THE ONTARIO RETIREMENT PENSION PLAN: BOON OR BUST?

THE ORPP IS A GOOD MOVE

By Hugh O'Reilly

At one time, funding your retirement was straightforward. Most Canadians could count on a decent standard of living in retirement from the three pillars of our retirement income system: the Canada Pension Plan (CPP), old age security and Guaranteed Income Supplement; employer-sponsored pension plans; and their own private savings. Most employer plans were DB, which guaranteed a consistent stream of income for as long as a retiree lived.

Today, those pillars have eroded and cracks are beginning to show. Canadians have had to endure shocks such as the 2008 financial crisis, prolonged low interest rates, the widespread conversion from DB to DC in the private sector and the increasing weight of greater need across the board. Many Canadians are worried about the future—and the likely outcome that their standard of living in retirement will be lower than what their parents enjoyed.

The time is right to shore up our retirement system, and the Ontario Retirement Pension Plan (ORPP) is a step in the right direction. With no clear direction federally to expand the CPP, and the pooled registered pension plan remaining a voluntary option, the best path to improving retirement security for the greatest number of Ontarians is the ORPP—as long as it's DB and mandatory for those without a comparable employer plan.

Although we know the ORPP is coming, many questions remain. Chief among them is the issue of comparability. Should an employer offering any type or level of plan be exempt? My view is, only workplaces offering a DB plan or participating in a multi-employer pension plan should be considered comparable, since the point of the ORPP is to enhance Ontarians' retirement income security.

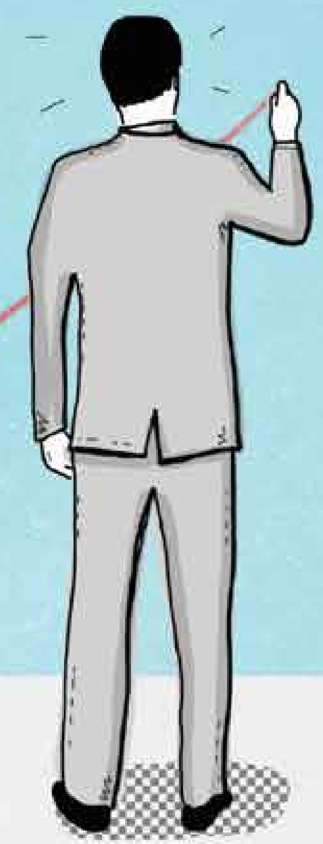
Some companies do offer generous DC plans—but even if they allow participants to save large sums of money, these plans can't be considered comparable to DB. DC plan members can't pool timing and longevity risks. And, as 2008 showed, Canadians' retirement savings can be vulnerable to a market event. People lost years of personal savings overnight. For those who were close to retirement age, there simply wasn't enough time to recover and earn back what they'd lost, through either employment income or investment.

DC plan members who make it to retirement with their nest egg intact are then left with limited, often expensive options to annuitize their savings or the potential that they may outlive their money. The key advantage of the DB model is, it provides a predictable stream of income for the rest of a retiree's life, independent of market conditions on an individual's retirement date.

The impact of financial losses or inadequate savings continues to reverberate through our society. Sun Life Financial's 2015 *Canadian Unretirement Index Report* finds almost 60% of respondents expect to continue working in some capacity after age 65, with 32% expecting to work full time—more than those who expect to be fully retired, for the first time in the survey's history. And of those who intend to work after age 65, 59% said they'd be working because they'd need to.

If Ontario's workers are so well served by existing savings vehicles and employer-sponsored plans, why do they have so little confidence they will be able to fully support themselves with those savings in retirement?

This is where the ORPP comes in.



TURNBULL/GETTY IMAGES

THE ORPP IS GOOD IN THEORY, BAD IN PRACTICE

By Joe Nunes

Over the years, a growing chorus of voices has been pleading with the provinces to lighten up on the overburden of pension regulation and give employers a fighting chance to provide a DB promise. Unfortunately, the province didn't listen—which hasn't been great for many DB plan members, because the punitive regulatory system has put the majority of private sector DB plans out of business.

