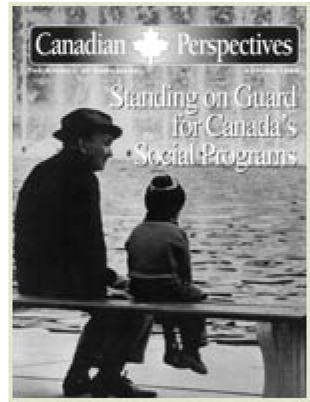
Public Pensions

1995-1998



In the early 1990s, the Chrétien government proposed restructuring Canada's already tattered public pension system with a new Seniors Benefit. The legislation would have slashed seniors' retirement benefits by thousands of dollars and created more poverty among the elderly. Working with citizens across the country, the Council launched a massive three-year campaign - involving a petition that drew half a million signatures - which helped defeat the legislation.

Canada's Public Pension System: Myth and Reality About Our Aging Population

Previous generations of Canadians fought hard to win universal public pensions both to recognize the contribution senior citizens have made to our society, and to provide the elderly some measure of comfort in their retirement years. Moreover, like all public programs and services, our pension system is an important tie that binds us together as a nation. It is an expression of our collective commitment to one another and to the fundamental democratic principle that all citizens have the right to services that enrich us all.

At a time when our nation, indeed our world, is becoming increasingly privatized and fragmented, it is well worth remembering the importance of public services. Public services, unlike those traded in the private marketplace, are not just commodities to be bought and sold. They are not goods that some may possess while others are dispossessed of them. Public programs, like our pension system, represent more than the needs they meet. They are visible expressions of our collective desire to provide for one another.

Today, the government's plans to overhaul our public pension system comes at a critical moment in our nation's history. Not since the Great Depression have so many Canadians been so pessimistic about their own futures and the future of the nation. Facing stubbornly high rates of unemployment, a declining standard of living, environmental degradation, and relentless attacks on our social safety net, there is little wonder why we are gripped with such a profound sense of pessimism.

Governments and corporate-backed think-tanks are exploiting our fears about the future by spinning tales of terror about our pension system. The Canada Pension is broke, they claim. They say the aging of the population will bankrupt the next generation. People should rely on their own savings and not look to government for handouts, they tell us.

We believe there is an urgent need to counter this irresponsible rhetoric. To set the record straight, the Canada Pension Plan is not broke. As a pay-as-you-go system, the CPP cannot be broke. It is true that an aging population will increase the costs of our public pension system, but these increases are both sustainable and affordable. Compared to private plans and RRSPs, Canada's public pensions provide far better value and coverage. Virtually all of the labour force is covered by public pensions and that makes them fare more effective in ensuring income security for seniors. By contrast, only about one-third of Canadians have been able to contribute to a personal RRSP plan.

Public pensions, unlike most private plans, are also portable and move with people from one job to another. They are fully indexed to inflation and offer survivors' benefits. And because public pensions are universal and publicly run, administration costs are extremely low -- about 1 per cent of total benefits.

There is, of course, need for changes to our public pension system. Benefits are still low and need to be strengthened. However, the proposals put forward from the government in recent months would actually undermine the security of most senior citizens.

Response to the Federal-Provincial Information Paper for Consultations on the Canada Pension Plan

In February of this year, the federal and provincial finance ministers issued "An Information Paper for Consultations on the Canada Pension Plan" outlining a number of proposals to reduce program expenditures and raise contribution rates. At the heart of the information paper is the belief that the CPP is facing a 'sustainability' and 'affordability' crisis due to a number of factors: the aging of the population, continuing slow economic growth, the

There is always a political judgement involved in deciding whether our public pension programs are sustainable or affordable. What is surprising in the current context, however, is that the government has offered no solid evidence to support its contention. For instance, in the 1995 Budget, it is pointed out that OAS and CPP expenditures expressed as a percentage of GNP will increase from 5.3 per cent in 1993 to a little more than 8 per cent in 2030 -- an increase of less than 3 per cent despite the fact the number of retired Canadians will double. In light of this, it is absolutely foolish and irresponsible to suggest that our public pension system will bankrupt us.

