Intelligence MEMOS

From: Keith Ambachtsheer, Malcolm Hamilton and Ed Waitzer

To: Canadian Pension Watchers

Date: May 15 2024

Re: **Canada Needs A New CPP Consensus**

The creation of the Canada and Quebec pension plans in the 1960s and subsequent amendments to them in the 1990s is a compelling story of how governments worked together to create and sustain one of Canada's greatest public policy achievements. Today we are faced with the thorny issue of how to determine a fair basis on which Alberta might choose to exit the CPP.

When the CPP was created, Ontario requested a provision to allow a province to leave the CPP by setting up an equivalent provincial plan. While open to different interpretations, Section 113 of the CPP act describes the calculation of the amount to be paid to a withdrawing province. Its essence is to transfer to the pension fund of the withdrawing province an amount that would have accumulated in that pension fund had it always been separate.

Alberta's share of the CPP's contributions has long exceeded its share of the benefits. Between 1981 and 2018, Albertans were responsible for 14 per cent of the CPP's contributions while collecting 10 per cent of the benefits. The difference, accumulated with actual CPP investment returns over time, is significant. Last September's **LifeWorks study** found that Section 113 could be interpreted to allow Alberta to claim about half of the CPP's accumulated assets.

If Alberta were to set up its own pension plan with half of the CPP's assets, employees in Alberta would contribute significantly less than they now contribute, and significantly less than employees in the other provinces. If other "low-cost" provinces withdraw, the contribution rate for employees in the "high-cost" provinces would increase further. The result would be a collection of identical provincial pension plans, each with its own contribution rate and larger administrative costs. Is such an arrangement fairer than what we have today? Is it more likely to unite, or divide?

Before answering these questions, we must address several concerns.

The first is whether the data required to perform the calculations set out in Section 113 are available or can be made available. If not, the process by which a province withdraws from the CPP will need to be reimagined.

More importantly, we need to agree on what constitutes "fair" contribution rates. Today all CPP members contribute the same percentage of contributory earnings and accrue the same pension as a percentage of their pensionable earnings. There are no differences by age, gender, or province of employment.

However, by design, those who entered the CPP at the outset received a much better deal. For example, those who retired at the age of 65 in 1976 received full pensions after contributing at a rate of 3.6 per cent for only 10 years. Those entering the CPP after 2002 will be expected to contribute at a 9.9-per-cent rate for 40 years to earn the same pension. The current contribution rate would be about 6 per cent without this intergenerational transfer. Arguably there were mitigating circumstances. The first generation had to contend with the Depression, the Second World War and runaway inflation. They paid for the upbringing of the baby-boom generation. The CPP helped them retire in comfort and allowed their children to concentrate more on saving for their own retirements and less on supporting aging parents.

As the fastest-growing province, Alberta had relatively fewer first-generation participants and more second- and third-generation participants than the other provinces. This is one of several factors that helps explain why Alberta's contributions were relatively high and its benefits were relatively low. The intergenerational transfer cannot be reversed, but some of the burden could be shifted between provinces.

Without some new source of CPP funding, such a shifting of burdens and/or the withdrawal of one or more provinces is a zero-sum game, with winners and losers. Ultimately the question is whether Canadians are best served by a CPP with one national contribution rate, or by a CPP with regional or provincial contribution rates. Setting up separate provincial pension administrators simply increases costs.

Reaching an acceptable compromise will be challenging, but we cannot proceed without one. As was the case when the CPP was cobbled together, we've come to a point where all involved must look beyond narrow self-interest and be cognizant of the risks and uncertainties of political posturing, inaction, or of referring the matter to the courts. The 22 million Canadians who are CPP members expect a sensible solution. Future generations deserve no less.

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