Enhancing the Canada Pension Plan: Agreement in Principle

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Office of the Chief Actuary

• The OCA is an independent unit within OSFI.
  – The Chief Actuary reports to the Superintendent;
  – however, the accountability framework of the OCA makes it clear that the Chief Actuary is solely responsible for content and actuarial opinions in reports prepared by the OCA.

• Mandate: conduct statutory actuarial valuations on the
  – Canada Pension Plan (CPP) – 19M members
  – Old Age Security Program (OAS) - 5M beneficiaries
  – Federal public sector pension and insurance plans – 0.8M members
  – Canada Student Loans Program – 0.5M loans
  – Employment Insurance Program – 17M workers

The following presentation reflects solely the views of the Office of the Chief Actuary
The agreement in principle sets out the broad parameters of the CPP enhancement.

- The agreement also established that both employee and employer contributions to the enhanced portion of CPP would be tax deductible, and that the Working Income Tax Benefit would be increased to help offset CPP contributions for eligible low-income workers.
Estimated additional annual combined employee/employer contributions (nominal; rounded to nearest $10; pre-tax)

Illustration of Additional Annual CPP Benefits for Different Age Cohorts and Income Levels ($2016)

Note: This illustration assumes that individuals have constant earnings and that individuals would take-up CPP benefits at age 65. The increase in benefits is based on contributions starting in 2025 (when enhancement is fully implemented); rounded to nearest $10.

Source: Finance Canada

Note: Assumes constant nominal earnings.
Source: Finance Canada
Enhanced CPP strengthens link between contributions and benefits

• The enhancement is fully funded.

• Each year of contributing to the enhanced CPP will allow workers to accrue partial additional benefits.

• Full enhanced CPP benefits will be available after about 40 years of making contributions.

• Partial benefits will be available sooner and will be based on years of contributions.

No past service liability is created
The phasing-in period of seven years gives time to consider investment strategies

- Full funding principle means that contributions will exceed benefits for the next 30 to 35 years.
- This will result in the accumulation of sizable assets.
- Proper funding and investment policies would need to be developed.
- Investing CPP enhancement assets should take into account its full-funded nature.
Enhanced part of the CPP is more sensitive to the investment environment than the current CPP

Sources of revenues

<table>
<thead>
<tr>
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<th>Partially funded CPP</th>
<th>Fully funded enhancement</th>
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<tbody>
<tr>
<td>Contributions</td>
<td>70%</td>
<td>30%</td>
</tr>
<tr>
<td>Investment income</td>
<td>30%</td>
<td>70%</td>
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For a new fully funded pension plan with duration of 20 years, the change of 1.5% in the expected rate of return increases/decreases the contribution rate by about 30%.

Source: the 26th CPP Actuarial Report
Insufficient rates provision of the current CPP serves as a safety net

- Insufficient rates provision of the current CPP is activated in the case its sustainability is jeopardised and its stewards (Federal and Provincial Ministers of Finance) do not agree on measures aimed at restoring the CPP sustainability
  - Neither contribution rate nor benefits are guaranteed

- Due to a higher exposure of the expanded CPP to the investment risk, a robust and effective self-adjustment mechanism should be put in place.

- Such mechanism may impact contributions, benefits or both.
Do persistent low-income workers benefit from CPP enhancement?

Share of persistent low-income workers: CPP contributors’ cohort aged 65-69 in 2014 (1.4 million)

Includes:
- Mid-career Immigrants
- Women born mid 20th century

In 2014:
- More than 75% of persistent low-income workers were not receiving GIS
- Since the GIS is a family benefit, over 80% of female persistent low-income workers do not receive GIS

Persistent low-income worker with high and medium labour force attachment:
1. More than 10 years with earnings between 10% and 50% of the YMPE
2. Less than 20 years absence from the labour force
Integration with defined benefit pension plans

• Many defined benefit pension plans in Canada are integrated with the Canada Pension Plan.

• This integration is an approximation based on the Registered Pension Plan (RPP) parameters.
  – For example, for the federal public service pension plan the integration of 0.625% is designed to replace approximately 25% of earnings up to YMPE after 40 years of service.

• The decision on potential changes due to the CPP enhancement will be taken by plan sponsors and could be subject to collective agreement.
Enhancing the Canada Pension Plan: Agreement in Principle

Thank you

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