It is true that costs will rise, but the government has terribly exaggerated the breadth of these increases. In fact, the 8 per cent of GNP that Canada will pay in 2030 is less than the current national average on similar programs in the OECD countries, including that of the United States. Why consider cutting a pension plan that is already so much smaller than in any other industrialized country?

The sensible option is to modestly increase the CPP contribution rate slowly over the next decade. A joint employer-employee contribution rate of 12.2 per cent, an increase of 5.6 per cent of total, would help us sustain the CPP. Because increases are shared between employers and employees, Canadians will be asked to contribute an extra 2.8 per cent of their pensionable earnings to maintain the integrity of a publicly-financed, fully-indexed, portable and universal pension system. For a maximum of $1,360 a year -- much lower than what most people pay for car insurance -- we can maintain a plan that provides Canadians with a retirement income equal to one-quarter of their insurable earnings. Few pension plans, either public or private, can boast such benefits for such a modest cost.

What's Wrong With the Government's Proposals?

The federal-provincial discussion paper sets a dozen ways in which the CPP could be cut back. The Council of Canadians strongly rejects the proposal contained in the consultation paper to reduce or eliminate the Yearly Basic Exemption (YBE). As this exemption currently allows some progressivity in the system by allowing those with low incomes to pay a smaller portion of their income in CPP contributions, the reduction or elimination of the YBE would disproportionately harm low-income earners.

The federal-provincial discussion paper also suggests raising the retirement age from 65 to 67. The difficulty with this option is that it again harms those with lower incomes. Since the age at which one retires is directly linked to one's income, those with higher incomes and thus higher retirement savings retire well before age 65. Those with lower incomes are forced to stay in the labour force longer.

Another major concern is that raising the age of retirement will make it harder for younger workers to find jobs because older workers would be forced to work longer.

The Council of Canadians also rejects recommendations that CPP benefits be reduced from the current 25 per cent replacement rate to 22.5 per cent. CPP benefits are not overly generous by any measure: the maximum benefit is only $8,560 per year. The seniors who would be most affected by reduced CPP benefits are those who rely almost entirely on government sources of income and who are already at or near the poverty line.

Furthermore, the federal-provincial paper suggests changing the fully-indexed nature of CPP to a partial indexation to inflation. This is perhaps the most substantial and regressive reform proposed. It would yield greater savings than any other measure proposed, but it would so by greatly reducing the real value of pensions seniors receive by 1 per cent per year.

Finally, the discussion paper offers a big carrot to the private pension industry. It suggests future CPP investment funds could be managed by private sector investment managers and invested in private sector companies. At a time when Canada's public infrastructure is in dire need of attention, it is odd the government would suggest redirecting funds to the private sector where the profit motive, rather than the public interest, will dominate. Moreover, public administration of the CPP fund has resulted in low operating costs. What will the costs be of turning over administration to the private sector?

The key to paying for public pensions is to address the real threat: unemployment. The basic issue has less to do with the aging of our population than with high levels of joblessness and stagnating wages caused by the disastrous economic policies of the past decade. Since funds for OAS come from tax revenues and CPP is financed by premiums paid by the current working population, high unemployment threatens our ability to fund our social programs.

The government, in fact, has admitted so much. The paper on the Seniors Benefit (p. 24) makes the following observation: "Slower growth in productivity and wage levels will compound the demographic problem by reducing the capacity of working age Canadians to finance growing pension costs. It would simply not be reasonable to count on a return to the high wage growth or high labour force growth of the 1960s and 1970s to make our public pensions affordable."

Here, in a rare and candid display of honesty, the government has openly admitted that the policies of free trade, deregulation, privatization, social spending cuts, and high interest rates have and will continue to fail Canadians. Surely, it is time to recognize that what the economy needs is a fundamental shift away from the current market liberalization agenda, toward a full employment strategy.

A focus on job creation also helps quell concerns about pitting one generation against another. In its discussion paper, the fear is raised that Generation 'X'ers' will refuse the pay for the baby boomers when they retire. However, this perspective ignores the fundamental issue: Generation 'X'ers' don't need lower CPP contributions in twenty years time. With official youth unemployment hovering near 16 per cent, young people need jobs now. And they will need public pensions in the future. To sacrifice the future benefits of young Canadians is not a way to build solidarity between generations.

