



# Municipal Pension Board of Trustees

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January 31, 2019

Michael Puskaric, MBA, CPA, CMA  
Director  
Public Sector Accounting Board  
277 Wellington Street West  
Toronto ON M5V 3H2

*via email: info@psabcanada.ca*

Dear Michael Puskaric:

**Subject: Submission re Employment Benefits: Non-traditional pension plans**

Further to our letter dated March 9, 2018, I am writing on behalf of the Municipal Pension Board of Trustees (the Board) in response to the Public Sector Accounting Board's (PSAB) call for public comment on the third and final consultation in the review of the retirement benefits section of the PSAB Accounting Handbook. Thank you for the opportunity to comment.

**About the Municipal Pension Plan (MPP or plan)**

The Municipal Pension Plan (MPP or plan) is the largest pension plan west of Ontario, with more than 300,000 members and more than 900 employers participating from the health, local government, education and community services sectors. Our plan alone represents more than 30% of all members of pension plans registered in BC, and approximately 1/3 of all pension assets (approximately \$50 billion) in the province. As a large plan provider, we strive to be an industry leader and an effective participant in the pension industry.

We are a multi-employer, contributory, defined benefit pension plan governed by a joint board of trustees. The board is fully responsible for the administration of the plan and investment of the fund.

Our participating public sector employers have no formal claim to any pension plan surpluses. In the event of an unfunded liability, both plan members' and plan employers' contributions will be increased equally to amortize the cost of the deficit. In this manner, unfunded liabilities are short term and contributions maintain the plan's fully funded status over time. We are proud to say that we are fully funded on a going concern basis, after allowing for the value of previously established amortization requirements to address going concern unfunded liabilities at prior valuations.

We understand that this phase of your project focuses on how public sector entities should report their share of the risk and costs of accrued pension liabilities, in light of evolving pension plan designs. As a funded pension plan, we do not follow PSAB standards. We use the Pension Accounting Standards as set out in Part IV of the CPA Handbook.

However, the PSAB standards are applicable to many of the employer entities who participate in the MPP. As participants in a multi-employer public sector pension plan, MPP employers record the contributions they make to the MPP as a pension expense in their own financial statements; they do not directly record any future obligation for pension liabilities in their financial statements. This practice follows the PSAB's defined contribution pension plan accounting requirements, and aligns well with our model of plan governance, where participating employers and members share the responsibility for plan governance.

In the unlikely event that the plan is wound up tomorrow, there is no entity or group of entities legally obliged to fund any shortfall. If a shortfall existed at the time of a wind up, benefits might need to be pro-rated. More specifically, the plan's trust agreement provides that, in the event the plan is terminated in its entirety, the plan sponsors will determine what happens if there is an unfunded liability. It reads as follows:

*If the assets in the Pension Fund as of the date of termination are insufficient to make full provision for all entitlements to receive a pension in respect of the Plan Members' membership in the Pension Plan to the date of termination, such shortfall will be dealt with in the manner as is then agreed to by the Signatories.*

Further the plan's trust document explicitly provides the following:

*Without limitation, no Plan Member, Employer, Signatory or union or association that represents any of the Plan Members shall be liable or responsible for any debts, liabilities, obligations or deficiencies of the Board, the Pension Plan or the Pension Fund.*

In our view, requiring employers participating in our plan to report in their financial statements any portion of the plan's liabilities would be misleading; it would materially misrepresent the financial position, liabilities and obligations of the reporting entity. It continues to make sense for our participating employers to report their current year pension contributions, following the defined contribution method.

### **Invitation to consult (ITC)**

The PSAB consultation document seems to suggest that employers participating in a multi-employer jointly sponsored pension plan, such as those participating in the MPP, change from reporting their pension expenses from the defined contribution method to the defined benefit method. Further the consultation suggests that the accumulated benefit obligation should

include contingent and constructive contributions and benefits. All three of these suggestions would be very challenging for our participating employers.

