asset values are not impaired.
- Since Management did not agree with the AG's interpretation of PSAB standards as related to jointly sponsored pension plans, a regulation was necessary in order to achieve the AG's accounting treatment and to allow management to sign off on the Statement of Responsibility.

Overview of Joint Defined Benefit Plans

- Sponsors are jointly responsible for decision making, share in contributions, and collectively address any plan funding surplus/deficit (at least every 3 years).
- Sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process
- For OTPP for example, the plan administrator is an independent board of directors that 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.

Historical Accounting for OTPP

- Since 2001-2002, the Province has recorded its portion (50%) of the pension asset of OTPP in accordance with public sector accounting standards.
- With regards to expected future benefit of the surplus, the Province would not expect to withdraw any surplus, but benefit through reduced future contributions.
- With regards to OTPP's own stand alone financial statements - they are prepared under a different basis of accounting standards relevant for or pension plans (Part IV of the CPA Canada Handbook) and is also different than the basis used by the OTPP to measure and report the net surplus or deficit for funding purposes.
- Accounting standards acknowledge that the objective of funding and accounting are different. Because of the different objectives, it is important to note that the discount rates used are also be different.

Province's Position on Asset Recognition

- 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

Asset Ceiling Test (Maximum Reportable Asset)

- Calculation of the asset ceiling test involves professional judgement
- 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 following slides consider this calculation relative to the Province's 50% share of OTPP

Considerations re: Surplus Withdrawal (Part b of the asset ceiling test)

- The Province does not expect to realize its expected future benefit 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
- As at March 31, 2016 the Province did not have a signed agreement with OTF regarding withdrawal of the surplus

Considerations re: Reduced Future Contributions (Part a of the asset ceiling test)

- While Section PS 3250 states that legal enforceability is required to report an expected benefit 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 expects to 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/reductions. 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, or when there is a surplus. The surplus “zone” for OTPP impacts how the pension surplus may be utilized by the Province summarized in Appendix 3
- In addition, the Income Tax Act (ITA) imposes limits on the level of contributions that may be made to a pension plan that has “excess surplus” (as defined by the ITA).
- 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

Reduced Future Contributions (Part a of the asset ceiling test) (continued)

- There is very limited guidance in PSAB standards 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.
- Based on the Province's best estimate calculation of the expected future benefit and the results of the actuarial valuations performed as part of the pension asset ceiling test, no valuation allowance was deemed necessary in relation to the pension asset of OTPP at March 31, 2016.

Other Measurement Considerations

- 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 (both in terms of selection of rate under PSAS and in Ontario's case, management's best estimate of the long-term 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
- The choice of rate used by the Province (long-term rate of return on plan assets) is **consistent** with the rate used by other Provinces in Canada for their pension plans (see Appendix 6)
- PSAS acknowledges that the objective of funding and accounting are different (Section PS 3250 paragraphs .008 to .010). Because of the different objectives, the discount rates used will also be different.

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 and assumptions
- 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 relating to OTPP that would have otherwise been reported on the Province's books as at March 31, 2016

Comparable Reporting by Provinces

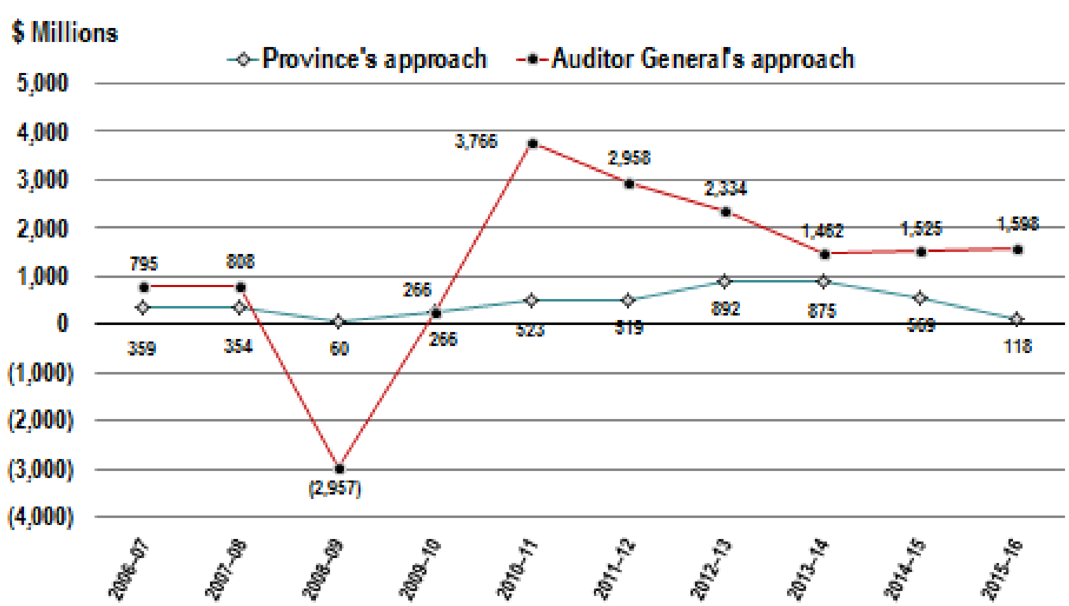
- Provinces such as British Columbia, New Brunswick, Manitoba and Nova Scotia do not report assets for their provincial sponsored pension plans or alternatively provide a valuation allowance to reduce the value of a pension asset balance to nil
- The different accounting treatment in the Province of Ontario (for OTPP) reflects the difference circumstances in these other provinces with regards to expected future benefits related to pension surpluses