The Seniors' Benefit

When the Liberals were in opposition, they strongly condemned the Mulroney Conservatives for clawing back OAS payments, and in so doing ending the universality of the program. At the time, Jean Chrétien reminded us that Canadians needed universal pensions so that benefits would be seen as a right of citizenship, not a hand-out given to those the government deems deserving. With the last federal budget, the Liberals have proven they are a party without memory and without shame.

By ending decades of official Liberal policy and killing the universality of public pensions, Finance Minister Paul Martin's 1996 budget rolled back the gains of previous generations and left many Canadians wondering how the changes will affect them. The pension cuts are particularly worrisome for the one-third of Canadian seniors who live in communities with populations of 10,000 or less. These small town and rural areas are already suffering disproportionately from cuts to health care, post-secondary education, social assistance and unemployment insurance announced in last year's budget.

Under the Liberal pension reforms, Old Age Security (OAS) and the Guaranteed Income Supplement (GIS) will be folded into a new package, the Seniors' Benefit. Although Martin claims most of us will be big winners under the new system, the Seniors' Benefit will provide payments to far fewer Canadians. In fact, the government's plan will only marginally help some seniors and will make many others worse off. As policy analyst Leonard Shifrin concluded, not even the Mulroney government at its worst produced such a fraudulent policy document.

The details reveal when the proposed Seniors' Benefit is in place, total pension payments will be 10 per cent less than under the current system. The very poor will see only a minor increase in benefits of $10 a month, or just 1 per cent. In 2001, the year the new plan comes into force, the maximum benefit will be $11,420 for a single person, well below even today's poverty line which is pegged at $15,452.

As those at the lower end receive a few extra table scraps, couples and particularly married women will be significantly worse off. That's because eligibility for the new Seniors' Benefit, unlike OAS, will be calculated on the basis of the combined income of both spouses.

Take the case of a wife with no independent income of her own. Under the new plan, she will begin losing her pension entitlement when her husband earns more than $40,000 a year. With the current OAS system, however, she would still enjoy some financial independence by receiving a pension of $394 a month regardless of what her husband earns.

Can we afford universal public pensions? The answer is yes, if the political will exists. For instance, while CPP, OAS and GIS will bear the brunt of the government's axe-wielding, no really significant tax changes are planned to make sure corporations and the very wealthy shoulder their fair share of deficit reduction. In fact, buried amidst the dry accounting language of the latest budget are plans to offer oil companies hundreds of millions of dollars in new tax breaks.

As well, the government has done little to address the multi-billion dollar tax assistance awarded to private retirement savings. RRSP tax breaks ate up over $15 billion in lost tax revenue last year, and half of these credits went to the richest 10 per cent of tax filers. In 1995, only someone earning over $80,000 a year could take advantage of the full tax subsidy offered for RRSPs. With each dollar contributed to an RRSP yielding a bigger saving, the tax break for each rich contributor is five times as large as for the bottom 70 per cent of income earners. RRSPs, as currently structured, favour the very wealthy.

Not surprisingly, the big financial companies are the ones pushing for cuts to public pensions because it would force more Canadians to buy private RRSPs, thereby fattening the already bloated profits of the banks. Action on the RRSP front could help us sustain universal public pensions. If we reduced the maximum RRSP contribution to $8,000 a year -- bringing it more in line with what most middle-income Canadians can afford -- the government would save up to $1.5 billion annually.

Conclusion

Public pensions are essential to the well-being of millions of seniors. The CPP, OAS and GIS have done a decent job in combating poverty amongst the elderly. However, despite the impressive gains, current benefit levels remain inadequate. Cast in this light, it is outlandish the government is considering cutting both Old Age Security and the Canada Pension Plan. Clearly, these programs need to be strengthened, not weakened.

Canada's public pension system is smaller and less expensive than in any other industrialized nation. The rhetoric about the affordability and sustainability of the program is nonsense. It is inspired by an agenda to reduce public pensions and push Canadians toward a private RRSP system, exacerbating inequality. A host of powerful financial interests who stand to benefit if public pension protection shrinks have subjected Canadians to a highly effective disinformation campaign. The cost-cutting proposals for OAS and CPP -- proposals that will push Canadians toward private pension plans run by the big banks -- fit squarely with these interests.

