



Office of the Superintendent of
Financial Institutions Canada

Bureau du surintendant des
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Office of the Chief Actuary

Bureau de l'actuaire en chef

Communication of Financial Information for the Canada Pension Plan

**Presentation by Jean-Claude Ménard
Chief Actuary
Office of the Chief Actuary (OCA)**

**to the
Eurostat/ILO/IMF/OECD Workshop on Pensions**

**Paris, France
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For additional information contact:
Kaitlin Sabourin
Communications and Consultations
Kaitlin.Sabourin@osfi-bsif.gc.ca
www.osfi-bsif.gc.ca

Canada

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Good afternoon, thank you for inviting me to speak here. Today, I will discuss how financial information for the Canada Pension Plan is communicated to various stakeholders.

Canada Pension Plan (slide 2)

The Canada and Quebec Pension Plans (C/QPP) are earnings-related social security programs. For the Canada Pension Plan, financing sources are contributions by employer and employee on employment earnings at the rate of 9.9%, and investment income.

The Canada Pension Plan is financed on a steady-state basis which is a partial funding approach aimed at stabilizing the asset to expenditure ratio. This basis was introduced in the mid-1990s to build a greater reserve of assets over time. Investment earnings on this pool of assets in turn help to stabilize the contribution rate and asset/expenditure ratio.

The key legislatively prescribed measure for evaluating the Canada Pension Plan is the steady-state contribution rate which is expected to remain below the legislated contribution rate of 9.9%.

So let me emphasize that the Canada Pension Plan was never subsidized by the Government, and its financing and governance structure ensures that no subsidies will ever be needed.

Main sources of financial status reporting for the CPP (slide 3)

This slide shows the main sources where financial information on the Canada Pension Plan can be found. The first one is the statutory triennial actuarial report that provides detailed information on the long-term sustainability of the CPP.

¹ Remarks to be accompanied by slide presentation, which can be found at the following link:
<http://www.osfi-bsif.gc.ca/Eng/Docs/OCA-JCM-03112016-Slides.pdf>

The other two are the Public Accounts of Canada and the Annual Report on the CPP. Both of these sources present consolidated financial statements of the Plan and information on its long-term sustainability.

All three reports are tabled in Parliament (slide 4)

The three reports discussed on the previous slide are tabled in Parliament and are accessible to the general public. While the focus of these reports differs, they share a common goal: to provide users with accurate, complete and transparent information. Thus, it is extremely important to ensure that the information found in these reports is internally consistent.

The legislation mandates regular CPP long-term sustainability reporting (slide 5)

The CPP has a very strong governance framework which is based on the statutory triennial financial review of the Plan by its stewards – the Federal, Provincial and Territorial ministers of Finance. The main focus of this review is the long-term sustainability of the Plan, and the main outcome is a decision on whether the legislated contribution rate and/or benefits need to be changed. Not surprisingly, the triennial actuarial report is a vital part of this review since it provides detailed information on the long-term sustainability of the CPP including cash flows projections and the applicable steady-state contribution rate.

If a decision to change the Plan is made, the law requires that a supplementary actuarial report should be prepared and tabled in Parliament.

The most recent CPP Actuarial Report as at 31 December 2012 concluded that the CPP is sustainable over the long-term under the legislated contribution rate of 9.9%.

Automatic Balancing Mechanism of the CPP (slide 6)

What will happen if the steady-state contribution rate is higher than the legislated contribution rate? The first line of defence is the agreement among CPP stewards on the course of action reached during the review. The ministers may decide to increase contributions and/or decrease benefits, or they may even agree to do nothing and wait until the next review to make decisions.

However, if the ministers are not able reach an agreement, the self-sustaining provisions of the CPP will be activated. Under these provisions, both the contributors and the beneficiaries are expected to share the financial burden: contributions will be increased and benefit indexation will be frozen until the next review.

So, as you can see, Canada takes the sustainability of the CPP very seriously.

CPP Actuarial Reports present balance sheet information (slide 7)

In order to provide the information needed for other types of financial reporting, the CPP actuarial report presents CPP balance sheets. This supplementary information can be found in the appendix of the report.

The presentation of the balance sheets has evolved from one report to the next. Today, the main emphasis is placed on the open group balance sheet, since it is consistent with the financing approach of the Plan. The information on the closed group balance sheet is presented in a footnote.

