The Actuarial Profession
making financial sense of the future

Pensions, benefits and social security colloquium 2011

Robert L. Brown

PENSION REFORM IN CANADA

25-27 September 2011

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Agenda

- Canadian Context
- Where we are today
- Proposals for Reform

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THE CANADIAN CONTEXT

- Three Pillars

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THE CANADIAN CONTEXT

- Pillar 1: GIS + OAS

- "GIS" Guaranteed Income Supplement
- A welfare payment
- Funded by general tax revenues
- Not taxable income
- Clawed back at a 50% rate

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THE CANADIAN CONTEXT

- Pillar 1: GIS + OAS

- OAS: Old Age Security paid to all Canadians aged 65+ with 40 years residency (from general tax revenues)
- Clawed back at a 15% rate above $67,688

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THE CANADIAN CONTEXT

- Pillar 2: Canada/Quebec Pension Plan

- An earnings related contributory plan
- Participation is mandatory
- Contribution rate is 9.9% (Split between employer and employee)
- Benefits are taxable

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THE CANADIAN CONTEXT

- Pillar 2: Canada/Quebec Pension Plan

- System is stable at 9.9% (not QPP)
- Contributions and Benefit Accrual stop at the YMPE of $48,300 ≈ AIW
- Benefit accrual is 25% of wages below YMPE (Max benefit is $11,520 today)

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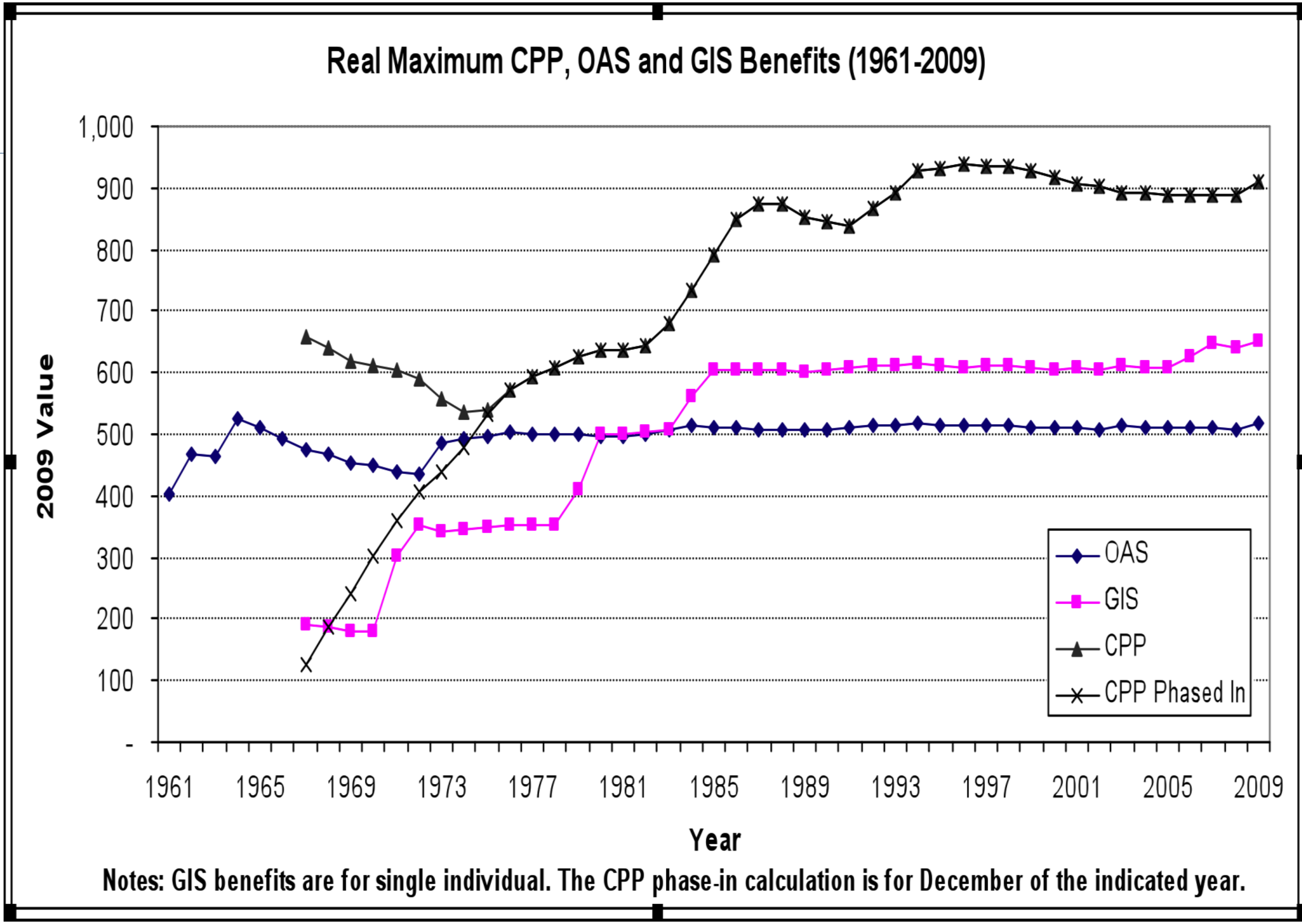
Real Maximum CPP, OAS and GIS Benefits (1961-2009)
2009 Value
1,000
900
800
700
600
500
400
300
200
100
-
1961
1965
1969
1973
1977
1981
1985
1989
1993
1997
2001
2005
2009
Year
OAS
GIS
CPP
CPP Phased In
Notes: GIS benefits are for single individual. The CPP phase-in calculation is for December of the indicated year.