First, the plan does not have a method to apportion liabilities between employers. This may be a significant barrier and ultimately be unachievable. The plan records accrued liabilities and accrued assets for the Plan in aggregate, with the result that there is no consistent and reliable basis for allocating the obligation, assets and cost to the individual employers participating in the plan. We have no methodology in place to do this, and no reasonable basis on which to construct a reasonable method. We would expect this to be a major concern for all multi-employer pension plans across all jurisdictions, especially with fluctuating combinations and levels of member employment and the movement of members between employers.

Second, accounting or attempting to assign a value to future changes to future contributions or benefits as a result of a valuation at the reporting date is problematic generally. It is one thing to assign a value to a past transaction or event that has a known future impact, and something quite different to try to quantify the impact of a decision that has not yet been made.

Third, assigning a deemed value to a future discretionary benefit (e.g., non-guaranteed future cost of living adjustments that are subject to the discretion of the board at a future point in time) is problematic. There is no certainty that the benefit will be paid. Even if a benefit were to be paid, the value is highly speculative. In our plan, future cost of living adjustments are granted at the discretion of the board after taking into account some specified limits and in the context of the entire set of circumstances at the relevant time.

Further, including contingent and constructive contributions and benefits in the accrued benefit obligation (ABO) seems inconsistent with the definitions of “accrued” and “obligation.” The stated focus of the ITC is to “the projected future cash flow component of the accrued benefit obligation.” If a benefit has not “accrued” then there is no future cash flow expected and no obligation to be accounted for.

We continue to be alarmed about the idea contemplated in the second round of the PSAB consultations, namely to value assets using an arbitrary discount rate that does not reflect the plan’s investment strategy and provides members leaving the plan with a risk-free asset at the expense of members remaining in the plan.

In short, we have some serious concerns with the concepts under consideration. We are worried that if the full set of changes under consideration is implemented, the resulting financial results will not reflect a participating employer’s pension obligations fairly, will in fact materially misrepresent an employer’s financial position, and will make the employer’s financial position seem more volatile year-over-year than it actually is. This is especially problematic in a public sector environment where balanced budgets are often the norm. Such an outcome would jeopardize the long term sustainability of public sector pension plans like ours.

We struggle to understand what the underlying problem is that requires a shift in practice and guidance. As far as we are aware, legitimate users of public sector financial statements (such as credit agencies) are not concerned whether liabilities are fairly presented. What is proposed is complicated, time consuming, subjective and fraught with the potential to produce misleading information that obfuscates participating employers' financial positions. Employers are not going to be called upon to fund unfunded liabilities in our plan.

In fact, the resulting information might incent behaviours that result in unintended consequences and undermine the success of the Canadian model of pension governance. It is not a stretch to anticipate that the employer plan partner might be incented to move their participating employers' ABO in one direction and pull plan governance levers at their disposal, even though the plan is well designed and well funded. This could seriously jeopardize the future of the plan.

Likewise, public sector employers that are required to produce balanced budgets may be required to cut public services to achieve a balanced budget, when the expenses they've recorded for the accrued benefit obligation never come to pass.

The potential unintended consequence of these proposed changes is the creation of public entity financial statements that are less meaningful, less transparent and less reliable to users. Our responses to the specific questions posed in the consultation paper are attached. Thank you again for the opportunity to provide comment on the PSAB Employment Benefits: Non-traditional pension plans.

Sincerely,



Gary Yee  
Board Chair

cc: Hilary Brown, Board Vice Chair  
Judy Payne, Executive Director  
Irene Schamhart, Board Secretary

Enclosure

**Municipal Pension Board of Trustees**  
**Response to PSAB Invitation to Consult**  
**Employment Benefits: Non-traditional Pension Plans**

In response to the specific questions posed by your consultation, we would respond as follows:

***Need for update of accounting guidance***

1. *Do you agree that there is a need to review and update Section PS 3250 to address plans that involve employers sharing different degrees of risk related to pension benefits with other parties (paragraphs .065-.081)?*