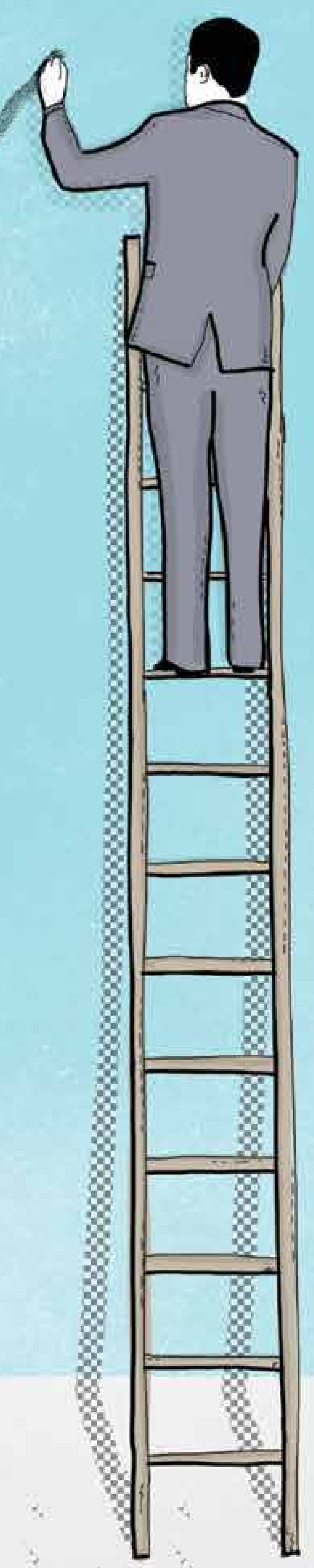
At first, the provinces seemed content to let the newly minted DC programs that replaced DB plans do their intended job of providing workers with a decent pension in retirement. Unfortunately, the same actuarial assumptions that failed to properly fund DB plans have failed to generate sufficient retirement income for DC members.

Recognizing that individuals and their employers are not saving enough for retirement, Ontario has been lobbying the federal government to expand the Canada Pension Plan (CPP). Unable to convince the feds that expanding the CPP was a good idea, some politicians tried to play a game of chicken: "If you don't work with us to expand the CPP, then we will build our own mini-CPP." Unfortunately for Ontario taxpayers and businesses, the province lost, and it's now very visibly committed to the Ontario Retirement Pension Plan (ORPP).

I have trouble understanding why there isn't more public outrage about the ORPP. The only thing I can suggest is, people are too busy to really dig into something that sounds simple (more income when I retire!) but is, in fact, very complicated. While I appreciate what the Ontario government is trying to do, I have a number of concerns with its approach.

The current proposal requires contributions from low-income workers. But with old age security (OAS), CPP and guaranteed income programs, it's unlikely these workers will be in dire circumstances at retirement relative to what they experienced in their working years.

The ORPP also requires full funding, which will mean either a 40-year-plus phase-in of full benefits or an acceleration toward full benefits where older workers benefit at the expense of future generations. The children and grandchildren of the baby boomers already face a less prosperous future and, in my opinion, shouldn't be burdened through additional intergenerational transfers of wealth. I worry it will be too tempting for the government to promise benefits today and push the costs to



"KICKING THE RETIREMENT CAN DOWN THE ROAD TO ANOTHER GENERATION ISN'T AN OPTION. WITH THE ORPP, WE'RE TAKING BOLD STEPS INTO UNCHARTED TERRITORY, BUT I'M CONFIDENT THEY'RE THE RIGHT STEPS."

Do we really want saving for retirement to be like playing a dangerous lottery in which you hope timing will be on your side? Or do we want a future where most people can depend on a secure basic level of income in retirement—one they've helped to fund?

On its own, the ORPP won't provide enough income to fund an individual's retirement, nor does it intend to. What it *will* do is increase the amount of secure income retired Ontarians have overall. It shores up one pillar and takes pressure off the other two.