THE CANADIAN CONTEXT

Pillar 3: Registered Pension Plans Registered Retirement Savings Plans/Tax Free Savings Accounts

- Employer RPPs: DB's in decline
- Now 38% of paid workers, but 25% in private sector
- Worry is future generations earning $40,000 to $80,000

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THE CANADIAN CONTEXT

- In total: High degree of protection for the poor
- For average worker: replacement ratio from government systems is 39%
- Lots of room for the private sector

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- OAS / GIS / C/QPP provide an acceptable floor of protection
- GIS clawback means it may be unwise for lower-income Canadians to have separate private savings (mitigated by new Task Free Savings Accounts)
- These benefits are highly targeted
- 1/3 of older Canadians get at least a partial GIS

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- WHERE DO WE STAND TODAY

  - Bob Baldwin’s Report to Ontario MoF
  - Jack Mintz Report (6 parts) to Whitehorse Summit
  - Edward Whitehouse (OECD) Report to Dept. of Finance, Ottawa

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Poverty Rates

- 4.4% of elderly in poverty (5th lowest in OECD)
- OECD average is 13.3%
- Because of highly focused Social Security benefits
- For higher income earners, Social Security benefits are small by OECD standards
- Leaves room for private voluntary systems

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Pension Coverage Rates

- Private sector coverage rates are down
- Particularly true for DB plans
- But number of workers with a pension is up
- True because labour force is growing faster than pension coverage
- With more females in the labour force, more households have at least one pension
- Workers move in and out of coverage

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- Point-in-time pension coverage rates would be more pessimistic than life-time coverage rates
- Coverage rates rise with earnings levels

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Replacement Ratios

- Retirement income is up
- For couples, from 1976 to 2007, up 55%
- For singles, up 79%
- Due to maturation of C/QPP and 3rd pillar savings (RPPs / RRSPs)
- Home ownership is high (5/6); most with no mortgage
- Replacement rates are about 80% (but vary widely by income levels)
- News today is good
- OECD congratulates Canada for mixed system

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Cost of Administration

- Social Security costs compare well with OECD (1/4 of the average)
- Only New Zealand is lower (mandatory DC plan)
- Costs of admin for Individual plans (RRSPs) are high
- 2% of assets per year or more
- A 2% levy means that 37.3% of the retirement accumulation is paid in fees
- Evidence shows that active asset management does no better than passive management for both pension plans and mutual funds
- With fees deducted, active management does worse

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Sources of Income

Source	1985		2001	
	Male	Female	Male	Female
Private Plans	20.5	9.0	36.3	23.4
C/QPP	15.5	10.1	21.2	20.3
OAS/GIS	26.1	45.2	19.3	34.3
Investment	21.2	28.0	10.7	14.0
Other*	16.8	7.8	12.5	8.0

