



Article from

Pension Section News

September 2015
Issue 87

Increasing Retirement Age: Report of the CIA Task Force

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In 2012, the Canadian Institute of Actuaries (CIA) created the Task Force on Retirement Age to conduct a review of issues related to retirement ages in light of evidence of Canadians' increasing life expectancies and apparent willingness to work longer. The CIA requested a document that discussed the consequences, reasons, pros and cons, and the transition issues of raising the retirement age for many well-known Canadian public and private sector arrangements.

The task force completed its review and issued a report in May 2013 as [CIA Document 213038](#). It concluded that it would be difficult to recommend one retirement age, formula or approach, deciding instead to assist the CIA to take a position on the issue in terms of presenting considerations for determining appropriate retirement ages. The task force report discusses the effect of raising the retirement age for the following plans/programs in Canada and related transition issues in light of certain key impacts:

1. Old Age Security/Guaranteed Income Supplement (OAS/GIS)
Impact: the projected cost of these programs as a percentage of gross domestic product (GDP)
2. Canada/Quebec Pension Plan (C/QPP)
Impact: effect on long-term contribution rates
3. Defined benefit (DB) plans
Impacts: early retirement subsidies in public plans (especially federal) and legislative provisions imposing constraints on retirement-age changes
4. Defined contribution (DC) plans
Impact: effect of increased longevity
5. Other government income programs—health coverage
Impact: long-term cost

The overall conclusion of the task force was that no true crisis exists in any of the five programs reviewed with respect to retirement age, for the following reasons:

- a natural tendency for retirees and employees to adjust to demographic shifts without legislation;
- no anticipated increase in the projected cost of OAS/GIS or contribution rates to the C/QPP due to stability in the average age at which pensions commence;
- the limited degree to which health care costs increase purely due to aging;
- a decreasing percentage of the Canadian population eligible to receive lucrative early retirement subsidies in private defined benefit plans; and
- existing members of public service plans being largely unaffected by or subject to any meaningful change in their plans.

BACKGROUND INFORMATION AND DEFINITIONS

The task force established the following definitions:

- **Retirement age:** the age at which workers elect to retire, which is evidenced by exiting the labor force
- **Entitlement age:** the age at which a recipient is entitled to retirement benefits under a particular plan or program (but perhaps with a reduction from “full” benefits)
- **Baby-boom generation:** the cohort in Canada born before and after the peak in live births in 1959 (some variations in beginning and

ending year exist); certainly, it was agreed that baby boomers would all be 65+ by 2031

- **Aged-dependency ratio (ADR):** the ratio of those age 65 or more to those age 20 to 64

The report includes a number of graphs illustrating increases in the age of Canada's population and Canadians' life expectancy from 1921 through 2006. The aging trend is primarily due to a number of factors: ever-improving life expectancy, continued aging of the baby-boom cohorts, and the low fertility rate of Canadian females now at 1.68 children per female, well below the rate of 2.1 required for population replacement. In addition, recent mortality studies suggest that mortality improvements for individuals over 65 of 0.5 to 1.0 years every 10 years. A surprising conclusion from the data is that the median age of the Canadian population is expected to remain stable and to start decreasing very slightly and very slowly only after 2050 if at all, after the baby-boom generation has passed. The passing of the baby boom is offset by the ever-increasing life expectancy of the remaining population. Table 2 of the report, reproduced below, shows the profile of the Canadian population over the next 20 years. It illustrates the rapid shift in Canada's demographics and that those 65+ will represent almost 25 percent of the Canadian population by 2036.

Age	1956	1976	1996	2016	2036
Under 20	39.4%	35.6%	26.7%	21.1%	20.2%
20-64	52.9%	55.8%	61.1%	62.4%	55.0%
65+	7.7%	8.6%	12.2%	16.4%	24.8%
ADR	14.6%	15.4%	20.0%	26.3%	45.1%
Inverse ADR	6.8%	6.5%	5.0%	3.8%	2.2%

The affordability of social programs in Canada depends upon the ADR. Table 3 of the report shows the ADR and inverse ADR.

Year	ADR	Inverse ADR
1956	0.146	6.9
1976	0.141	7.1
1996	0.200	5.0
2016	0.263	3.8
2036	0.451	2.2

Based on the above tables, Canada has a rapid shift in ADRs, which may impact the affordability of Canada's social programs. Canada can afford these programs but only in a growing Canadian economy. Canada has the second highest increase in the aged-dependency ratio between 2010 and 2050 of the Organization for Economic Cooperation and Development (OECD) nations. Only Italy's is higher. Canada is higher than both the United States and United Kingdom.

PROJECTED COSTS OF SOCIAL SECURITY

The two most important social security programs in Canada are the OAS/GIS and C/QPP public retirement programs, and health care.