- We agree there is a need to review and update Section PS 3250 to include target benefit plans.
- We also support the notion that accounting standards for employee benefits could better reflect the nature of shared risk and multi-employer realities of many non-traditional plans.
- We take exception with the conclusions drawn in paragraph .078. Employers that participate in the MPP have an obligation to make the required contributions; they assume no responsibility for an unfunded liability, which essentially belongs to the plan in our joint trust model.
- Why is comparability of financial statement for public sector employers participating in single-employer or multi-employer defined benefit plans an over-riding objective? The underlying risks and obligations in pension plans can be very different. Overly simplifying the distinctions between the plans does not improve financial reporting or comparability.
- We are unclear on the problem trying to be solved. Which group of end users is having difficulty with the current approach? Credit rating agencies who have a need to understand a public sector employer's obligations do not seem to have any difficulty in determining credit risk in the public sector.
- If PSAB implements equivalent standards similar to those issued by other standard setters, then it is imperative that PSAB approve the exception where insufficient information is available to use defined benefit accounting.

***Accounting issues arising from developments in public sector pension plans***

2. *Are there any developments in the landscape of public sector pension plans that may require accounting guidance that have not been identified in this Invitation to Comment (paragraphs .009-.019)?*

- The jointly sponsored multi-employer model is almost unique to Canada and justifies treatment different from other jurisdictions. The independence of Canadian jointly sponsored public sector pension plans is well established, and is held out as a model worldwide for jurisdictions to aspire to.<sup>1</sup> This independence means that instead of treating public pension plans as extensions of government (with obligations directly to plan beneficiaries) the plans should be treated as the entity with the obligations to beneficiaries.

3. *Are there any plan features that may have accounting implications that have not been identified in this Invitation to Comment (paragraphs .020-.050)?*

- We are a contributory pension plan, and our members make almost half of all contributions to the plan. In the event of an unfunded liability, the board raises contributions for members and employers equally.
- We understand that paragraph .014 of the existing PSAB 3250 covers the treatment of a pension plan with both defined benefit and defined contribution entitlements. This existing section goes on to state that an entity would determine the defined benefit component of the ABO using the defined benefit accounting guidance and the defined contribution component using the defined contribution accounting method. This provision should be retained. The general principle for accounting for and recognizing different entitlements differently should continue.
- The termination and wind-up provision of each plan should be considered. Our plan is not required to follow provincial legislative requirements for wind-up and we are not required to prepare a solvency valuation.

***Potential accounting guidance***

4. *Do you agree that an expanded classification approach is not a viable option to address the accounting for all types of public sector pension plans (paragraphs .072 and .090)? If you disagree, what classifications:*

- (a) would capture all types of public sector pension plans; and*
- (b) can be practically and conceptually differentiated from each other?*

- Without taking a position on the question, we don't believe moving to the proposed two classification approach is appropriate. It is overly simplified and does not reflect the unique structures and risks within our plan. Paragraph 110 should be retained to allow employers participating in multi-employer pension plans to continue using defined contribution accounting.

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<sup>1</sup> See "The Evolution of the Canadian Pension Model: Practical Lessons for Building World-class Pension Organizations", 2017, International Bank for Reconstruction and Development / The World Bank which speaks to how the Canadian independent governance model for public pension plans is held out as best practice worldwide.

- Recognizing that the breadth of pension plan design is limited only by the terms included in the governing trust documents, it may be difficult to design a categorization system that accurately classifies plans. Perhaps a more flexible principle-based method would be preferable.

5. *Do you support a simple two-classification approach (paragraphs .093-.096)?*

- No, not unless the effect is to preserve the status quo for public sector entities participating in multi-employer pension plans. It is overly simplified and does not reflect the unique structures and risks within our plan. Paragraph 110 should be retained to allow employers participating in multi-employer pension plans to continue using defined contribution accounting.

