Driving Innovation through the Ontario Retirement Pension Plan

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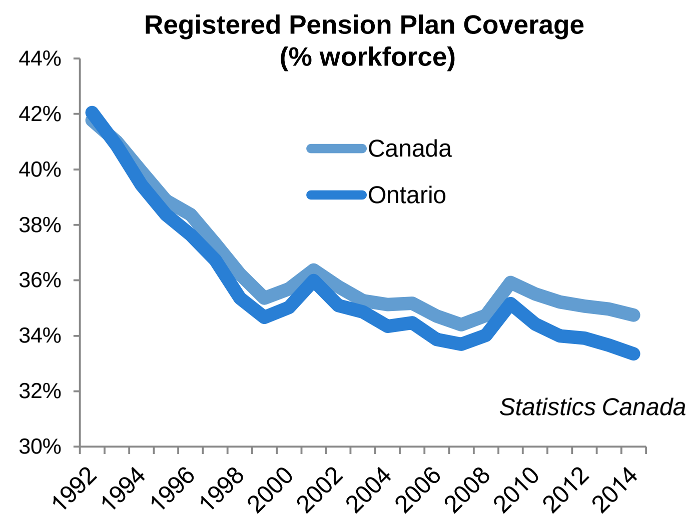
Defining the Problem

Almost one-half of retirees are worried about outliving their money. This anxiety is shared by three-quarters of Canadian who are not yet retired.

Angus Reid Institute (ARI), "Retirement in Canada" July 1, 2015

Since 1966 – when the CPP was created – life expectancy has increased by approximately 10 years for both men and women, adding to the ongoing trend of incremental growth in life expectancy.

Statistics Canada



- Experts recommend that individuals aim to replace between 50% and 70% of their income in retirement.
- In reality, evidence shows that many Canadians are not saving enough, which raises the question on the **role of government** (provider, enabler, something else?)
- Left unaddressed, Canadian jurisdictions will:
  - See future **seniors face financial hardship**;
  - **Experience serious fiscal pressure** through increased government assistance to seniors (which could crowd out needed government investment in education, health care, etc.); and
  - **Miss opportunities for stronger long-term economic growth** if the current levels of retirement savings are not increased.
- In 2014, the government announced it was creating the **Ontario Retirement Pension Plan** (ORPP) to support enhanced retirement benefits for Ontarians.
- The government determined that a **mandatory** (vs. voluntary) plan was necessary to ensure that all working Ontarians would have access to adequate savings in retirement.

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Key Features of ORPP

- In 2014, the government announced it was moving forward with the creation of the **Ontario Retirement Pension Plan** (ORPP) to support enhanced retirement benefits for Ontarians.
- The ORPP was modelled on the strengths and principles of the Canada Pension Plan (CPP) and, where possible, designed to be consistent with the federal *Income Tax Act* and Ontario *Pension Benefits Act*.
- At maturity, the ORPP was expected to cover over **450,000 Ontario-based employers** and approximately **4.5 million employees** and collect over **$6 billion annually** in contributions.
- **The ORPP would:**
  - Require eligible employers and employees to each contribute 1.9% of employee earnings, for a **total maximum contribution rate of 3.8%**.
  - Aim to replace **15 per cent** of an individual's pre-retirement earnings up to **$90,000** based on 40 years of participation.
  - Provide a **retirement benefit** and a **survivor benefit**.
  - Require benefits to be earned as contributions are made.
  - Exempt employees / employers who have **comparable workplace pension plans**.
  - Be treated as a **deduction for tax purposes** for contributing employers and employees.

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Targeted Coverage

<u>Comparable Workplace Pension Plans</u>

- The government's consultations in developing the ORPP revealed that employees covered by a workplace pension plan are often well-equipped to receive a **predictable stream of income** in retirement.
- To account for, and preserve, existing generous workplace plans – while providing access to workers without adequate pension coverage – the government developed the concept of a "**comparable workplace pension plan**."
- Employers offering **comparable plans** would not have been required to participate in the ORPP for those employees participating in their comparable plan.
- To provide employers the opportunity to further enhance retirement benefits for their employees, employers **with comparable plans** would have been permitted to **opt-in t**o the ORPP beginning in 2020.
- A comparable plan was defined as a **registered pension plan** (RPP) that met a **minimum threshold benefit and contribution level** which provided a high likelihood that its members would receive (at least) a **similar retirement benefit** to the ORPP.
- The concept of a comparable plan was anchored in key **ORPP design parameters**, including
    - **Pool longevity** and **investment risk** to protect members from outliving their savings and the volatility of investment returns;
    - Target to replace up to **15 per cent** of an individual's **earnings** over their career; and
    - Require **"locked-in" contributions** and accumulated benefits.
- Comparability thresholds were developed in consultation with actuarial and pension experts for defined benefit (0.5% annual accrual rate), defined contribution (minimum 8% contribution rate, with at least 4% from the employer) pension plans.
- The **ORPP Administration Corporation** (ORPP AC) intended to use an **e-platform** to enroll employers and determine comparability of workplace pension plans.

