Office of the Provincial Controller

# DRAFT- Ontario Teachers' Pension Plan Asset - Options

# Objective

- Identify considerations with approaching the Ontario Teachers' Federation (OTF) to negotiate changes to the Plan's terms in order to meet the Auditor General's (AG) interpretation of the standard to recognize a pension asset.

# Overview of AG concerns

- The Province and the AG have differing views of the requirement for recognition of a net pension asset of a jointly sponsored pension plan (OTPP and OPSEUPP).
- The AG believes that recognition of an asset requires:
  - a legally enforceable right to unilaterally access the asset, or in the absence of such a right;
  - an agreement in place at year-end with the Co-Sponsor which addresses reduced future contributions
- The Province considers there needs to be the expectation of benefit from the accrued pension asset through future reductions in contributions to recognize a net pension asset, and that accounting references related to surplus withdrawals are applicable.
- No issues or concerns were raised by the AG with respect to the accounting related to HOOPP and CAATPP, multiemployer plans (CAATPP had a relatively minor reported asset in 2015/16; HOOPP was in a net liability position at the end of 2015/16)
- More background discussion on the issue is included in Appendix 1.

# Context

1. The Panel's conclusions
   a) Recognition of asset:
      - » The Panel agrees that the net pension asset 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.

   b) Measurement of asset:
      - » In all analyses with different interpretations of "minimum contributions", present value of expected future accruals for service for the current number of active employees exceeds the present value of minimum contributions.
      - » No valuation allowance is required for either accrued benefit asset recognized in the Public Accounts.

# Context

2) The pension surplus/deficit and corresponding asset determined by the accounting valuation does not align with the surplus/deficit determined by the funding valuation. The partners can only make decisions regarding the funding valuation.
   - Surplus or deficit exists once a funding valuation is filed.
   - Members can use surplus to reduce contributions and/or improve benefits. The government can only reduce contributions.
   - The partners are responsible for determining how to use a surplus or address a deficit identified in a funding valuation based on the guidelines set out in the Funding Management Policy (FMP).

# Context

3) The Public Sector Accounting Board (PSAB) has established a task force to review the standards on pension plans. Should its review result in changes to the standards, these new standards would apply to the province.

# Potential Options

If it is determined that the government should implement changes to the OTPP, this could be approached in two ways:

1) Negotiate a change to the existing language in the plan terms with the OTF (i.e. the FMP)
2) Legislative changes (unilateral action that does not require OTF support)

**Note**: Each option has considerable operational and implementation issues. In addition, these options would require internal legal advice before exploring any further to evaluate the risk and impact of any potential legislative change.

# Considerations

- TPP is managed by the Partners' Committee
  - The Board members are appointed jointly by the partners.
  - Decision on funding of deficits and application of surplus is jointly made in accordance with the FMP.
  - Both Partners and the Board are required by the governance structure of the plan to work towards a common purpose, a fundamental reason why the plan is the best managed and best funded in the public sector. For example:
    - The partners must annually determine the extent of indexation that the plan will provide, based on its funded status; and
    - The Board determines the discount rate that is used to establish the funding level.

# Considerations

- The AG has suggested that the government requires unilateral access to surplus before it can report an asset.
  - This fundamentally changes the existing governance where partners focus on the plan, as a whole, rather than an individual amount.
- It is likely the OTF will expect similar unilateral access to surplus and/or changes to the portion of CIP that is currently not matched by the government.
- This would change how the two Partners interact with each other and could affect each Partner’s decision making with respect to the plan overall.
  - If each sponsor is motivated by its own “unilateral rights”, there is less incentive to consider their common purpose.
- This would also impact the way the Board interacts with the Partners.

# Risks

- Stakeholder risk
  - The Ministry of Education is currently engaged in negotiations with the teachers' federations on two fronts:
    1) Negotiating a 'remedy' in response to the Superior Court decision against the Crown related to the Putting Students First Act (PSFA), 2012 Charter challenge.
    2) Negotiating extensions to the current collective agreements.

- Negotiating or legislating change to the pension plan terms could adversely impact these on-going negotiations and compromise the ministry's ability to deliver on these key priorities for the government.

# Risks

- Risk of negotiating pensions as part of labour negotiations.
  - Currently, pension issues are negotiated between the government and the OTF (with affiliate representation).
  - Recent negotiations have been very civil between government and the OTF and there is risk that if drastic changes are forced upon the OTF, conversations could become more adversarial and could also result in pension issues being negotiated as part of labour negotiations.

# Risks

- Reputational risk
  - The OTPP attracts and retains high performing executives, staff and Board members with extensive experience in a wide range of disciplines required to oversee a complex pension plan.
  - Over the past ten years, the OTPP has had the highest total returns of the biggest 330 public and private pension funds in the world. The main factors behind the success and high performance of the Plan are strong governance and competitive salaries.
  - Depending on the scope of legislative changes being considered, there may be potential impacts on the Plan's existing governance structure and the long term sustainability of the Plan's recruitment and retention strategy.

# Risks

- Timing risk
  - The most recent review of the FMP lasted almost three years (2012-2015).
  - If all parties agree that a review is required, a committee could be assembled by the sponsors to evaluate the impact of potential changes while ensuring the Plan's long-term sustainability.
- It is unlikely the government could either have an agreement with employee sponsors on "unilateral right" before March 31, 2017, or introduce legislation to that effect without, at a minimum, a constitutional and / or legal challenge from employee sponsors or other stakeholders, such the Board and other beneficiaries of the plan.
  - As such, the same accounting issue will likely repeat for the upcoming budget, based on the AG's opinion as stated in her September 13 letter.

## Appendix 1: Background of issue

- 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
- 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. Since 2001-2002, the Province has recorded its portion (50%) of the pension assets of OTPP and OSEUPP in accordance with public sector accounting standards.

# Appendix 1: Background of issue (continued)

- OTPP and OPSEUPP meet the definition for joint defined benefit plans as the sponsors are jointly responsible for decision making, share in contributions, and collectively address any plan funding surplus/deficit. Sponsors can be said to have equal opportunity to benefit from surplus utilization through the negotiation process. Unilateral control is not necessary for asset recognition (as also seen with government partnerships); shared control is appropriate for a JDBP.
- Reporting the pension assets reflects 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. Uncertainty relating to pension surpluses relates to measurement, not uncertainty regarding expected future benefits for the Province.