6. *Do you agree that PSAB should further develop the potential guidance discussed in this Invitation to Comment (paragraphs .097-.155)? If yes, are there any specific areas that the Board should further develop?*

- If the PSAB decides to depart from the current guidance, then yes further guidance is required.
- More specifically, we believe guidance is required to clarify that where a public sector entity participating in a multi-employer pension plan has no obligation to fund the ABO apart from continuing to make required contributions, then their “share” of the obligation is zero. Further, employers participating in our plan should continue to be classified as multi-employer and jointly sponsored for accounting purposes, and continue to use defined contribution accounting. An exemption should be provided to those public sector entities that cannot determine their share of the ABO; a paragraph to this effect, similar to that used in the international accounting standards, should be included. There is no feasible way for our plan to segregate liabilities by employer, when we do not segregate assets.
- For clarity, where government is not responsible for the plan’s debts or obligations, then it should be clearly stated that it is not a sponsoring entity. In our plan, the provincial government is one of the settlors of the trust, but they explicitly have no obligation for plan liabilities. It would be inappropriate to require them to record any share of the plan’s ABO.
- Similarly, it will be important to clarify how other public sector entities with affiliated entities are to account for ABOs. In our plan, we have some participating employers in the health and local government sectors with affiliated entities; while we believe none of our participating employers have an ABO, the standards should provide guidance on how affiliated entities should report ABOs.
- It’s not clear to us whether the intent is to reflect the ABO on the face of the financial statements, or whether the requirement could be met through an enhanced note.
- However, we believe the following information would be most relevant and helpful to users of the entity’s financial statements:

- brief statement of the pension plan, how it is funded, and its current funded status
- when the next valuation of the plan will occur
- amounts of contributions made by the entity and its employees.

More importantly perhaps, the overall aggregate position of the plan is more relevant to the public, than either the detailed reporting of actuarial valuations or the notional apportionment of a share of ABOs to participating employers.

- As we noted in the second round of the PSAB consultations, we believe public sector pension liabilities should be measured using the pension plan's actuarial assumption of expected rate of return, not a bond rate. This is important in order to fairly represent the plan's (and the participating members and employers') investment risk and avoid providing a member leaving the plan with a risk-free asset at the expense of the members remaining in the plan.
- Contingent contributions and benefits should not be included in the ABO, until they've been determined and are no longer subject to any conditions.

7. *Do you agree with the general principle for the potential accounting guidance stated in paragraph .100?*

- We agree with the general principle outlined in paragraph 100:  
*The entity should recognize its share of the accrued benefit obligation of the pension plan in its financial statements, reflecting the substance of the terms in the plan and taking into consideration relevant factors, facts, events and circumstances*  
 if there is additional guidance to the effect described in 6.
- In our plan, individual participating employers are not accountable for the plan's liabilities, and attempting to report their "share" of those liabilities would be misleading. It would obfuscate the entity's true financial position and performance, and it would suggest an obligation that does not exist.
- We believe that when an entity's share of the ABO cannot be determined or the terms of the plan do not apportion responsibility for a share of the ABO to an entity, then the entity's share should be deemed to be zero. In effect, and consistent with other standard-setting bodies' approaches, the standards should revert to defined contribution accounting when insufficient information is available to use defined benefit accounting.

8. *Are there any specific areas that may be challenging in applying the general principle stated in paragraph .100?*

- Our participating employers' obligations are to make required contributions to the plan, assuming that the fund is invested for the long term and in the best interest of the trust's beneficiaries. Employers are not obliged to fund the promised benefits, themselves.



