Funding **Policy – RCA**

ACTUARIAL SERVICES

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OVERALL PRINCIPLES

Funding is a joint responsibility of the OMERS Administration Corporation (“AC”) and the Sponsors Corporation (“SC”). This Policy sets out funding objectives and identifies risk factors and risk management mechanisms to deliver on the pension promise.

The Policy also sets out the protocols for the preparation of actuarial valuations, related calculations, annual projections and the determination of the Allocation Threshold and for selecting and monitoring actuarial assumptions.

This Policy applies to the funding of the Retirement Compensation Arrangement for the OMERS Primary Pension Plan (“RCA”).

Next renewal date:	March 2023
Frequency of review:	3 years

Context

The RCA provides the same pension benefits as the Primary Plan but in excess of the Primary Plan’s maximum levels, which are imposed by the ITA. Governed by the *OMERS Act, 2006* and the ITA, the RCA is a separate trust arrangement that is not registered as a pension plan under either the PBA or the ITA.

One-half of every dollar of contributions and realized investment earnings (including interest and dividends, where applicable) are required to be deposited into CRA’s non-interest bearing Refundable Tax Account. The remaining assets in the RCA Fund are invested in accordance with its *Statement of Investment Policies and Procedures* (“RCA SIP&P”).

The funding of the RCA takes into account this context and:

- AC’s fiduciary responsibilities as administrator of the RCA and trustee of the RCA Fund;
- AC’s investment principles for the RCA as captured in the RCA SIP&P; and
- SC’s *Statement of Plan Design Objectives and Strategy for the Retirement Compensation Arrangement for the OMERS Primary Pension Plan* (“RCA SPDOS”).

Funding Responsibilities

The RCA is funded by equal member and employer contributions, based on contributory earnings in excess of the Allocation Threshold (discussed below), and taking into account the investment earnings on the RCA Fund.

Funding is a joint responsibility of AC and the SC.

AC’s responsibilities under the *OMERS Act, 2006* include:

- asset allocation and investment management;
- establishing a funding policy;

- appointing the external actuary;
- providing for the actuarial valuation;
- determining the actuarial assumptions and methods based on the recommendations of its external actuary; and
- providing reasonable technical support to the SC, including estimates of the impact of any proposed plan changes.

In addition, under the Memorandum of Understanding between AC and the SC, AC is also responsible for providing cash flow projections and approving the annual actuarial valuation prepared by its external actuary.

The SC's responsibilities under the *OMERS Act, 2006*, as they pertain specifically to the RCA, include:

- determining the design for benefits;
- setting contribution rates; and
- establishing or changing a reserve to stabilize contribution rates.

The RCA SPDOS provides the approach for the determination of contribution rates, the design of benefits and the establishment of the Allocation Threshold.

Funding Objectives

The SC's principal funding objective is to ensure the continuing health and long-term viability of the RCA, taking into consideration:

- the appropriate balance between competing funding objectives, particularly with respect to concepts such as equity, sustainability, security of benefits and cost;
- the RCA's tax treatment, including the amounts recorded in the Refundable Tax Account;
- the size of the RCA's obligations relative to those of the Primary Plan; and
- any funding flexibility that is available between the RCA and the Primary Plan.

The RCA is not subject to the minimum funding standards under the PBA. Given the tax treatment of the RCA Fund, the RCA is partially funded, operating on a modified-pay-as-you-go basis.

The funding target as established by the SC is to ensure the existing RCA Fund, projected contributions and investment earnings are sufficient to pay for benefits and expenses for a period of 20 years following each valuation date. The funding target is reviewed and revised as appropriate by the SC. Where appropriate, AC shall provide to the SC its views on the funding target.

Mechanism to Achieve Funding Target

To achieve the funding target, total contributions received each year are allocated between the Primary Plan Fund and the RCA Fund in accordance with the Allocation Threshold. The Allocation Threshold is the level of contributory earnings below which the related contributions are directed to the Primary Plan Fund and above which the related contributions are directed to the RCA Fund. In accordance with SC By-Law 24-01, the Allocation Threshold is constrained to fall between a lower limit and an upper limit.

The Allocation Threshold is set each year by the SC, based on calculations by the AC external actuary.

Funding Risks

If the Allocation Threshold is constrained by the lower limit imposed by SC By-Law 24-01, the RCA Fund would be allocated contributions less than the amounts necessary to achieve the 20-year funding target.

This risk to achieving the 20-year funding target would result primarily from a prolonged decline in overall contributions collected if there are:

- a significant reduction in contribution rates as set by the SC;
- a decline in active RCA membership; and/or
- employers leaving OMERS.

As the plan matures, unfavourable plan experience that leads to higher than expected benefit payments and adverse investment experience will place a larger burden on a shrinking active contributor base. Unfavourable plan experience could result from:

- unexpected increases in contributory earnings, particularly late in members' careers;
- unanticipated improvements in life expectancy and other negative plan experience different from actuarial assumptions, both in the short and long term;
- terminating members electing a commuted value transfer, if permitted, rather than a deferred pension; and
- adverse behaviours by employers and members, such as exercising a plan feature at the expense of all other employers and members.

Other funding risks include reputational, legislative, regulatory and political uncertainties.

Understanding that the funding target and methodology to achieve the target are the responsibility of the SC under SC By-Law 24-01, in the event that circumstances indicate that the funding methodology presents a material increase in the risk to the continuing health and long-term viability of the RCA, AC will advise the SC of the AC's fiduciary concerns.

