MPP - About the Plan—Questions & Answers

The Municipal Pension Plan is widely recognized to be well designed and well administered. It is a model for other jurisdictions interested in pension plan reform.

People are talking about pensions more often these days. You can learn more about the Plan's sustainability, cost-effectiveness, fairness and value and about BC Public Sector Pension Plans by reading these concise questions and answers (below).

The publication An in-depth look at BC public sector pension plans explains how the plans are structured and how they manage risk to deliver pension benefits on a sustainable basis from one generation to the next.

Municipal Pension Plan top five questions

1. Who pays for Municipal Pension Plan pensions?

Plan members and their employers pay by making contributions to the Pension Plan during the years the member works for a public sector employer and is a member of the Plan. These contributions are invested, and in turn, the Plan's investment income finances about 75 per cent of the cost of pensions. Contributions from members and employers make up the remaining 25 per cent.

2. What happens to contributions in the Pension Fund?

The Municipal Pension Board of Trustees invests the Plan's funds, and the returns help to pay the cost of pensions.

3. What benefits does the Plan pay?

Guaranteed basic pension — The basic lifetime pension payment (the monthly payment each retired member receives) is paid for as long as the member lives and may continue to be paid to the member's spouse or dependant after the member's death. The basic pension benefit is defined and is based on how many years of pensionable service the member has accrued in the Plan and the member's highest average salary (highest 60 months, not necessarily the last 60 months).

Cost-of-living adjustments (non-guaranteed) — Cost-of-living benefits are not guaranteed until they are granted. Once granted, they become part of the basic pension. This benefit is available at the discretion of the Board and provided there are sufficient funds in the Plan's Inflation Adjustment Account. The Board of Trustees annually considers whether to grant a cost-of-living adjustment.

Post-retirement group benefits (non-guaranteed) — Retired members have accessto extended health care and dental plans at group premium rates that typically are more affordable than individuals could purchase on their own. Retired members may be eligible for a subsidy.

4. How does the Plan ensure there will be enough money?

Every three years, the plan actuary conducts an actuarial valuation to determine if the plan is sufficiently funded. If this valuation determines that there will be insufficient funds to meet the basic pension promise to members, employer and member contribution rates will be increased.

5. When contribution rates are increased, who pays?

Members and employers share any contribution rate increase equally. If the actuary determines total contributions should be one per cent higher, member contribution rates increase by 0.5 per cent and employer contribution rates increase by 0.5 per cent.

BC public sector pensions top five questions

1. What kind of a pension is available to BC public sector workers?

Public sector pension plans in British Columbia provide an important component of employees' total compensation. Most public sector employers in BC offer their employees a defined benefit (DB) pension plan through the College, Municipal, Public Service or Teachers' pension plans. These BC public sector pension plans are the focus of this Q&A.

Some Crown corporations, such as WorkSafeBC, BC Hydro and the Insurance Corporation of BC, have their own pension arrangements.

2. What is a DB pension plan?

DB plans use a formula (years of service x highest average salary x accrual rate) to calculate an individual's pension. Based on this formula, the pension plan promises to pay plan members a predetermined pension for life after they retire. This allows participants to plan for retirement because they know well ahead of time the value of an important portion of their retirement income.

In other types of pension plans, such as defined contribution plans, a member's pension benefit cannot be predicted. This is because the benefit available at retirement is based on how well the member's individual investments perform over time and how much the member will receive from an annuity or other income-generating vehicle at retirement.

In addition to providing the benefit of predictability for plan members, DB plans offer advantages for employers, as they can be an effective way to recruit and retain a quality workforce.

3. How can the BC public sector pension plans be sure they can provide the pension promised to members given changing demographics and uncertain investment markets?

The BC public sector pension plans are required to meet certain funding requirements under their joint trust arrangements. Each pension plan's board is required to manage its assets to ensure there is enough money for current and future pensions.

On advice from the plan's investment manager, the boards manage plan investments to balance potential investment gains and investment risk. This helps ensure the plans remain financially sound. When an investment market downturn results in losses to the plans, as was the case in 2008, the trustees expect to recover those losses over time as the markets rebound.

Every three years, an independent actuarial valuation is conducted by the plan actuary to determine if the plan is sufficiently funded. (An actuarial valuation is an assessment of the long term financial health of a pension plan by an independent actuarial consulting firm.) If this valuation determines that there will be insufficient funds to meet the plan's basic pension promise to members, the board must increase employer and member contribution rates. The intent of this process is to keep the plan at or near a funding ratio of 100 per cent.

4. Do DB (defined benefit) plans cost more than DC (defined contribution) plans?

Public sector pension plans are efficient and well administered. There would be similar costs for any type of employer-sponsored pension plan. Most of the other costs to administer the plans are borne by the plans themselves and are paid from the plans' assets.

The large scale and professional management of the BC plans, for example, enables them to operate very efficiently. There is also a case to be made that DB plans can provide similar benefits for less money than other types of pension plans because they allow the sponsors to pool risk and purchasing power[1]. According to one U.S. study[2], the cost is 46 per cent lower for DB plans.

There is also evidence that the investment returns of DB plans generally outperform the returns of other types of pension plans, likely because DB plans are "perpetual investment pools" that can be truly managed over the long term[3]. As a DB plan's operating costs are typically paid from its assets (which consist largely of investment income), a case could be made that better investment returns in DB plans provide more funds to offset the administrative costs for these plans.

The BC public sector pension plans pay 70 to 80 per cent of the cost of pensions through investment returns.

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[1] Donald E. Fuerst, Mercer Human Resource Consulting, "Defined Benefit Pension Plans: Creating Value for Employees and Employers"

[2] National Institute on Retirement Security, "A Better Bang for the Buck—The Economic Efficiencies of Defined Benefit Pension Plans"

[3] Stephen P. McCourt, "Defined Benefit and Defined Contribution Plans: A History, Market Overview and Comparative Analysis," *Benefits and Compensation Digest*, Vol. 43, No. 2, February 2006

5. Where does the money come from to pay for public sector pensions?

Both employers and employees contribute to the plans, and their contributions are invested. The plans' investment income finances about 70 to 80 per cent of the benefits paid to members. Contributions from members and employers make up the remaining 20 to 30 per cent. Each generation pays in advance for its own pension benefits, and employers and employees equally share the risks associated with funding the defined benefit portion of the plans.