Businesses are concerned about increased costs, but we need to ask what the cost will be to future generations—and to our economy—if we sit back, do nothing and hope for the best. It will be unfortunate and short-sighted if employers choose to scale back or eliminate their existing plans when the ORPP is in place: there's a reason we have more than one pillar in our retirement system. Ensuring retirees have incomes that allow them to participate meaningfully in the economy is good for everyone.

The ORPP could be implemented in a very cost-effective way for Ontario taxpayers. For administration, a highly effective and tested system already exists for the CPP—a system Ontarians have already paid for. My view is that Ontario should, for a fee, be given access to and allowed to use the existing CPP administration platform.

I also believe the ORPP doesn't need to have a full bricks-and-mortar structure. There are ways to design it to be more virtual, as it draws upon the expertise already existing in some Ontario plans.

Developing a full internal investment capability is not necessary for the ORPP Administration Corp. This cost can be avoided by using the investment expertise of some of Ontario's jointly sponsored pension plans. Ontario's large DB jointly sponsored public sector plans are global leaders in what they do, both as investors and as pension administrators. Pension plans around the world look to our model for an example of how to get pensions right, and we can bring that expertise to the ORPP for the benefit of everyone in Ontario.

Kicking the retirement can down the road to another generation isn't an option. With the ORPP, we're taking bold steps into uncharted territory, but I'm confident they're the right steps. The ORPP will improve retirement income security and give a broader universe of Ontarians the means and confidence to retire with dignity. These are worthy goals—and worth the cost and effort it will take to make them reality.

Hugh O'Reilly is president and CEO of OPTrust.
horeilly@optrust.com

"I WORRY IT WILL BE TOO TEMPTING FOR THE GOVERNMENT TO PROMISE BENEFITS TODAY AND PUSH THE COSTS TO TOMORROW—ALL DISGUISED IN ACTUARIAL ASSUMPTIONS THAT WILL TAKE DECADES TO PROVE RIGHT OR WRONG"

tomorrow—all disguised in actuarial assumptions that will take decades to prove right or wrong.

Note also that the current proposal establishes a "pension plan" in Ontario—not a social program. As a result, there is no mechanism to access the favourable tax treatment of the CPP without co-ordinating this program with other tax-assisted programs defined under Canada's *Income Tax Act* (ITA). This means the ORPP will need to be integrated with the pension adjustment system for determining worker eligibility for other programs such as RRSPs, registered pension plans and profit-sharing plans. Essentially, for many workers who have reached the maximum savings threshold under the ITA, it won't generate any new savings. Savers are only changing where those savings are invested.

Because Ontario is travelling this road alone, there's no opportunity to leverage the infrastructure the federal government has put in place for the CPP—an infrastructure that allows for collecting and investing contributions as well as determining and paying benefits. The administrative operation of the CPP is large and complex, and it will be difficult for Ontario to replicate these services. It takes $600 million a year to run the CPP—in fact, one Fraser Institute study suggests the real number might be more than three times that amount.

Finally, an Ontario-only solution with exemptions for certain employers and their workers means the program will not have as much critical mass as an expanded CPP. Broad participation is very important as a way to spread the governance and administrative costs over as many members and dollars as possible. Currently, DC plan sponsors are not targeted for exemption, but there has been heavy lobbying by this group. And if they're exempt, it will mean even fewer participants sharing the cost of this boondoggle.

The reality that few people want to face is, in a low interest rate environment, it's very expensive for employees and their employers to fund an adequate retirement income. In this context, the fact that Canadians are undersaving for retirement is no surprise.

I'm skeptical the ORPP will work—even if Ontario includes every worker and works with the federal government to get favourable tax treatment as well as a beneficial arrangement for the program's administration and investment. But if the ORPP is to have any chance of working, these are the necessary steps the government needs to take.

Joe Nunes is president of Actuarial Solutions Inc. joe@actuarialsolutionsinc.com