OAS/GIS costs are paid from general revenues (from taxpayers). Currently \$36.5 billion (2012), this cost is projected to increase to \$108 billion in 2030

(41 percent increase from baby-boomer retirements, 32 percent from longevity increases and 27 percent from inflation). OAS/GIS increases with the consumer price index (CPI), a standard measure of price inflation. Meanwhile, GDP, from which OAS/GIS are paid, normally increases faster than CPI. As a result, and notwithstanding projected increases in the ADR, OAS/GIS costs as a percentage of GDP are projected to remain relatively stable, increasing from 2.3 percent of GDP currently (2012) to 3.1 percent in 2030 and then returning to 2.6 percent of GDP in 2050. Changes to the OAS/GIS retirement age from 65 to 67 has mitigated some cost increases but further changes in the retirement age should not be necessary to maintain cost stability. Similar cost stability is reflected in projections for the C/QPP programs in the 25th CPP and QPP actuarial reports. The CPP is sustainable at 9.9 percent of pay and QPP at 10.8 percent of pay (as at 2017). The CPP has adjusted its early/late adjustment factors to reflect increases in life expectancy.

With respect to health care, it is well established that costs rise with age. However, the cost impact of aging is only about 1 percent per capita per year and most reports on the impact of aging on health care costs in-

dicating that even a low level of economic growth can support an expansion of health care services. Further, with increases in longevity, health care costs that occur toward the end of life are delayed and aggregate health care expenditures are pushed downward. Therefore, as far as population aging is concerned, health care costs are sustainable.

RAISING THE ENTITLEMENT AGE AND PUBLIC POLICY

A question arises as to whether it would be good policy to raise the entitlement age, i.e., normal retirement age of Canada's social security programs, notwithstanding their cost sustainability based on the analysis provided in the report. To address this question, reference is made to a 1999 paper prepared by Brown and Bilodeau in which a model is developed to determine a macroeconomic indicator of an optimal age at retirement. This model was based on a fraction for which the numerator is total demand for consumption of goods and services by all members of society and the denominator the total supply of goods and services by the country's working population. The balancing variable in the model was the retirement age and the model projected that from 2017 to 2034 Canadians should retire between ages 60.3 to 60.9 to keep supply and demand of GDP in balance.

Brown and Bilodeau noted that the denominator of this ratio can increase with increases in the labor force (e.g., due to increases in immigration or the rate of labor force participation)

or increases in capital investment leading to higher rates of productivity growth (currently 0.9 percent per year). Brown and Bilodeau's analysis indicated that with a 1.29 percent increase in productivity, no increase in retirement age would be required to maintain equilibrium. With flat productivity, the retirement age would need to rise to only 65.7 by 2046 for equilibrium. Essentially, from the model's perspective, no change in retirement age would be needed to maintain balance, although Brown and Bilodeau indicated that due to increasing life expectancies, male and female retirement ages would need to increase from 65 currently to around 74 by 2041 to maintain a constant period of payout for social security benefits (i.e., equal to 1966 levels when the C/QPP were introduced).

THE SHIFT IN RETIREMENT AGE PRIOR TO ANY CHANGE IN OAS ELIGIBILITY AGE

The average age at which people leave the labor force has been 63.4 for men and 62.2 for women (2009). These ages are expected to increase to 64 by 2030. This is not expected to impact the economy, as many retirees have continued to work in some fashion and continue to contribute to the economy. The percentage of working retirees age 60-65 in 2006 was 22.7 percent for men and 13.1 percent for woman.

The task force report contains some analysis on retirement ages and the transition from work to retirement, citing a

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study by the Régie des rentes du Québec in which the retirement age was defined as the age after which 50 percent or more of a person's income comes from retirement pensions and savings rather than employment income. The Régie observed this age to be between 59 and 60 (later for self-employed workers). The report also covers some general trends in retirement ages and income, employment status and working in retirement as well as data from OECD countries on retirement ages.

The report also reviews a number of international reports, concluding from the data that “we should expect that Canadian workers will stay in the labour force longer, regardless of public policy.”

RECENT CHANGES TO OAS/GIS AND C/QPP

In 2012, the Canadian federal government introduced changes to the OAS/GIS to increase the eligibility age and introduce the option of delaying retirement. The eligibility age for the basic OAS pension and GIS will increase gradually from 65 in April 2023 to 67 in January 2029. The Spouse's Allowance eligibility age will increase from age 60 to age 62. Starting July 2013, the OAS pension can be deferred for up to five years with an actuarial increase of 0.6 percent per month of delay, with the objective of encouraging longer labor force participation.

The normal C/QPP retirement age is 65. Pensions can start earlier or later by up to five years with a constant 0.5 percent per month adjustment

factor. Starting in 2011, the adjustment factor for early retirement was gradually increased to 0.6 percent per month over the period Jan. 1, 2012, to Dec. 31, 2016. For postponed pension commencement, the increase adjustment factor will grow to 0.7 percent per month for retirements on and after January 2014, as indicated in the following table.

