"IMPROVING CANADA'S RETIREMENT SAVING: LESSONS FROM ABROAD, IDEAS FROM HOME"

A Commentary

By Keith Ambachtsheer

The goal of this brief review is to assess the contributions Patrik Marier's IRPP Study makes to Canada's pension reform process as it stands today, prior to the next meeting of the Finance Ministers' on pension reform in Alberta, in mid-December 2010.

Canada's Pension Reform Process Today

The multi-year study of, and debate on how Canada should reform its retirement income system is moving along, but is by no means complete. There is a growing consensus that the primary target of pension reform should be the millions of Canadian middle-income, private sector workers who are not members of an employer-sponsored Registered Pension Plan. As Marier, among others, points out, the risk is that the current situation will lead to many of these workers experiencing significant reductions in living standards when they retire. Two broad approaches to addressing this problem have emerged:

1. Expand the CPP through raising the YMPE (currently $47,200), raising the income replacement rate (currently 25%), or some combination of the two.

2. Expand supplementary pensions through a viable strategy that will enroll the target group into one or more cost-effective pension plans or retirement savings accumulation arrangements that would sit on top of the current OAS/GIS/CPP/QPP public pension component.

In this context, Marier's stated goal is to contribute to Approach 2 by studying what other countries have done to address this challenge, and what Saskatchewan has done to date.

It is worth noting that the University of Calgary's School of Public Policy has just published a paper by Jon Kesselman titled *"Expanding Canada Pension Plan Benefits: Assessing the Big CPP Proposals".* So between the Marier and Kesselman papers, Canada's policy-makers have the luxury of assessing new insights in both possible approaches to addressing Canada's middle-income, private sector workers pension coverage problem.

Marier's Contribution to the Pension Reform Debate

The value of understanding how other countries (e.g., New Zealand, Norway, Sweden, and the UK) have addressed similar challenges is self-evident. What Marier discovers, however, is that the value of these lessons is limited. A strong element of multi-decade path-dependency runs through each of the four country pension reform stories. In each

case, the specifics of the solution were heavily influenced by what came before, and by the country's social-cultural fabric.

For example, Marier points out that Norway's decision to mandate employers to provide adequate pension arrangements for their employees required the kind of robust national government-business-labour bargaining process that does not exist in Canada. In the case of Sweden, the big pension reform story was to move to a big, mandatory, self-adjusting, national, pay-go defined contribution scheme. Adding on the small AP7 personal accounts piece was almost an afterthought. The two countries with a more Anglo-Saxon orientation (NZ and UK) have neither Canada's CPP/QPP equivalent, nor a history of mandating participation in large occupational pension schemes. This led both countries towards designing 'soft persuasion' personal pension account arrangements on a national basis, with features such as auto-enrolment, auto-investment, and auto-contribution escalation features.

So it is not surprising that the models of the Saskatchewan Pension Plan, and that province's Co-operative Superannuation Society Pension Plan, offer the best 'fit' for reforming Canada's retirement income system (other than through CPP/QPP expansion). They operate independent from government, and offer good governance and operations mechanisms. Naturally, considerable redesign would have to be done for one of them (or some blend of the two) to operate on a multi-provincial or national level. Also, Marier stresses the need for Canada to carefully consider the role that 'soft persuasion' devices such as auto-enrolment should play to ensure broad, pan-Canadian participation in a much-expanded version of a SPP/CSSPP type-of supplementary pension arrangement. And finally, Marier points out, there is always the challenge of reaching consensus on the way ahead within Canada's unique decentralized political structure.

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Commentary

By Monica Townson

There is no shortage of ideas on how to fix Canada's pension difficulties. But unless changes are made soon, many Canadians will end up with inadequate incomes in retirement. Public pension programs alone do not provide enough replacement income for retirees to maintain their standard of living in retirement. But most Canadian workers do not have a workplace pension plan and the majority of individuals are not saving through other means such as RRSPs.

Policy makers are now considering ways to encourage people to save more for retirement and options to improve coverage of workplace pension plans. The alternative is to increase the benefits provided by the CPP/QPP. Ultimately, we may see a combination of all these options. The objective is to improve coverage of the retirement income system and to make sure retirees can accumulate enough savings to provide an adequate income in retirement.

Other countries have faced similar problems and have taken measures to address the situation – often by developing systems of individual accounts, whether mandatory or voluntary. But while such examples are interesting, they do not necessarily provide viable alternatives for Canadian policy makers. For example, unlike public earnings-related pension schemes of many European countries, which are designed to provide an earnings-replacement rate about 50% of the average wage, the CPP/QPP aims for a modest replacement rate of 25% for 40 years of contributions. Old Age Security programs add another 14% to the replacement rate for someone earning at the average wage. In other words, private retirement savings options in Canada are expected to provide a much higher percentage of retirement income than they are in other countries. **This has to be taken into account when looking at reform approaches taken in other countries.**

Voluntary schemes or automatic enrolment with opting out may do little to improve coverage and individual accounts, adopted in several of the countries studied in Marier's paper, transfer the risk of retirement provision on to individuals, and do not guarantee adequate income in retirement. Such schemes tend to be much more costly than public pension systems.

While reformers concentrate their efforts on designing new savings options for the third tier of Canada's retirement income system, they may yet be persuaded that the solution they seek is already in place. The CPP/QPP covers virtually everyone – both workers and their dependants – it is indexed for inflation, it is portable across jobs, it is well managed at low cost and is secure for the future. These characteristics, Marier suggests, make this option attractive. Increasing the replacement rate of the public pension plan would require a modest increase in contributions, but may well be the most cost-effective and straightforward way to go.

Monica Townson is an independent consultant and Research Associate with the Canadian Centre for Policy Alternatives working in the field of social policy. She has written six books and a wide variety of studies on pensions and retirement, income security programs and other social policy issues. She was a member of the Pension Commission of Ontario for 11 years and served on the Canada Pension Plan Advisory Board. She also chaired the Ontario Fair Tax Commission which reported on tax reform in the province after a three-year study.