APPENDICES

Appendix 2:Comparison of key measurements of the Province over the prior 10 years

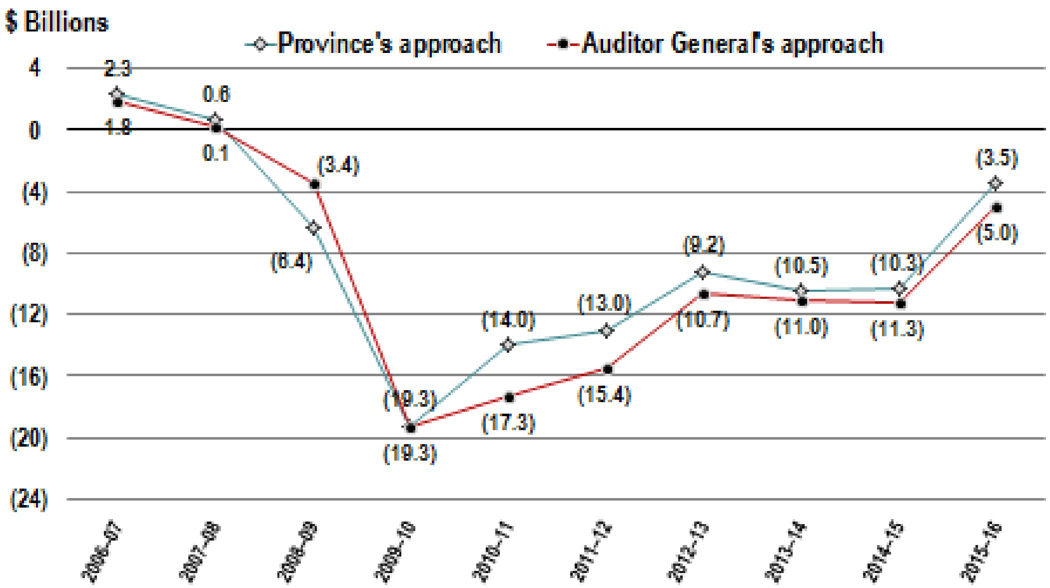
OTPP expense comparison — 10-year

Chart 1



Appendix 2: Comparison of key measurements of the Province over the prior 10 years

Surplus/(deficit) comparison — 10-year Chart 2



Appendix 6: Discount rates used by other Senior Canadian Governments and Pension Plans

Government

Ontario – LT ROR	**6.25**
Alberta – LT ROR	6.5
Saskatchewan – LT ROR	6.5
BC – LT ROR	6.5
Quebec LT ROR	6.5
NFLD – LT ROR	6.3
NS – LT ROR	7.75
MB – LT ROR	6.25

Plan - Funding

OTPP	**4.85%**
AB – Post 1992 PP	6
SK – SHEPP	NA
BC – PSPP	6.5
QC - CARRA	5.8
NFLD – MUPP	5.8
NS - NSTPP	6.25
MB - MTPP	6

Plan F/S

OTPP – MR of Prov. Bonds	***3.25***
AB TPP – LT ROR	7.0
SK – LT ROR	6.5
BC – LT ROR	6.5
QC – LT ROR	6.4
NFLD – LT ROR	5.8
NS – LT ROR	6.25
MB – LT ROR	6