

# **CARP Submission to the Standing Committee on Finance: Proposed Framework for Pooled Registered Pension Plans**



**February 28, 2012**

## ***Canadians Need Help Saving for Retirement***

The core goal of any country's pension system is to provide an adequate system available to the full breadth of the population that is sufficient to prevent poverty in old age. It must be affordable by the employers and employees and other participants and robust enough to withstand major shocks, including economic, demographic, and political volatility. Recent events have demonstrated that Canada's retirement system is not meeting this goal in part because of inadequate pension coverage.

Ongoing economic problems have focused public attention on the need for Canadians to prepare for their own retirement and there is a growing recognition of the need for a new broadly based retirement savings vehicle. That is where the consensus largely ends.

CARP's longstanding focus with regard to the larger issues of pension plan coverage and savings adequacy has been on the 3.5 million middle income earners working for smaller employers and the 4.9 million earning less than \$30,000 per year.<sup>1</sup> This grouping of 8.4 million Canadians tends not to have occupational plans and is most at risk for retirement income inadequacy. It is for this group primarily that advances in pension reform are needed.

There are competing visions of what level of coverage is necessary, whether it must be mandatory, how big it should be, who should manage it and whether it can or must adequately address the needs of low and middle income Canadians.

CARP has consistently called for a supplementary Universal Pension Plan modeled on the CPP with mandatory enrolment, utilizing the existing payroll deduction mechanism, professional management, a governance role for the members, a mandate that is focused entirely on optimal performance and independence from government or any single employer. Defined benefits (DB) are also essential to achieving all of these goals.

In response, the federal and provincial governments ultimately acknowledged in June 2010 that there is a retirement savings gap and that government has a role to play in facilitating the creation of a supplementary pension savings instrument. At that time, the Finance Ministers also proposed to consider a "modest" enhancement to the CPP, an element that, despite repeated calls for progress, has been absent from apparent consideration.

Bill C-25 provides for the creation of Pooled Registered Pension Plans (PRPP's) which were meant to address the needs of the large proportion of Canadians who struggle with saving for retirement.

As currently designed, PRPPs fall short of the core goal of providing a universally accessible and affordable retirement savings vehicle that would help provide an adequate retirement income. PRPPs can be made to help Canadians better save for their own retirement, but only if current design problems are corrected before being offered to Canadians.

## ***Who We Are***

CARP is a national, non-partisan, non-profit organization with over 300,000 members across the country. CARP is committed to advocating for pension reform that will enhance the quality of life for all Canadians as we age into retirement. Retirement security is a principal concern for our members and our advocacy. These are our recommendations to help older Canadians save for retirement.

## **Recommendations**

CARP calls on Parliament to amend Bill C-25 to ensure that PRPPs be designed to mitigate the inherent risk associated with private sector pension plans. This can be accomplished by legislating protections that ensure affordability, benefit adequacy, portability, fiduciary responsibilities, and proper risk management to ensure sustainability:

1. Savings adequacy must be an integral goal of PRPPs.
2. PRPPs should be of a sustainable size and offer benefit portability to plan participants, even during sustained employment with a single employer.
3. PRPPs should offer defined benefits, which are superior to defined contribution plans in cost/benefit and resistance to market fluctuation.
4. PRPPs should operate under regulated maximum Management Expense Ratios (MER) and have governance and accountability mechanisms that properly balance the interests of employers, employees, and retirees.
5. PRPPs should be universally available to the employed, self-employed, and even the unemployed, regardless of whether the employer has enrolled in the plan. Similarly, the plans should be mandatory or based on auto-enrolment, with the possibility for individual opt-outs, contingent upon the inclusion of the above measures.

## **Correcting the Course on PRPPs**

Pooled Registered Pension Plans are an improvement on the status quo, but more must be done to ensure that PRPPs will meet the needs of Canadians who struggle with saving for retirement. As structured currently, PRPPs share many of the pitfalls associated with RRSPs and there is little reason to believe that PRPPs will help Canadians save for retirement more effectively than RRSPs.

