PRI Technical Basis

The technical basis for calculating an employer's pension liability under the ITP2 plan, when the employer uses the book reserve method, is set by Pensionsregistreringsinstitutet PRI, ideell förening (The Pension Registration Institute, a non-profit association). This follows from the ITP2 collective agreement between Svenskt Näringsliv and PTK (Confederation of Swedish Enterprise and The Council for Negotiation and Cooperation for 25 trade unions, respectively).

The PRI Technical Basis sets out how the three parts of the PRI liability must be calculated. The three parts are:

- Present value of accrued old age pension rights
- Special Indexation Reserve (Sw: "Kvarstående särskilda värdesäkringsmedel")
- Consolidation reserve

1. **Present value of accrued old age pension rights**

Accrued old age pensions rights, including indexation to pensions under payment, are calculated by Alecta, using Alecta's technical basis. This gives the same pension benefits regardless of whether the PRI book reserve method is used or pensions are secured through an insurance solution in Alecta. (Alecta is a Swedish Life and Pension Insurance Company/Institute for Occupational Retirement Provisions.)

Traditional actuarial methods are used for calculating the present values of accrued old age pension rights and use the following:

- A discount rate
- Assumptions on mortality and future operating costs
- Additional rules for calculations

1.1 Discount rate

The discount rate is 3 % per annum gross of operating costs and 2.85 % per annum net, applicable from 1 January 2022. Before the change the discount rate was 4 % per annum gross and 3.84 % per annum net.

The opinion of the PRI Association is that the use of a fixed discount rate, on a reasonable level, is the preferred method of valuing pensions, as opposed to a market-based discount rate, provided the pension is a defined benefit pension that is backed by credit insurance against sponsor insolvency and where no funding is required. A fixed discount rate removes any fluctuations in the value of the liability. Furthermore, the ability of the employer to fulfill the pension liability is not correlated to a market-based discount rate.

The Association continuously reviews the technical basis. The primary basis for setting the discount rate is the long term profitability of companies, defined as the average return on assets.

For several years, the Association's board of directors has noted that a discount rate of 4 % per annum is typically lower than the average long-term return on assets. However, in the board's annual review of statistics, the board has noted a decline in the return on assets for Swedish companies. Hence the margin between the return on assets and the discount rate of 4 % is at risk of being too small. This is the justification for reducing the discount rate to 3 % from 1 January 2022.

The discount rate can be adjusted in different ways for the Swedish capital yield tax ('Avkastningsskatt'). When deciding the approach the Association's board has been influenced by IAS 19, whereby the pension liabilities shall not take into account the investment yield tax applicable on employer's pensions liabilities or the assets in a pension foundation.

The conclusions above are only valid if the pension benefits are protected by a mandatory credit insurance against sponsor insolvency. These policies are issued in Sweden by PRI Pensionsgaranti.

1.2 Mortality assumptions
The number of individuals covered by the PRI system is sufficiently large to derive statistically credible mortality assumptions. These assumptions can be different from Swedish population mortality or the insured population mortality. Historically, different mortality assumptions from those used by Alecta have been used for calculating PRI liabilities. However, recent mortality experience has shown very close similarity between the PRI experience and the Alecta experience. The mortality assumptions in the PRI Technical Basis have therefore been aligned with the mortality assumptions used by Alecta for calculating PRI liability redemption premiums. The board will continue reviewing the mortality in the PRI population.

1.3 Future operating costs assumptions
The operating cost assumption is of less economic significance than the discount rate and the mortality assumption. It has been expressed, as discussed above, as a reduction to the discount rate. The current assumption mirrors many years of experience of the charges for operating costs for PRI Pensionsgaranti.

2. Special indexation reserve

The special indexation reserve is calculated following a framework of rules set up in a collective agreement between Svenskt Näringsliv and PTK.

This framework contains

- An interest rate that is derived from the yield on government bond

- A reduction in the reserve for the years when Svenskt Näringsliv och PTK have agreed that the reserve can be released for indexation or other purposes
- An increase in the reserve by an amount equal to a percentage of the pay-roll for salaried employees in the years when Svenskt Näringsliv och PTK agreed that such an increase shall be made.

The special indexation reserve does not relate to a pension liability. It is an obligatory reserve held on the employer’s balance sheet to ensure consistency with a corresponding reserve held on Alecta’s balance sheet (for ITP2 pensions secured through insurance).

3. Consolidation reserve

In addition to the present value of accrued old age pension rights and the special indexation reserve, PRI ideell förening, also decides on a consolidation reserve. The purpose of the consolidation reserve is to be a reserve for indexation to old age pensions. The indexation is determinedby Alecta before each year-end but is not included in the calculation of the present values at year end. From January 1, 2022, the consolidation reserve is 2 % of accrued old age pension rights. The consolidation reserve was 4 % before this change. The reduction in the consolidation reserve is justified by expectations of continued low inflation.