* Includes work earnings

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Pension Reform Models

I Smart DC plans

- Keith Ambachtsheer's Canadian Supplementary Pension Plan (CSPP)

II Expand the C/QPP

- Canadian Labour Congress (CLC)
- National Association of Federal Retirees (FSNA)
- Canadian Association of Retired Person (CARP)

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III Target Benefit Plans

- Model suggested by Ontario (OECP) and Nova Scotia
- Now referred to as Pooled Retirement Pension Plans

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I Smart DC Plans

Keith Ambachtsheer – CSPP

- Auto enrolment (but you can opt out)
- Use C/QPP payroll deduction mechanism
- Aim for 60% replacement ratio in total (with Q/CPP)
- No contributions if earnings < $30,000 (GIS clawback)
- Admin at arms length from government (like CPPIB model)
- Lower overall costs (admin and advice)
- Total costs < 0.3% of assets per annum
- Buy deferred annuities as retirement approaches

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II Plans to Expand the C/QPP

- Many variations on this theme
- CPP rules say new benefits must be fully-funded
- Today's C/QPP contribution rate is 9.9%
- But plan could be funded with 5.9% contributions
- The other 4% is to pay for past legacy liabilities
- But the plans to expand C/QPP work on retirement benefits with small or no change in ancillary benefits (death/disability/orphans)
- This can be done with a 5.5% contribution

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II Plans to Expand the C/QPP

- Today's benefit is 25% up to YMPE
- If we were to move to 70%, it would cost the sum of:

  + 9.9% of salary from the YBE to YMPE (old benefits)

  + 9.9% of salary up to YMPE (for new benefits)

  + 15.4% of salary from YMPE to new limit

  (e.g., ITA limit of $122,222)
- Note: This is a very large contribution for low income workers
- Note: New full 70% benefits will take 40 years to accrue

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II Plans to Expand the C/QPP

Advantages:

- Required infrastructure already exists
- Investment agencies (CPPIB / Caisse) already exist
- Plan has the advantages of size / scale

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II Plans to Expand the C/QPP

Disadvantages

- May cause good existing plans to fold (all proposals)
- Low income workers contribute more but then lose benefits to GIS clawback
- Lower tiers of extended benefits cost 19.8%
- The upper tier costs 15.4%
- As plan matures, contribution rate takes on added volatility because of increased dependence on investment returns
- Not a diversified system (all eggs in one basket)
- Takes 40 years to achieve full benefits

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III Target Benefit Plans (Part 1)

- Consistent with OECP and N.S. reports
- Plan is DC for sponsor / employer
- Worker has a target benefit which actuarial projections say DC will buy (i.e. start with Target Benefit and work backward to required DC)
- Benefits can go up; and also down

  (e.g., indexation before and after retirement)
- Similar to many Ontario MEPPS today

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III Target Benefit Plans (Part 2)

- Assets would be commingled in large pools
- Provides advantages of size
- Independently managed (could be private sector)
- Achieves low cost (< 0.5% of asset)
- No need for employer relationship (even self employed could join)
- Collective risk management vs. Individual Accounts
- Requires amendments to PBAs and ITA
- Now high on the radar screen
- Pooled Retirement Pension Plans

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Q & A

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Guidelines for Social Security Actuaries and Technicians

IASP(1)

- Has existed since January 2003
- Was drafted as a Standard but used as a Education Note
- 2011, decision to draft a new ISAP for Social Security
- But also a Generic Standard
- The two should not overlap

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ISAP for Social Security

- Generic Standard now exists
- Statement of Intent for Social Security ISAP also approved
- New ISAP for Social Security in its 4^{th} draft
- Hope for Council approval in May, 2012

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ISAP for Social Security

- Meant to apply to Valuation activity
- Local Association may adopt this or approve a local Standard at least as good
- Few exist today
- A real need in less-developed countries

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Desirable Characteristics of SSP Actuarial Work

- Objectivity
- Scientific Rigour with some Reliance on other Experts
- Reflection of all relevant features of the SSP
- Peer Review

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Information to be Included in the SSP Report

1. Description of SSP Provisions
2. Data base
3. Assumptions
4. Methodology
5. Results

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Q & A

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