Thoughts on Pension Reform in Canada



By Minaz Lalani, FCIA, CERA

Most of us who work as retirement actuaries do not believe that there will be a revival of Defined Benefit (DB) plans. Only corporations that are oligopolies restricted to local markets, or that have bargained plans, or ones that pass on their costs to ratepayers, multi-employers and public entities will continue with DB plans.

As I see it, there will be little, or no activity in the reinstatement of DB plans, conversion back from Defined Contribution (DC) to DB plans, or setting-up of new DB plans. The merits of DB plans have been articulated by pension experts/actuaries and discussed with plan sponsors, and the views are recognized by plan sponsors as being valid but plan sponsors continue to close DB plans for future hires and establish DC plans. Al Roth, an economist at Harvard University summarizes similar issues by saying, "In theory, there is no difference between theory and practice but in practice there is a great deal of difference." In my humble opinion, in practice, there is little chance of a revival or the return to DB plans. Based on the DB plan experience in Australia and the UK, DB plans will decline as THE retirement vehicle for Canadian workers.

As actuaries we need to 'devise creative solutions'; however, I disagree that we need to become creative in designing the next era of DB plans. Most of us have heard of Benjamin Franklin's famous phrase, "In this world nothing can be said to be certain, except death and taxes." I would like to add retirement and abbreviate the quote to "Nothing is certain, except death, retirement and taxes."

The following are some ideas that could be considered for retooling our ailing pension system: I would like to see RRSP and Money Purchase Plans at the same level playing field. As the term RRSP suggests, it is a vehicle to accumulate savings for retirement. If this is the case, these savings should be locked in (similar to a Money Purchase Plan) and only available to provide pension income.

- The government could institute a payroll tax (call it a Retirement Savings Tax). These deductions would be paid into an individual savings account ("locked-in" RRSP) and be used to provide pension income. This idea is in line with the principle of Libertarian Paternalism (moving people into a direction that will make their lives better - that is to say, protecting them from themselves (refer to the book "Nudge" by Thaler and Sunstein).

- Retirement actuaries should participate in designing Defined Contribution (DC) Plans that provide for adequate retirement income and assist in the management of DC risks.

- The CIA should push financial institutions (via regulatory intervention) to provide for more financial products in the distribution, or de-accumulation phase to allow individuals to access competitive products that protect them from inflation, longevity, interest risks and provide them protection guarantees (yes, similar to annuities but well-priced with flexible and better settlement provisions).

Such ideas are plentiful; the challenge is how we as actuaries can harness the power of retirement

actuaries to implement ideas and tools that truly re-tools the pension system that actuaries can be proud of, and that demonstrates our thought leadership in pension matters.

It is safe to say that all individuals/employees will have a non-working period (retirement) during their lifetime and they will need income to maintain an adequate standard of living. This income can be provided by a plan, we will term Retirement Income Plan (RIP - the acronym should- not to be confused with "Rest in Peace"). Retirement actuaries should become creative in designing the RIP. We should not have pre-conceived notions whether the RIP is a DB, DC, hybrid, or any other design not yet imagined. The retirement business is not declining- it will always be there—what it looks like, and how it is shaped is our challenge- retirement actuaries should rise to this challenge and design the RIP. The CIA should lead this charge and once the RIP is designed, it should put its energy and resources into ensuring that policymakers and all stakeholders buy into the design. Are we up for the challenge?

In closing, I would like to share an anecdote worth keeping in mind when we attempt to design the RIP, or re-tool our pension system: When NASA began the launch of astronauts into space; they found out that pens wouldn't work at zero gravity because ink won't flow down to the writing surface. To solve this problem, NASA hired Andersen Consulting (Accenture today). It took them one decade and $12 million. They developed a pen that worked at zero gravity, upside down, under water, on practically any surface including crystal and in a temperature range from below freezing to over 300° Celsius. Guess what the Russians used? Yes, a pencil!

Minaz Lalani, FCIA, CERA, is a member of the Enterprise Risk Management Applications Committee.

Canadian Institute of Actuaries/Institut canadien des actuaires
http://www.actuaries.ca/