Following the tabling of the actuarial report, the Office of the Chief Actuary usually releases an actuarial study that provides more detailed information on various balance sheets.

Open group should be used to account for intergenerational risk sharing and social contract (slide 8)

This slide reiterates the most important point that was addressed several times during the last two days.

The choice of methodology used to produce a pension system's balance sheet is mainly determined by the system's financing approach. The financing approach also influences cost and risk sharing among the program's stakeholders and generations of participants.

Pay-as-you-go and partially funded systems represent social contracts where, in any given year, current contributors allow the use of their contributions to pay current beneficiaries' benefits. As a result, such social contracts create a claim for current and past contributors on the contributions of future contributors. The proper assessment of the financial sustainability of a pay-as-you-go or partially funded social security system by means of its balance sheet should take these claims into account. It should be emphasized that these claims are not government debt.

The traditional closed group methodologies do not reflect these claims since only current participants are considered. In comparison, the open group approach accounts explicitly for these claims by considering the benefits and contributions of both current and future plan participants.

Some thoughts on the closed group approach (slide 9)

The closed group approach is often considered a backward-looking approach. In reality, in the preparation of the closed group balance sheet, a number of assumptions is made to determine liabilities: economic assumptions such as discount rate, inflation, real wage increase, as well as demographic assumptions such as mortality rates, disability incidence rates, retirement rates, etc.

While these assumptions may be considered sufficient to report on occupational pension plans, they are definitely not for social security systems. For example, countries may have different demographic prospects that will impact their comparisons. But this is not captured through the closed group methodology (remember Canada and South Canada discussed on Day 1 of our seminar).

Looking forward is critical for social security systems assessments (slide 10)

Social security systems are fundamentally different from traditional pension plans, since they are long-term systems affected by a country's past and future economic, demographic and policy environments. They are supposed to be enduring in nature and cover multiple generations.

So, to provide a comprehensive and objective picture, future developments should be taken into account in both assessing the long-term sustainability and compiling a balance sheet that could be used for an intelligent analysis, including a meaningful comparison between countries.

CPP Consolidated Financial Statements provide multiple disclosures (slide 11)

Two notes to the CPP consolidated financial statements address the financial status of the Plan. The first note (the longer one) talks about the long-term financial sustainability of CPP. It discusses its financing principles, summarizes the main findings of the latest actuarial report and provides a sensitivity analysis.

The second note presents the balance sheets of the CPP under the open and closed group approaches.

Note 14 discusses the interpretation of information presented in the balance sheets (slide 12)

While the numbers shown in this note are very important, what is even more important is the discussion on the interpretation of the information. This discussion is aimed at enhancing users' understanding and at minimizing the possibility of misinterpretation. As an example, this slide contains several quotes from Note 14.

In general, I encourage you to read both notes – the link is provided at the beginning of the presentation.

Public Accounts of Canada favour the open group approach (slide 13)

Finally, it is stated in the Public Accounts of Canada that: "if the CPP's financial sustainability is to be measured based on its asset excess or shortfall, it should be done on an open group basis that reflects the partially funded nature of the CPP, that

is, its reliance on both future contributions and invested assets as a means of financing its future expenditures.”

The key to good disclosure is the cooperation between professions (slide 14)

The journey to develop the notes to the CPP consolidated financial statements was long and not always smooth. What was the key to the eventual success was the willingness of members of the “triple “A” team” - actuaries, accountants and auditors - to cooperate and understand each other’s position. Other countries will include other professionals, but in many instances, these three professions are the key players.

Finally, even if we are very proud of these disclosures, the search for perfection is endless. Each year we revisit these notes and try to make them more complete, more transparent, and, just, better.

To conclude... (slide 15)

We are all here with the same goal: to help countries properly measure the robustness of their pension systems. As such, the communication of financial information should be relevant, clear, complete and internally consistent. One of the answers may be the use of multiple disclosures – the way chosen in Canada.

The actuarial community is and will continue to be committed to work with all interested parties such as international organizations, accounting bodies, and Governments to develop the reporting requirements that will provide meaningful and complete information to users.

Thank you for your attention. I will be happy to answer any questions that you have.