- They are not universal or mandatory – employers can decide whether to auto-enroll employees. Employees who are auto-enrolled can opt-out after 60 days.
- There is no guarantee against high costs and fees – the promise of low fees comes only from the potential scale of investment that may be achieved by ‘pooling’. Recent pronouncements suggest that the government will not use the regulatory power contained in Bill C-25.
- It strictly requires a defined contribution (DC) plan; administrators are not permitted to offer a DB plan even if they can and would like to.
- A PRPP will be locked-in, like other DC plans – making it impossible for employees to change plans, should they want a different plan or provider, during employment with a single employer.
- The fiduciary responsibility, which lies with plan administrators, is not sufficient to preclude conflict of interest investments nor does it adequately prioritize the interests of investors.

PRPPs, as currently designed, represent a marginal improvement over RRSPs. The potential for auto-enrolment and the pooled nature of investments is an improvement over the status quo. PRPPs, however, are not yet up to the challenge of helping Canadians save adequately for their own retirement.

## **The Savings Gap**

There is already a significant underuse of private, registered, savings vehicles. Seventy-one percent of Canadians are concerned about the performance of their RRSP, given the current state of the economy and volatility of the financial markets.<sup>ii</sup> Canadians’ confidence is dropping in their ability to save with private, market-based, savings plans.

Approximately 36% of Canadians are not confident in their ability to save for retirement, compared to 18% in 2010. And, 42% are less optimistic about the financial markets this year compared to last year.<sup>iii</sup> RRSPs, simply, have not been the answer to the problem of retirement savings, and in their current form, there is little reason to believe that PRPPs will fill the gap.

- Canadians now contribute \$33.9 billion to RRSPs, which is only 5.1% of the total room available to eligible tax-filers.
- Canadians leave \$630 billion dollars of RRSP contribution room untouched.
- The number of eligible taxpayers has increased, but fewer Canadians contributed to RRSPs in 2010 than did in 2009.<sup>iv</sup>

PRPPs are only a marginal improvement over RRSPs, and Canadians have proven their reluctance to invest through DC savings vehicles with high fees and costs and little fiduciary oversight. To better help Canadians save for retirement and boost their confidence to do so, the federal government must ensure that PRPPs have legislated protections for investors and are designed to reap the highest savings for all Canadians.

### ***Australia's Failed Experiment***

Australia provides a useful precaution in proceeding with PRPPs as currently structured. Australia's pension system, the cornerstone of which is their Superannuation Fund, relies largely on private, defined contribution schemes that resemble PRPPs in many regards.

As with PRPPs, the Australian Superannuation system is based on the assumption that market competition delivers better results and economic efficiency. Mandatory contributions through private banks and administrators have resulted in a substantial growth of contributions, but net returns have been low.<sup>v</sup>

In fact, Australia's superannuation funds were among the hardest hit in the OECD during the first wave of global recession, with real losses of 26.7% in 2008.<sup>vi</sup> Despite the presumed role of competition, Australia's mandatory, DC, employment based pension system has performed poorly. Expert accounts show that the system continues to be restrained by high fees and costs and market competition has added undue complexity to investor choice without producing real returns.

Private, DC plans, have not been the answer in Australia and they are unlikely to be the answer in Canada. More than 25% of Australian seniors live in poverty. This is the fourth highest old-age poverty rate in the OECD countries and more than double the OECD average.

After decades of improvement, the percentage of seniors living near or in poverty in Canada rose by 25% from 2007 to 2008.<sup>vii</sup> It is estimated that approximately 260,000 or about 5-6% of Canadians over 65 still live in poverty.<sup>viii</sup> Canada's public pension system has been credited with the improvements in poverty among seniors over the past decades, but those effects have matured and caution should be exercised before following on the path of countries that have not fared well with private sector experiments.