Effective date	Decrease factor	Increase factor
January 2014	0.56%	0.70%
January 2015	0.58%	0.70%
January 2016	0.60%	0.70%

This means that in the future, if a person starts a CPP pension at age 60, it will be reduced by 36 percent. Pension payments starting at age 70 will increase by 42 percent. Slightly different rules apply to QPP benefits.

In addition, the Work Cessation Test was removed. Now for both the CPP and QPP, additional contributions are required with slightly more pension benefits earned (actuarial equivalent). For the CPP, the report notes that for each additional year the retirement age is increased, it will result in 0.3 percent lower contributions.

RETIREMENT AGE AND DB PENSION PLANS

Defined benefit plans may encourage early retirement by allowing unreduced pensions to be paid before normal retirement age (usually 65) if certain age and service criteria are met. Alternatively, plans may not encourage early retirement by not offering such incentives.

In the public sector, DB plans cover 82 percent of the workforce and participation rates are high with age 60 as a typical retirement age.

Unsurprisingly, early retirement incentives are popular among plan members and unions and, sometimes among employers for downsizing programs. However, many of these incentives have been removed over the last 10 to 15 years with the result that workers have deferred early retirement for a variety of reasons including insufficient pension savings, high levels of economic uncertainty and job enjoyment.

Most defined benefit plan members retire within one or two years of the plan's unreduced retirement age, subject to applying some common sense comparison of the pension payable versus employment earnings to be forgone on retirement.

The report incorporates a thorough review of early retirement incentives in defined benefit plans. The report notes that in the 1980s and 1990s, employees wanted “Freedom 55” and to abruptly stop working whereas employers benefited from younger, better-educated employees entering the workforce. Employers could afford the significant costs of early retirement pensions due to high interest rates and rapid economic growth.

The report notes that conventional wisdom has evolved, with employees taking more inter-

est in longer careers, wanting to work longer and looking for more gradual transitions through phased retirement versus abrupt work stoppage. For employees, retirement age is increasingly a personal choice. For their part, employers are increasingly motivated to retain knowledgeable and experienced staff, to contain the cost of subsidized early unreduced pensions and to sponsor scalable pension plans to meet the needs of a scalable workforce. In the private sector, only one-third of employees have a workplace pension plan with only 20 percent participating in DB plans, most of which are expected to adjust their retirement age and eligibility ages in an actuarial neutral way, similar to CPP and OAS plan changes. In the public sector, DB plans cover 82 percent of the workforce and participation rates are high with age 60 as a typical retirement age. The report suggests that early retirement incentives in public sector pension plans are unlikely to change due to taxpayers being poorly informed about their cost and pensions being considered part of the “deal” for working in the public sector—i.e., slightly lower pay than in the private sector compensated by generous guaranteed pensions. In addition, and unlike private sector pensions, public sector pension costs are not valued on a marked-to-

market basis with the result that their true costs are understated or incorrectly valued.

The report suggests that in terms of public policy and the sustainability of pension plans, Canada's problems are less severe or dire due to low public debt, abundant natural resources, strong banking systems, partially funded C/QPP plans and modest public pension benefits. However, population aging is still an issue in Canada, which could be addressed by some combination of later retirement, less private borrowing and more retirement savings. The report suggests that the high cost of early retirement incentives could be addressed by amendments to the Income Tax Act to remove permitted subsidies for early retirement benefits (e.g., the 30/60/80 value),

or through collective bargaining changes with public sector unions to reduce contributions and early retirement incentives. The report notes that some changes have occurred in the public sector, including 50 percent cost-sharing, conditional indexing, shared-risk pension plans and gradual increases in retirement ages.

RETIREMENT AGE AND DC PENSION PLANS

By definition, defined contribution plans, registered retirement savings plans or other capital accumulation type plans do not provide a guaranteed pension at retirement. Instead, an individual's retirement income from these vehicles depends upon their accumulated contributions, investment income and bond yields if or when annuities are purchased.

Consequently, in a DC plan, any age is an unreduced retirement age. If individuals defer retirement and market rates and investment income are favorable, retirement incomes can increase. Earlier retirement and/or poor investment performance will result in less retirement income. The report notes that DC plan benefits are easily portable. Members typically work for multiple employers in a career, are often self-employed, and work as contract employees or part time. The report addresses DC retirement ages minimally, concluding that they are probably driven by social security retirement ages more than by anything else.

With respect to other government programs (provincial welfare, workers compensation, employment insurance, LTD

and STD almost all of which are provincially funded) raising the retirement ages beyond 65 will mean those programs cover older workers and become more costly. This provides little incentive to the federal government to be concerned.

In conclusion, though there is a trend for longevity increases in Canada and there are some public policy reasons to entertain increasing retirement ages under various Canadian programs, there is still no compelling reason to do so with a broad-brush stroke in Canada. ■



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