Ontario Teachers' Pension Plan sponsors to file fully-funded valuation with regulators

Surplus funds to be held in reserve

The Ontario Teachers' Pension Plan (the plan) is fully funded for a seventh consecutive year, underscoring its long-term financial health and sustainability.

As such, the plan's sponsors, Ontario Teachers' Federation and the Ontario government, have decided to file the January 1, 2020 valuation with the regulators. The surplus will be classified as a contingency reserve.

The sponsors' decision to classify the surplus as a contingency reserve is intended to reduce volatility in the funded position of the plan and facilitate stability in members' contributions and benefits.

HIGHLIGHTS

- **The $6.1 billion preliminary funding surplus as of January 1, 2020 will be classified as a contingency reserve.**
- **This year's filing has no impact on members' contributions and benefits:**
  - **> 2020 contribution rates will remain at 10.4% of earnings up to the Canada Pension Plan (CPP) limit and 12% of earnings above the CPP limit (or 11% on average).**
  - **> The January 1, 2021 cost-of-living increase for all pension credit will remain at 100%.**

QUESTIONS YOU MAY BE ASKING

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Q: IS MY PENSION SECURE?

A: Yes, your pension is safe and secure.

While the fund is likely to be affected by current markets, Ontario Teachers' Pension Plan Board (Ontario Teachers') is well positioned to navigate them. By sticking to their fundamentals, including strong liquidity, aligned partnerships and first-class talent, Ontario Teachers' will continue to deliver on their goals of first-class service and retirement security for you over the long-term.

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Q: WHAT WILL THE CURRENT ECONOMIC DOWNTURN CAUSED BY COVID-19 MEAN FOR PENSIONS?

A: Members can rest assured that there's no current impact on pension payments. Retired members will continue to receive pension payments as scheduled. Pension income is based on your earnings and service in the plan.

Also, with the decision to file the January 1, 2020 valuation, there will be stability in contribution and benefit levels at least until the next valuation is filed. The next valuation will not need to be filed until January 1, 2023.

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Q: HOW DID THE 2020 PRELIMINARY SURPLUS ARISE?

A: The key factor that led to the 2020 preliminary surplus is that plan assets grew faster than liabilities (the cost of future pensions) due to a strong 10.4% total-fund net return in 2019.

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Q: WHY IS THE SURPLUS BEING CLASSIFIED AS A CONTINGENCY RESERVE?

A: Classifying the surplus as a contingency reserve is beneficial for plan members because it facilitates greater stability of contribution rates and benefit levels in case a future filed funding valuation shows a decline in assets or an increase in pension costs. In essence, classifying the surplus as a contingency reserve is a way of "saving for a rainy day."

It's aimed at keeping the plan fully funded with "base provisions" as referred to in the Funding Management Policy – meaning an average contribution rate of 11% and full inflation protection on all pension credit.

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Q: WHY DID THE DISCOUNT RATE DROP FROM LAST YEAR?

A: Ontario Teachers' is facing imposing headwinds. Even before the onset of the COVID-19 pandemic, Ontario Teachers' board recognized after years of strong financial market returns, the threat of an economic downturn was very real and the long-term return on assets is likely to be lower than recent history.

With these factors in mind, for the first time since 2016, Ontario Teachers' board decided to lower the real discount rate to 2.60% from 2.75%. This was seen as a prudent decision, particularly given the maturing demographics of the plan's membership, extremely challenging investment environment and in light of the recent impact of the COVID-19 pandemic on financial markets.

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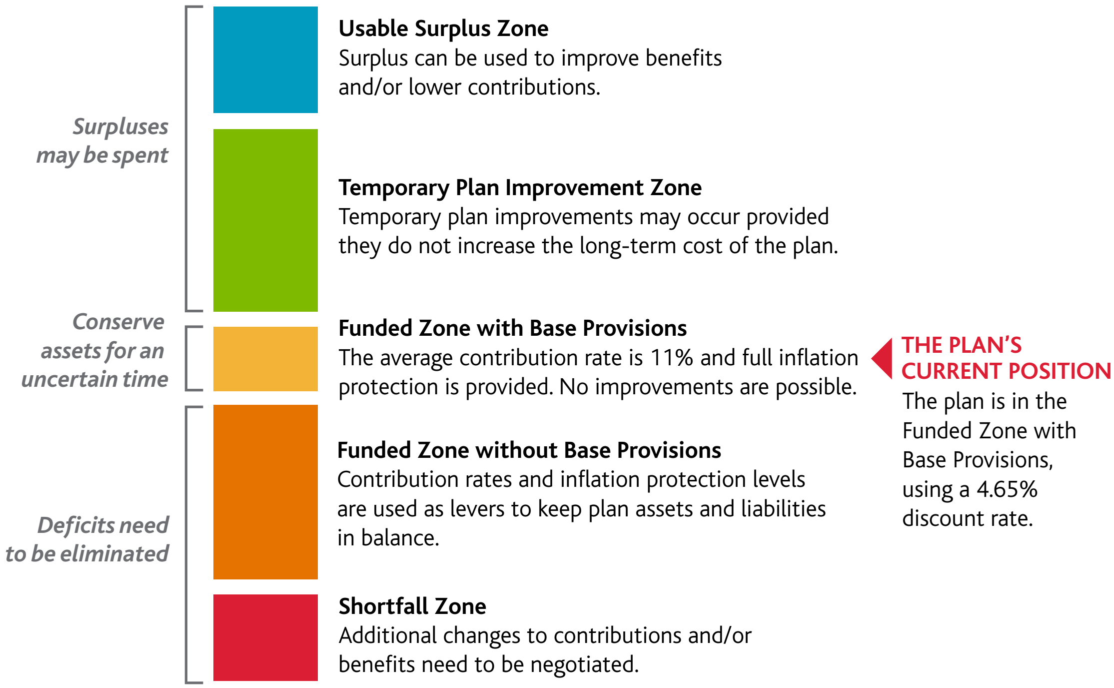
Q: WHAT'S THE ROLE OF THE FUNDING MANAGEMENT POLICY?