Funding Risk Management

Funding risks are monitored and managed through a coordinated process involving a variety of protocols:

- **Actuarial** – annual actuarial analysis provides information about the RCA's projected future cash flows and fund balance over successive 20-year time horizons and under various economic and demographic scenarios.
- **Contribution and Benefit** – contributions and benefit design are varied to the extent that the Allocation Threshold falls below the lower limit.
- **Investment** – taking into consideration the taxation of the RCA Fund, investment strategies and policies are developed to achieve a return that reflects an acceptable amount of risk and contributes to meeting the 20-year funding target.
- **Other** – including monitoring, influencing and responding to the legislative, regulatory and political landscapes.

Contribution and benefit protocols are addressed under RCA SPDOS, while investment protocols are addressed under the RCA SIP&P. The balance of this Policy addresses actuarial protocols.

Actuarial Protocols

Actuarial assessments shall be conducted with the following basic principles:

- compliance with all relevant legislation and professional standards and requirements; and
- long-term viability of the funding objectives shall not be compromised for short-term objectives.

Actuarial assessments comprise primarily the following:

- annual actuarial valuation for financial reporting purposes;
- annual actuarial projections including the determination of the Allocation Threshold;
- periodic review of actuarial assumptions and methods and work performed by AC's external actuary; and
- actuarial analysis of proposed plan changes.

Annual Actuarial Valuation

An actuarial valuation shall be performed as at December 31 each year:

- the actuarial valuation shall be performed on a going concern basis;
- the going concern actuarial valuation shall be performed using the projected unit credit actuarial cost method and the reported value of the RCA Fund;
- both demographic and economic assumptions used for the going concern actuarial valuation should be set based on relevant emerging experience of the RCA and the Primary Plan (since members of the RCA are also members of the Primary Plan) and should reflect expectations of the broader economic environment. Other than the real discount rate assumption, actuarial assumptions represent the best estimate of the most likely outcomes of future events; and
- the methodology to determine the real discount rate assumption, set as at July 1 prior to the valuation date, should:
  - reflect the expected long-term investment return of the RCA target strategic asset mix, taking into account the impact of the Refundable Tax Account; and
  - include a margin for conservatism to maintain a stable discount rate which in turn promotes a stable progression of actuarial liabilities from year to year.

Annual Actuarial Projections and determination of the Allocation Threshold

Unless an alternate approach is deemed appropriate following a periodic review of assumptions and methods (see below), the same actuarial assumptions used for the annual actuarial valuation for financial reporting purposes will be used for the calculation of the Allocation Threshold for purposes of the funding target.

Projections of the RCA's funded status and the determination of the Allocation Threshold shall be prepared annually and should cover the following elements:

- projections of cash flows and fund balance;
- projections shall be performed over a time horizon at least 20 years or the relevant period specified in SC By-Laws;
- projections should cover different demographic and economic experience scenarios, including stress testing. The scenarios should be broad enough to cover both favourable and unfavourable experiences, with specific focus on existing and potentially new risk factors that would have material implications to the projected cash flows and fund balance; and
- projections should also cover the impact of any changes in actuarial assumptions during the projection horizon if these assumptions are under stress. Sources of gains and losses from the annual actuarial valuation should be reviewed to identify potential stresses.

Periodic Review of Actuarial Assumptions and Work Performed by AC's External Actuary

Since RCA members are also members of the Primary Plan and because the pension benefits under both plans are integrated, the periodic review of actuarial assumptions and independent reviews of the work performed by AC's external actuary should be made in conjunction with any analysis completed for the Primary Plan, as follows:

Actuarial Assumptions and Methods	Minimum Review Frequency
Discount rate assumption	Annually
Long-term inflation assumption	Annually
Other assumptions (e.g. demographic, salary increase)	Evaluated annually, comprehensive experience study at least every 5 years
Independent assessment of actuarial assumptions and methods and work performed by AC's external actuary	Every 10 years

Actuarial Analysis of Proposed Plan Changes

The funding impact of any changes to the RCA, including the impact of changes to the Primary Plan, either considered or proposed by the SC, shall be analyzed by AC using the actuarial protocols and the results submitted to the SC for its consideration.

Responsibilities

The VP, Actuarial Services and Plan Actuary is responsible for:

- providing direction to the oversight of, and to the coordination of the work performed by, AC's external actuary; and
- preparing actuarial analysis.

AC's external actuary is responsible for:

- performing the annual actuarial valuation and providing the independent actuarial opinion and certification for funding and financial statement reporting purposes;
- calculation of the Allocation Threshold;
- recommending the actuarial assumptions and methods;
- providing official cost estimates for plan design changes; and
- conducting special projects such as experience studies.

Exceptions

The Policy Sponsor may grant non-substantive exceptions to this Policy but shall report such exceptions to the AC Board in writing.

Responding to Incidents of Non-Compliance

The Policy Manager is accountable for identifying incidents of potential non-compliance under this Policy based on established procedures, and reporting such incidents to the Policy Sponsor.

Monitoring and Reporting

The Policy Manager is responsible for administration of the Policy, including implementing procedures to enable compliance, monitoring and reporting, as well as to coordinate training as required.

Documents related to this Policy

- Memorandum of Understanding – describes the roles of the SC and AC in the OMERS Plan Funding Process;
- RCA SIP&P – sets out how the assets of the RCA Fund are invested by AC;
- RCA SPDOS – sets out the approach for the determination of contribution rates, the design of benefits and the establishment of the Allocation Threshold; and
- SC By-Laws – set out determination of the Allocation Threshold.

ROLES & RESPONSIBILITIES

Policy Approver	AC Board of Directors	Responsible for approving the Policy
Policy Sponsor	Chief Financial and Strategy Officer	Ultimately accountable for the Policy, including its development, implementation and administration
Policy Manager and Monitor	VP, Actuarial Services and Plan Actuary	Responsible for the design and operational effectiveness of the day to day administration of the Policy and for the monitoring, compliance and reporting functions of the Policy