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- The plan is structured to share risk across all employers, regardless of payroll size, number of employees or members, sector, when they joined or left the plan, or modified their participation to include or exclude classes of members. The plan pools risk across multiple member groups, regardless of age, gender, occupation, level of employment, number of employments, when they joined or left the plan,, and employment transfers. The plan records accrued liabilities and accrued assets for the plan in aggregate. There is no consistent and reliable basis for allocating the obligation, assets and costs to individual employers participating in the plan.
  - No individual employer is accountable for all or even part of the plan's accrued benefit obligations. It seems to us to be impossible to assign even a notional share of the plan's obligations to a participating employer.
  - Our plan exists as a separate legal entity from each participating employer. The plan is separately governed, managed and regulated – independent of any individual participating employer. Our plan obligations are not the participating employers' obligations. As the Plan Administrator, the board determines how the ABO is to be met, determining funding and investment policies that meet the pension promise. Participating employers owe required contributions to the plan, not to beneficiaries of the plan.
  - In our context, it would be impossible to accurately and fairly represent even an individual participating employer's *notional* share of the MPP's ABOs.
  - Attempting to calculate a notional share of the plan's ABO would be challenging, time consuming and increase plan administration costs.
  - More to the point, how would a notional share (with no actual underlying obligation) increase understanding of the entity's financial position or performance? Actuarial valuations can be quite volatile, and we question whether the value of the resulting estimates would justify the additional effort and expense. We are of the opinion that it wouldn't; a notional share would only obfuscate and confuse.
  - Worse, a notional share might lead to unintended consequences, including misleading users of financial statements and inciting them to draw negative conclusions about an employer's financial position and stability or the cost and sustainability of the pension plan.
  - Contingent contributions and benefits should not be included in the ABO, until they've been determined, not subject to conditions, and virtually certain.
9. *Do you agree that the effects of risk-sharing provisions should be reflected in the actuarial assumptions used to determine the accrued benefit obligation of the plan (paragraphs .108-.131)?*
- We agree that the effects of risk sharing provisions should be reflected in the actuarial assumptions used to determine the ABO in cases where an entity has ownership of surpluses/deficits and obligations, and its share of the ABO can be determined.
  - Please also see our response to 8.

*10. Do you agree that the entity should report its share of the accrued benefit obligation of the plan that reflects the ultimate cost and risk it bears (paragraphs .132-.155)?*

- No. The employers that participate in our plan are not responsible for the ABO in the plan; we have no concerns with them reporting their ABO as zero. As previously stated, we have concerns with the suggestion that public sector employers should report a notional ABO, including contingent and constructive contributions and benefits, when their responsibility is limited to making required contributions.

*11. Do you agree that it is in the public interest that the accrued benefit obligation reported by the participating employer of a multiemployer defined benefit plan reflects the risk and cost related to the pension benefits they offered to their employees (paragraphs .141-.146)?*

- No. In fact, we believe it would be contrary to the public interest to require employers participating in our plan to report in their own financial statements the ABO that reflects the risk and cost related to their employee's pension benefits.
- In the unlikely event that our plan was wound up tomorrow, there is no entity or group of entities legally obliged to fund any shortfall. If a shortfall existed at the time of a wind up, benefits might need to be pro-rated. More specifically, the plan's trust agreement provides that in the event the plan is terminated in its entirety, the plan sponsors will determine what happens if there is an unfunded liability. Further our trust document explicitly provides that employers are not responsible for plan liabilities. It makes no sense to require these employers to report the risk and costs of employee pension benefits. The risks and costs are shared with participating employees and belong to the plan as a whole, not the employer.
- It would be more useful to users of the entity's financial statements to be able to easily locate information about the aggregate exposure for the plan with respect to all members and employers. This is the practice our participating employers currently follow.

*12. What challenges do you anticipate in determining the entity's share of the accrued benefit obligation of the plan that reflects the ultimate cost and risk it bears (paragraphs .132-.155)? How might the challenges be overcome?*

- Please see our response to 8.
- As we've stated earlier, we do not see any practical manner in which we could apportion ABOs between our participating employers. By design, there is no mechanism for allocating assets, surpluses, deficits, gains or losses to individual employers. This is particularly acute in a multi-employer plan where it is common for members to have employment with more than one employer participating in the plan, either concurrently or consecutively.
- We note that the accounting standards issued by other standards setters recognize this and revert to defined contribution accounting when insufficient information is available to use defined benefit accounting. We believe that the standards set by PSAB should follow this approach.

**Other**

*13. Are there any reasons that the potential accounting principles and guidance discussed in paragraphs .097-.155 would not be appropriate for estimating accrued non-pension benefit obligations?*

- We have no additional comments.

*14. Are there specific issues with, or related to, Sections PS 3250 and PS 3255 that have not been identified in the 'Background of the project' section that PSAB should consider in this project?*

- We have no additional comments.

In conclusion, we support the continued practice by participants in a multi-employer public sector pension plan to record the contributions they make to the MPP as a pension expense in their own financial statements; they should not be required to record any future obligation for pension liabilities in their financial statements.