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Plan Sustainability

- The ORPP was designed to be **sustainable over the long-term** (**100+ years**).
  - Detailed actuarial projections were used to determine that the ORPP would be funded on a sustainable basis at a combined contribution rate of 3.8%.
- Similar to CPP, the ORPP's funded status would have been measured by its contribution rate differential: ***Rate Differential = Current Contribution Rate*** *minus* ***Sustainability Rate***
- *The ORPP Act, 2016* established **funding rules** designed to ensure that adjustments made in response to a funding excess or shortfall would have had a **distributed effect** on active members, retirees and employers.
- To demonstrate sustainability, the **ORPP AC** would have been required to file an **actuarial valuation** of the ORPP **every three years** and to make the valuation public and subject to independent peer review.
- Mirroring the CPP, the government also intended to establish an independent **Office of the Chief Actuary** to conduct actuarial valuations and assessments of the ORPP and provide advice.

Intergenerational Equity

- The ORPP was being designed to **minimize inequities,** providing reasonable intergenerational fairness and minimizing cross-subsidization. For example:
  - ORPP benefits would have been earned as contributions were made to enhance equity.
  - The internal rates of return between the initial cohort and future members of the ORPP were relatively similarly (5.59% and 5.25%, respectively, compared to a much wider differential in existing social security plans).

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Pension Benefits

- The ORPP was designed to provide two core benefits: **a retirement and a survivor benefit.**
- Unlike the CPP, the ORPP would not have offered other benefits such as a disability benefit, death or dependent child benefit.
- **Survivor Benefit**: An ORPP survivor benefit would have been payable to the surviving spouse of an ORPP member or their beneficiary or estate (also unlike the CPP).
  - This reflected the approach of RPPs and was designed to increase fairness to members.
  - ***Pre-Retirement Death:*** If a member died before retirement, a lump sum would have been paid to their spouse, beneficiary or estate.
    - At a minimum this amount would have been equal to the member's contributions + interest.
  - ***Post-Retirement Death (without a spouse):*** If a member retired without a spouse, they would have received a full pension.
    - If the member died within 10 years of retirement, the remaining value of their pension up to 120-months after retirement, would have been paid to their beneficiary or estate.
  - ***Post-Retirement Death (with a spouse):*** A retired member with a spouse would have received a joint survivor pension. The member's retirement benefit would have been adjusted and when they died, their spouse would have received a survivor benefit for life.
    - A member and spouse could also have chosen to waive the survivor benefit and receive a full pension with a 10 year guarantee.

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Regulatory Framework

- The ORPP was being designed to be consistent with the RPP framework under the federal *Income Tax Act.*
- However, this regime would have limited several desired design features of the ORPP and created challenges for administration:
  - **Plan Design:** Self-employed individuals would have been unable to participate in the ORPP and retirees would have been unable to contribute to the ORPP and continue to collect their retirement benefit if they re-entered the workforce after retiring (permitted by the CPP).
  - **Administration:** A number of RPP rules, designed for single employer-sponsored workplace pension plans, would have been a barrier to efficient and effective administration of the ORPP, including restrictive RPP investment rules, impractical information disclosure requirements and restrictions on borrowing for start-up costs.
- **Excellent collaboration** between federal and Ontario officials supported positive discussions to identify acceptable solutions to these challenges. For example, tax treatment of ORPP contributions.
  - Contributions were intended to be **tax deductible** for both employees and employers.
    - Like other RPPs, ORPP contributions would have effected an employee's pension adjustment, thereby reducing the employee's RRSP deduction limit.
    - To support ease of administration, there were ongoing discussions on the calculation of an employee's **pension adjustment** related to the ORPP.

QUESTIONS?