

THE GIFT ANNUITY PROGRAM OF THE UNITED CHURCH OF CANADA FUNDING POLICY

1. Overview

The United Church of Canada (UCC) sponsors a gift annuity program whereby donors enter into a contract for a gift annuity product with the UCC. The gift annuity product provides a fixed level periodic annuity payment payable for the lifetime of the annuitant (and their survivor) with the remaining account balance payable, upon the death of the annuitant, as a gift remainder to the beneficiary of the contract, notably the UCC, its General Council Office or other recipients which may or may not form part of the National Accounts of the UCC. The annuity contracts are irrevocable. The standard wording guarantees that the annuity payments will be made and the contracts are priced using the basis recommended by the Canadian Charitable Annuity Association (CCAA). Membership in the CCAA also confers on the UCC the obligation to perform a triennial valuation of the gift annuity program by a qualified fellow of the Canadian Institute of Actuaries (CIA).

The gift annuity program at UCC consists of assets which, together with the expected investment return on those assets, are expected to be sufficient to provide for all future guaranteed annuity payments, all future gift remainder payments and all future costs of administering the gift annuity program.

This funding policy sets out the expectations for the funding and valuation of the UCC gift annuity program.

2. Funding Objectives

This funding policy, being established in 2025, is being set so as to ensure that the assets of the gift annuity program are sufficient to meet the obligations of the program and to ensure the sustainability of the program for the foreseeable future. A secondary objective of the funding policy is to encourage good governance of the program.

The Executive of the General Council has deemed it to be desirable that the funding objective be managed such as to achieve a target level of at least 115% of the actuarial liabilities determined for the program, with a minimum acceptable funding level of 95%.

Section 4 (below) of this funding policy sets out the valuation expectations for the UCC gift annuity program, including the establishment of reasonable margins against unexpected risks and contingencies. The funding objectives are deemed to be met when the assets of the gift annuity program meet or exceed the valuation objectives set out below.

3. Risks Faced by the UCC Gift Annuity Program

There are a variety of risks faced by the UCC gift annuity program. These include

- (a) fluctuations in future investment returns for the gift remainders or in the interest rates used to determine the discount rates for the liabilities;
- (b) investment risk may also arise due to mismatch between the cash flow characteristics of the assets and those of the liabilities;
- (c) adverse changes in mortality experience or mortality improvement (longevity risk);
- (d) inadequate provisions for future administration expenses of the program including inflation risk; and
- (e) declines in the size of the gift annuity program so as to make it unsustainable on a standalone basis.

The margins included in the valuation basis (see Section 4.3 below) are intended to cover these and other future adverse contingencies not explicitly provided for in the actuarial liabilities.

Note that pooling of investment risks with UCC treasury funds also serves to support the sustainability of the program as it provides the critical mass for access to more attractive investment options and cost efficiencies.

4. Valuation of Gift Annuities

4.1 Valuation Basis

The process, method and assumptions for valuation of the UCC gift annuity program follow the accepted actuarial practice in Canada for valuing gift annuities issued by quasi-insurers.

Specifically, they follow the CIA 2024 Educational Note entitled “Considerations in the Determination of the Actuarial Liabilities of Canadian Charitable Gift Annuities”. The UCC has determined that a valuation of the gift annuity program should be undertaken no less frequently than every three years, in accordance with the expectations of the CCAA.

The valuation approach is derived from the International Financial Reporting Standards (IFRS17) which became effective January 2023 for the life insurance industry in Canada. This valuation approach determines the present value of cash flows, taking into account all future guaranteed annuity payments, all future gift remainders payable upon death and all future costs of administering the gift annuity program. The cash flows have risk margins added to reflect uncertainty. The valuation projects liabilities over a long-term horizon which takes all future expected cash flows into consideration.

4.2 Best Estimate Assumptions

In accordance with best practice for actuarial work in Canada, the valuation includes best estimate assumptions as follows:

- (a) Discount rates used in the valuation are consistent with those developed by the CIA for the purpose of IFRS17 reporting for the life insurance industry in Canada.
- (b) The assumed mortality basis is derived from tables relevant for (gift) annuitant mortality, updated periodically or with reference to the experience of the UCC program.

- (c) Mortality improvement factors are applied based on factors derived by the CIA for mortality improvement for annuities in Canada.
- (d) Administration expenses (adjusted for expected future inflation) are derived from assessment by the UCC of the costs of administering the gift annuity program.

4.3 Margins

Projected cash flows for the annuities, gift remainders and expenses are determined with margins, at the discretion of the actuary, which are intended to represent a confidence level of 75 to 85 percentile for such cash flows relative to the best estimate assumptions determined above.

In addition to the explicit margins applied to the projected cash flows, it is recommended that an additional margin be included for the UCC gift annuity program. This additional margin is expected to allow for a greater range of potential outcomes and to ensure the future sustainability of the program. In particular the additional margin is meant to address

- (a) the absence of explicit capital requirements for the UCC gift annuity program (as is maintained by life insurers offering such annuities in Canada in accordance with regulatory expectations) and
- (b) the lack of additional margins under IFRS17 to be applied to the discount rates or the expected returns on the gift remainder component of the gift annuity program which would provide for unexpected capital market fluctuations such as interest rate movements or equity market declines.

An additional margin of 15% is being recommended for this purpose.

5. Management Action

When the assets of the program exceed the upper range of the funding objectives, the Executive of the General Council may elect one of more of the following courses of action:

- (a) Modification of the spread being applied to the asset return used to determine the gift remainders so as to restore financial equilibrium of the gift annuity program;
- (b) Withdrawal, in whole or in part, of the excess surplus in the program, for equitable (e.g. pro rata) distribution amongst the beneficiaries of the gift remainders under the program; or
- (c) Such other actions as may be deemed appropriate, with the support of the actuary valuing the gift annuity program, to restore the annuity program towards the funding objective.

It may be noted that if the assets of the program consistently exceed the funding objectives of the program, the risk of a “tontine” emerges, whereby there would be an excess residual value remaining in the program after the annuitant population has matured for which ownership would be uncertain.

Conversely if the assets of the program were to fall below the lower range of the funding objectives set out above, the Executive of the General Council may elect one or more of the following courses of action:

- (a) Modification of the spread being applied to the asset return used to determine the gift remainders so as to restore financial equilibrium of the gift annuity program;
- (b) Additional financial support to the program, to be sourced on an equitable basis from all the beneficiaries of the gift remainders under the program; or
- (c) Such other actions as may be deemed appropriate, with the support of the actuary valuing the gift annuity program, to restore the annuity program towards the funding objective.

Any actions taken to restore the financial stability of the gift annuity program would take into account the long-term impact of such action on the financial security of the gift annuitants as well as on the future sustainability of the program. Historical actions taken in this regard may also be taken into account as setting precedent for such actions, as well as any other pertinent information, on the advice of the Executive of the General Council and the valuation actuary, at the time.

When evaluating options to address either a surplus or deficit in the fund, it is important to note that the risks of the program are asymmetric between UCC and the beneficiaries. As the administrator of the program, the UCC may be deemed to bear an additional responsibility for any financial support required if the assets of the program fell below the lower range of the funding objectives, given that it has more direct control over the sound financial management of the program. Conversely, it may be reasonable for UCC to benefit more than other beneficiaries for any surplus arising due to the assets of the program exceeding the upper range of the funding objectives.