### ***Canadians are Losing Confidence in Retiring Securely***<sup>ix</sup>

Overwhelmingly, older Canadians preparing for retirement are unsure of their ability to live securely past their working years.<sup>x</sup>

- 72% of pre-retirees are concerned about “maintaining a reasonable standard of living for the rest of their life.”
- Approximately 50% admit to being unprepared for retirement.
- 87% of pre-retirees expect to receive income from government supplements.

Canadians are becoming too familiar with the threat of insecure retirement. Such data suggests that pension reform requires more than minor adjustments. A growing and aging contingent of working Canadians needs proposed pension mechanisms to reflect contemporary challenges. Most importantly, however, 8.4 million Canadians need these instruments to safely and robustly cover existing gaps in savings adequacy.

### ***CARP Members Expect Low Fees, Low Risk, and Defined Benefits***

CARP members do not support PRPPs as currently designed. The overwhelming majority of CARP members insist that PRPPs must feature low fees, as offered by the CPP Investment Board and other large retirement funds. The CPP and most large not-for-profit large pension funds operate at a management expense of less than 0.5%. Private sector savings vehicles, such as RRSPs, exact fees in excess of 2.5%. The resulting difference for investors can be thousands of dollars in reduced retirement savings.

CARP members also expect the government to provide legislated risk controls and protections for investors. Real fiduciary responsibility must be a fundamental aspect of PRPP legislation. Almost two-thirds of CARP members do not trust the private sector to deliver safe, low cost, risk-free pension plans to Canadians and one-fifth of members do not trust the private sector “at all”.

Most CARP members insist that PRPPs should be able to offer defined benefit (DB) options rather than just defined contributions. More than half of CARP members insist that a DB option in PRPPs is “extremely important”.

Members do not trust the private sector to provide safe, low-cost retirement plans. Members prefer the public option and the majority think that an enhanced CPP or another public option has a vital role to play in retirement security, whether along with PRPPs or alone.

### ***Provide Canadians with the Best Means of Saving for Retirement***

CARP members welcome any action that improves on the status quo – which has left many of them with financial insecurity as they face retirement – for their children as well as themselves.

However, they have always favoured a public option to avoid the high costs and lack of accountability in private offerings and strongly supported CPP enhancements. Since the proposal rules out a public option, and call for a Defined Contribution approach, CARP will be looking for legislated protections to ensure affordability, benefit adequacy, portability, fiduciary responsibilities, and proper risk management to ensure sustainability.

## References

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<sup>i</sup> Ambachtsheer, Keith: The Canada Supplementary Pension Plan (CSPP) Towards an Adequate, Affordable Pension for All Canadians. C. D. Howe Institute May 2008

<sup>ii</sup> BMO Financial Group, archived at <http://newsroom.bmo.com/press-releases/bmo-annual-rrsp-study-majority-of-canadians-plann-tsx-bmo-201112080751376001>

<sup>iii</sup> Ibid.

<sup>iv</sup> Statistics Canada, Registered retirement savings plan contributions 2010. Archived at <http://www.statcan.gc.ca/daily-quotidien/111202/dq111202b-eng.htm>

<sup>v</sup> Sy, Wilson. "Redesigning Choice and Competition in Australian Superannuation". Rotman International Journal of Pension Management, Volume 4 • Issue 1 Spring 2011.

<sup>vi</sup> OECD, Pensions at a Glance, archived at <http://www.oecd.org/dataoecd/8/61/43071222.pdf>.

<sup>vii</sup> Campaign 2000, 2010 Report Card on Child and Family Poverty in Canada: 1989 – 2010, 2010.

<sup>viii</sup> Statistics Canada, 2006 Census, *Income Status Before Tax and Income Status After Tax (8) and Economic Family Status and Age Groups (80) for the Persons in Private Households of Canada*.

<sup>ix</sup> CARP poll December 23 - 26, 2010 n= 1300.

<sup>x</sup> Canadian Institute of Actuaries, *Retirement Risk: Defining Retirement Horizons*.