



EXCLUSIVE INTERVIEW:

Tony Williams, a senior actuary and partner at PBI Actuarial Consultants Ltd. discusses his firm's two-tiered prescription for pension reform

Today I am pleased to interview Tony Williams, an actuary and partner in the firm of [PBI Actuarial Consultants Ltd.](#) with offices in Vancouver in Montreal.

Both the Federal Minister of Finance Jim Flaherty and his Ontario counterpart Dwight Duncan have gone on record as favouring a two-pronged approach to pension reform including both limited enhancement to the CPP and legislative amendments that would facilitate large, private sector multi-employer plans.

But the devil will definitely be in the details.

PBI has already put considerable thought into a similar two-tiered approach, including how CPP amendments may impact contribution levels.

Q. Tony, is there a pension coverage crisis in Canada, and if so, can tell me what that really means?

A. Well, I do believe there is a coverage crisis. You can see that pension plan coverage across the country has been declining for several decades so only about one in four Canadians are in employer-sponsored pension plans.

While there may be some coverage through the CPP and some employees use their RRSP, very few are in an employer-sponsored pension plan. Therefore, I definitely think there is a crisis.

Q. There have been studies done in Alberta/B.C., Ontario and Nova Scotia over the last several years. In addition acronyms from the CLHIA to PSAC to CARP to the CFIB have all been promoting different solutions to the coverage problem. Can you break these proposals into a couple of categories and briefly describe them?

A. Sure, I'd be happy to because there is a lot of information and ideas coming which is good. I've been trying to stay on top of these issues for several years. For example, part of the mandate of the Alberta/B.C. commission was to look at pension coverage.

One of the solutions they came up with is for some kind of a provincial or national DC plan on a voluntary basis — called the “ABC Plan.” So that's one example. Now that would be a defined contribution solution and employers would have to opt out of it. The idea is that at least that would get many more people into some kind of pension arrangement and start to accumulate retirement savings.

I have some concerns about that type of arrangement. I make no bones about it. I think the defined benefit type of plan provides better risk sharing. Nevertheless, the ABC Plan would have the advantage of scale. One of the problems in Canada is that there are extremely high expenses associated with pension plans, particularly Group RRSPs and DC plans. If you can get economies of scale by grouping large numbers of employees, you should be able to dramatically reduce the operating costs for these kinds of plans.

Q. So would it be fair to say the proposals are sort of in two camps...one is a government or industry opt-out DC plan and the other is some sort of top-up to the CPP?

A. Yes that's right. Getting to the other side, there is a camp of supporters — and I guess I include myself in that — who say, “We've got the CPP. In recent years its financing has worked quite well and it already reaches all Canadian workers and provides a basic level of benefit.” As a result, one option proposed is various ways of increasing the CPP.

We can still have a voluntary system on top of that but it would top-up what is provided from the CPP. So for example the Canadian Labour Congress and the former actuary for the CPP have proposals and we think those are worth looking at. The scale and the structure are already there and there is a financing mechanism. It would still leave room for supplemental plans but provide more working Canadians with a floor of pension benefits.

Q. So what exactly is your firm proposing in your submissions and presentations?

A. Well, it's more along the lines of a defined benefit solution but there are a couple of parts to it. I think it's worth looking at expanding the Canada Pension Plan although it may be a little more modest in terms of the amount.

We suggest that the covered % be increased for future earnings. Boosting CPP to 70% of pay is maybe going further than we need to. We could up the % of earnings to be replaced from 25% to maybe 35% or 40%...somewhere in that range, depending on affordability. This would provide a better base, but people would still be required to have their own savings or be in an employer-sponsored plan on top of that. But there would be fewer people that would have very low retirement income.

Currently, employees who are retiring without an employer-sponsored plan or saving in their own RRSP and depending on CPP and OAS are not going to have very a good retirement income.

A survey commissioned by the Canadian Institute of Actuaries prior to the meeting in PEI this week shows Canadians are very concerned about having adequate retirement income so I think that supports that there is a good reason to consider proposals such as extending the CPP.

Now even if you improve CPP that wouldn't be retroactive or help people who are retiring without adequate retirement savings over the next 10 or 20 years. So there might be a need for some other supplemental program in the short term and there may be a need for employers and the government to share the financing of that because employees don't have the money.

In addition, the private pension system in Canada has a lot of problems with being multi-jurisdictional. There have also been issues with pension plan financing being limited by the income tax rules so employers and plan sponsors are hesitant to fund pensions to the right level because once they put the money into the fund they can't get it out.

Q. When you suggest bringing the CPP up to 35% or 40% of salary, are you also suggesting changes to the Yearly Maximum Pension Earnings which is currently around 40%?