A: In 2003, the sponsors adopted a Funding Management Policy (FMP). The FMP provides the sponsors with a guidance framework for decision making when there's a funding surplus or shortfall.

The guidance framework in the FMP is robust, transparent and based on strong actuarial and economic principles. These mechanisms have been utilized by the sponsors for many years, providing guidance in their decisions related to valuation filings. The FMP framework has proven to be very effective and has contributed to the current strong position of the plan.

A key component in the FMP is 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. If action is required, guidance is provided on how to use any surplus funds or resolve any shortfall. Specifically, the FMP helps answer the question – when is it possible or necessary to increase or decrease benefits, lower or raise contribution rates, or simply conserve assets for an uncertain time?

Funding Management Policy Zones



During 2012 through 2018, the focus of the sponsors was to return the plan gradually over time to be fully funded with base provisions – an average contribution rate of 11% and full inflation protection on all pension credit. Since January 1, 2018, the plan has been providing base provisions to all members. As of January 1, 2020, the plan remains in the "Conserve assets for an uncertain time" funding zone within the FMP. This means that any surplus funds are reserved to facilitate stability in contribution and benefit levels.

While the FMP outlines preferred mechanisms associated with its various funding zones, it's ultimately the sponsors' responsibility to decide which actions to take.

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Q: DOES THE 2020 PRELIMINARY SURPLUS MEAN THE PLAN'S PAST FUNDING SHORTFALLS ARE OVER?

A: Shortfalls could happen in the future, however, financial levers available to the sponsors help manage the plan's funding status. Sponsors can adjust benefits and/or contribution rates, or utilize conditional inflation protection, if needed to keep the pension plan in balance.

That balance continues to be challenged by numerous factors, including member demographics, a low-growth environment, climate change, highly competitive investment markets and now the COVID-19 pandemic. There can be no assurance of high returns in this complex and rapidly changing investment environment.

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Q: IF THERE'S A DEFICIT IN THE FUTURE, CAN WE USE THE RESERVE TO BALANCE THINGS OUT?

A: A future deficit could occur if assets are outweighed by liabilities on a future valuation date. Reserving the surplus at this time makes it available for investing and earning returns, helping to protect the fund against future deficits. In other words, it's a preventative measure against future deficits occurring, not a cure should one occur in the future.

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Q: HOW DO YOU DETERMINE HOW MUCH INFLATION PROTECTION TO PROVIDE?

A: When the plan has a funding shortfall, smaller cost-of-living increases help to bring the plan back into balance. When there's a funding surplus, inflation levels may be partially or fully restored.

Pension credit earned before 2010 is 100% protected against inflation. Annual cost-of-living increases for pension credit earned after 2009 are conditional and depend on three factors:

1. Annual changes in the cost of living, as measured by increases in the Consumer Price Index (CPI).
2. The plan's funding status, which is used to gauge how much of the CPI increase the plan can afford to provide.
3. When you earned your pension credit.

Inflation Protection Levels

PENSION CREDIT	ALLOWABLE LEVELS*	CURRENT LEVELS*
Earned before 2010	100%	100%
Earned during 2010-2013	50% to 100%	100%
Earned after 2013	0% to 100%	100%

* Percentage of annual cost-of-living increase, based on changes in the CPI

The current 100% inflation level will remain in effect at least until the next funding valuation is filed with the regulators. A funding valuation must be filed at least once every three years.

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IMPACT ON YOUR PENSION

To see how inflation increases affect your annual pension each year, sign in to your Ontario Teachers' online account. The information will be available online in late October, shortly after the annual inflation rate is determined for the following calendar year. Visit this page to register for or sign in to your Ontario Teachers' account: www.otpp.com/members

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Q: WHY WILL SOME GENERATIONS OF MEMBERS RECEIVE DIFFERENT BENEFITS THAN OTHERS?

A: Pension plan provisions change over time and no generation of teachers has received exactly the same benefits as the one before or after it. For example, inflation protection wasn't provided automatically until the mid-1970s, and many older members didn't have an opportunity to retire at an 85 factor or receive a 10-year pension guarantee.

Keep in mind that Ontario's Pension Benefits Act protects the value of pension benefits already earned by working and retired members.

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Q: CAN A MEMBER MAKE ADDITIONAL CONTRIBUTIONS TO THE PLAN?

A: No, contributions to the plan are based on a percentage of salary. The plan isn't set up to take additional contributions from members to improve their benefits.

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MORE INFORMATION

- Visit the pension plan's website at www.otpp.com/funding
- Talk to your affiliate pension representative(s)