

**Pensions**  
**The Pension You Need**  
**Not Worry About**

**By: Bruce Little**

***Exclusive Online Article***

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**BENEFITS AND PENSIONS**  
**MONITOR**

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## **Pensions**

### **The Pension You Need Not Worry About**

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Pension worries are back at the forefront of Canadians' concerns and the top of their politicians' in-baskets. The stock market crash has undermined the personal savings of Canadians who count on their share holdings for retirement income, while those expecting a company pension built over years of work see a parade of equally grim stories. Many company pension plans are now 'below water,' their accumulated savings (their assets) having fallen short of their promises to pay (their liabilities).

### **Sharp Declines**

The federal Superintendent of Financial Institutions said in December that the assets of federal pension plans were two percentage points shy of their liabilities at mid-year and because "financial markets have experienced sharp declines" since then, "we can expect asset values for many plans to be severely eroded at year-end." A few days later, the Ontario government announced a program of temporary solvency relief for pension plans.

Even before the turmoil in financial markets brought a new urgency to the pensions issue, four provinces – Ontario, Nova Scotia, and (jointly) British Columbia and Alberta – produced new pension studies, complete with recommendations designed to allay rising concerns over retirement income.

However, the shocking decline in pension values probably scares Canadians most. Even the Canada Pension Plan's huge asset base, which now stands at \$108.9 billion, has shrunk under the meltdown. Should Canadians worry that CPP retirement pensions, the foundation of many people's retirement finance planning, won't be there when they need it? The answer to that one is an emphatic 'no.'

In 1995, such fears were widespread, with reason. The CPP's assets were falling and the plan's chief actuary had just projected that the CPP would run out of cash unless the contribution rate was put on a track to rise to more than 14 per cent of covered earnings by the time the baby boomers all retired. Today, we know the contribution rate has been frozen at 9.9 per cent since 2003, yet the CPP's assets, despite the latest setback, were at last count almost triple what they were in 1995 and the chief actuary's latest report said the plan is financially sound for another 75 years.

### **Grim Outlook**

The difference between the grim outlook and this happier outcome was that Ottawa and the provinces carried out a reform of the CPP that was barely noticed at the time and largely forgotten since. In the first three decades after the CPP was launched in 1966, governments had sweetened benefits without increasing the contribution rate enough to cover the higher costs. Two rounds of changes – in 1985 and 1991 – had failed to correct the problem. By 1995, governments were back in talks once more, this time with officials and finance ministers in a 'never again' frame of mind.

Though they fought over many other issues, the ministers realized the CPP was a very good plan that could be put on sound financial ground through a three-part solution:

- increase contribution rates rapidly, but then freeze them
- trim future benefits

Those two measures would quickly generate a much bigger fund, which led to the third – and most important – change. They handed the CPP fund over to a new arm's length organization which would invest in the same manner as other pension plans. The legislation and regulations gave the new CPP Investment Board even more operational independence from government than the Bank of Canada and it was explicitly told to invest with the sole purpose of maximizing returns for the CPP's members.

### **Bigger Cushion**

Today, even though the CPP fund, like every other pension plan, has lost money in the latest stock market crash, it

still has a much bigger cushion than it would have had without the 1997 reform. Better yet, the annual revenue from workers' CPP contributions will continue to exceed expenditures for about another decade. After that, the CPP will dip into its accumulated savings to help pay benefits, but the annual draw will amount to no more than about two per cent of the fund itself, which will keep growing. Worry about workplace pensions if you will but don't worry about the CPP. When it's needed, the CPP nest egg will ensure that all the bills can be paid.

Governments too often act only for the short term and with regard only to their own interests. In 1997, politicians from four parties and 11 governments co-operated to make Canada's national pension plan sustainable for the very long term. These days especially, that's something to be grateful for.

Bruce Little is the author of 'Fixing the Future: How Canada's Usually Fractious Governments Worked Together to Rescue the Canada Pension Plan,' published recently by University of Toronto Press and the Rotman School of Management.