A. Yes, I think that should be looked at because CPP currently just provides such a basic level. I've seen proposals from the former actuary for the CPP to dramatically increase the YMPE. I'm not sure it needs to be three or four times the average wage, but 50% more than the average would capture the pension coverage for a much larger group of working Canadians than the current YMPE.

I think some people think that because they are part of CPP it's going to be ok, but it's really just designed for people with the most basic income levels.

Q. I want to go back to the nuts and bolts of the changes you are proposing for the CPP. You are proposing:

- **An additional 15% of YMPE accrual layer for future CPP/QPP service only (from 25%-40%)**
- **Normal retirement age at 67**
- **No built-in retirement subsidy**
- **Determine contributions to self-finance this (50% employer; 50% employee)**

Q. Can you hazard a guess as to the total impact on employer/employee contributions if your proposal is implemented?

A. By doing a little bit of extrapolation from some of the numbers out there, there will be additional contributions required from employees and employers. The first part is if the YMPE was increased, the % contribution level would be applied to a larger earnings base, increasing the overall \$ contributed.

The other side of it would be if the actual replacement ratio was increased. That would increase the % of pay. I've seen some numbers. The CPP's goal is to be well-funded not necessarily fully funded.

Our proposal could easily add a couple of % of pay to the employer and employee required contributions over time to support this increased coverage.

Q. We're paying a total of 10% now. To go to 35% or 40% you think will increase total contributions to what? 15%? 18%?

A. It may end up being a bit less than that but I don't think it would be as high as 18%. Again, I would have to do more work on the number but total contributions would go up into the low teens.

Q. Groups such as the CFIB are opposing any form of mandatory pension program that would increase payroll costs, particularly for smaller businesses. How would you respond to their concerns?

A. Their concerns certainly are valid and this is always a balancing act. On the one hand, if we just focus on keeping costs as low as possible so businesses are as competitive as possible we are going to be putting forward a huge retirement income problem for future generations to solve.

Instead of an ad hoc approach to the problem, PBI believes we need to face the medicine now and do what needs to be done. All businesses in Canada would face the same contribution increases so it's not like competition among domestic firms would be affected.

I also think it is much more efficient to have an expansion like this to the CPP rather than just rely on RRSP-type basis because of the fee differential. So I think employers need to be educated on the effect of the lower cost base and how that affects them as well.

Q. Now a key element of your proposal is to increase the normal retirement age to 67. While this is consistent with emerging practice in the U.S., Germany, Denmark and the U.K., do you think there is a political/practical appetite for this in Canada?

A. Well it's probably a bit of a hard sell, but I'm not proposing we change the existing retirement age for the CPP at least for service that is already been put in, but this is consistent with what we are doing with our private pension plan clients saying that these early retirement benefits are very, very expensive and people are joining the workforce later, like in their late 20s or even later than that. It's unrealistic to think that people can start in the workforce at 30 and retire in their late 50s with a high pension. You know, the numbers just don't work out.

Q. But we are talking about 67 for a full pension, and that's a big chunk for a country where the average retirement age is around 62.

A. Yes, but what I'm leading to, is if we get this right going forward, then say the retirement age is set at 67— I was going to suggest 69, but 67 seems to be in the right direction — with longevity, people are going to receive those pensions for a very long period of time. But if someone does choose to retire and start their benefits early, say at age 60, this would still allow them to do it. But the adjustment in their pension would reflect what's in the plan, so there would probably be a reduction in the order of at least 5% per year from age 67 until they actually retire. And that would promote consistency and sustainability among CPP members.

Q. What would the phase in period be until older Canadians could actually claim an enhanced pension under your proposal?

A. If this next layer of the CPP starts in the next year or two, for the first few years there will not be very much additional pension there. It will really take 20 or 30 or 40 years for that tier to evolve into a full benefit much like the original CPP when it came into effect in the 1960s. However, in that case there was a very generous phase-in period for people who retired shortly after the CPP came into effect.

I'm not suggesting we take that kind of approach as it would be very, very expensive but there could be some kind of supplement program to bump up the CPP for those people who are already age 55 and don't have an adequate pension. Then the transition program would eventually fall off over the next 10 or 20 years.

Q. So we are trying to get this sorted out for our children?

A. That's right. If we get our target right, then we can deal with the problem of people close to retirement who may not have the option to continue working at high paying jobs and contributing because they are physically or mentally able to work. It is unrealistic to think huge numbers of these people can actually decide when they want to retire.

Thanks Tony for agreeing to talk to me today. I expect that PBI will be an active participant in the dialogue over the weeks and months to come.

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