Communication of financial information for the Canada Pension Plan

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

by Jean-Claude Ménard, Chief Actuary, Canada

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Canada Pension Plan

- Canada Pension Plan (CPP) is the 2nd public pillar of the Canadian Retirement Income System (DB, earnings-related)
- Financed through employer/employee contributions and investment earnings
- Partial funding approach with contributions being the main source of financing
- The key legislatively prescribed measure for evaluating the CPP is the steady-state contribution rate
  - It is expected to remain below the legislated contribution rate of 9.9% of covered earnings.

Government doesn’t and won’t provide any subsidies to the CPP
Main sources of financial status reporting for the CPP

Long-term sustainability reporting


Consolidated Financial statements
All three reports are tabled in Parliament

The goals are

– to provide stakeholders with the information on the financial status of the CPP to allow making informed decisions
– To enable comparison of government finances
– To educate, and not to confuse the users!

Reporting should be internally consistent.
The legislation mandates regular CPP long-term sustainability reporting

- The CPP has a strong governance mechanism that is based on the triennial review of the Plan by Federal, Provincial and Territorial (FPT) Ministers of Finance
- A vital part of this review is the triennial actuarial review with its results tabled in Parliament
- Supplementary actuarial reports are prepared when the CPP is amended.

The results contained in the latest CPP Actuarial report confirm that the legislated contribution rate of 9.9% is sufficient to financially sustain the Plan over the long term.
**Automatic Balancing Mechanism of the CPP**

- Self-sustaining provisions of the CPP provide additional safeguards for the CPP sustainability
- The mechanism is activated only if FPT Finance ministers can’t agree of ways to restore CPP sustainability
- It defines the cost-sharing mechanism between contributors and beneficiaries if the Plan is deemed to be unsustainable
  - Increase in contributions and freezing of benefits indexation.
CPP Actuarial Reports present balance sheet information

- The main content of the CPP Actuarial Report focuses on the long-term cash flows projections used to determine the steady-state contribution rate.

- However, Appendix A of the report presents the CPP balance sheet.
  - The main emphasis is made on the open group balance sheet.

*Pension system’s balance sheet should reflect its financing approach*

  - The information on the closed group balance sheet is presented in the footnote.
Open group should be used to account for intergenerational risk sharing and social contract

- CPP, as a partially funded plan, represents a social contract
  - Each year current contributors allow the use of part or all of their contributions to pay current beneficiaries’ benefits
  - Claims for current and past contributors to contributions of future contributors is created
  - A balance sheet should take these claims into account

These claims are not government debt.

- At any valuation date, these claims
  - could be expressed as present value of future contributions of current and future contributors
  - represent a part of system’s assets

- The corresponding future benefits should also be taken into account.
Some thoughts on the closed group approach

• Closed group approach is supposed to be backward-looking. But is it really the case?
  – It makes assumptions about future like mortality, expected rate of return, inflation, etc.
  – Are these assumptions sufficient for assessing properly social security systems?

• In majority of cases, the answer is “no”.
Looking forward is critical for social security systems assessments

- Social security systems are fundamentally different from traditional pension plans
  - 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
- To provide comprehensive and objective picture, future developments should be taken into account in compiling a balance sheet for social security schemes.
CPP Consolidated Financial Statements provide multiple disclosures

- **Note 13: Financing of the Canada Pension Plan**
  - Summary of the financing principles of the CPP
  - Main findings of the latest actuarial report

- **Note 14: Actuarial obligation in respect of benefits**
  - CPP balance sheet is presented under two approaches
    - open group, and
    - closed group without future accruals

- Same information is included in the Public Accounts of Canada.
**Note 14 discusses the interpretation of information presented in the balance sheets**

- The choice of the methodology used to produce a social security system's balance sheet is mainly determined by the system's financing approach.

- The CPP was never intended to be a fully-funded plan and the financial sustainability of the CPP is not assessed based on its actuarial obligation in respect of benefits.

- The CPP is intended to be long-term and enduring in nature, a fact that is reinforced by the federal, provincial, and territorial governments' joint stewardship through the established strong governance and accountability framework of the CPP.
“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

- The Canadian disclosure model is a result of
  - many hours of discussions,
  - efforts to understand each other’s position, and
  - several compromises

between professionals involved in the reporting process:

  Actuaries
  Accountants
  Auditors

The triple “A” Team!
To conclude...

- The reporting of financial information for social security systems should be internally consistent
  - The information provided should educate and not confuse
- Multiple disclosures similar to those used for the Canada Pension Plan could be the answer
- International organizations, Governments and actuarial community should work together to develop the reporting requirements that will provide meaningful and complete information to users.
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Thank you