Pensions Fact Sheet

Canada's Public Pension System

What are the components of Canada's public pension system?
Old-Age Security (OAS)

- Available to all Canadians who turn 65
- Must have lived in Canada for at least 40 years after reaching age 18 to receive full amount.
- Maximum benefit amount in December 1995 was $394.76/month.

Guaranteed Income Supplement (GIS)

- Paid to seniors whose incomes, not including OAS, are below the poverty line ($15,758 for a single person in an urban centre in 1995.)
- In 1994 about 40% of seniors qualified for GIS.

Spouses Allowance (SPA)

- Paid to 60 to 64-year-old spouse of an old-age security pensioner or to any low-income widow aged 60-64.

The estimated cost of these three transfer payments in 1995/96 is $21 billion.
Canada/Quebec Pension Plan (CPP/QPP)

- Financed through mandatory contributions from employers, employees and self-employed persons.
- 1996 rate is 5.6% of insurable earnings, half paid by employer, half by employee. Self-employed people pay the full amount.
- Contributions are made on insurable earnings, those between the Year's Basic Exemption (YBE) - set at $3500 in 1996 - and the Year's Maximum Pensionable Earnings (YMPE) - set at $35,400.

In 1995 about 10 million Canadians contributed to the Plan with about 3.2 million people receiving benefits of approximately $16 billion.

Do we really need public pensions?

Since public pensions were introduced in Canada the number of seniors living in poverty has decreased significantly. In 1980 the average poverty rate of seniors was 32.8%. By 1993 the rate had fallen to 19.8%.

Despite these gains, many seniors, in particular single women, still live in poverty. In fact, latest figures show an increase in poverty among seniors, largely due to decreasing provincial income supplements for older people who are poor. Without a national public pension, many more seniors will fall below the poverty line.

With our aging population, can we still afford public pensions?

The Canada/Quebec Pension Plan does not cost the federal government any money. It is financed directly from employee and employer contributions.

While benefits for the OAS, GIS, and SPA come from general government revenues, it is estimated that even with our aging population, the costs of these programs will not rise above the rate of economic growth. However, if, as some people have suggested, CPP/QPP is privatized or benefits are significantly reduced, many more seniors will have to rely on OAS, GIS, and SPA benefits in order to survive.

Rather than an aging population, the biggest problem facing our pension system is Canada's shamefully high level of unemployment. Because funds for OAS and GIS come from tax revenue paid by the employed workforce, and because employers and the current working population fund CPP premiums, high rates of unemployment drain government revenues for public pensions.

Is it true the Canada Pension Plan is broke?

CPP is a "pay as you go" plan. The employees of today pay the benefits of current retirees. Therefore there is no fund to "run out". As long as there are contributions there will be a Canada Pension Plan.

In fact, the CPP has traditionally run a surplus, which has been loaned out, to the provinces. Since 1991 the CPP has maintained this reserve at an amount equal to about two years worth of benefits.

Some people say we can save money by privatizing the CPP/QPP. Is that true?
Privatizing CPP/QPP only makes sense if you are very rich and can take advantage of private RRSPs. However, most working Canadians need their public pension plan - only about one-third of Canadians have RRSPs.

As well, privatizing the CPP/QPP will potentially cost the government more. Already, Ottawa is foregoing an estimated $15 billion in taxes per year for private RRSPs. And only 17% of all eligible contributions are currently made. The costs of a private plan would be astronomical. In addition, the administrative costs of running a universal public pension system are much smaller than those of a private plan.

Also, by privatizing public pensions there would likely be an increase in expenditures on income-tested programs such as GIS and SPA, for those seniors who cannot afford to invest in private plans.

Finally, it's important to remember our public system offers many benefits, such as disability allowances, survivors' benefits and protection from inflation. RRSPs and most private pension plans do not.

What is the government proposing?

Gambling that younger Canadians are not willing to pay higher premiums, the government is exploring a number of ways to reduce the costs to CPP/QPP, OAS, GIS and SPA. Some of these include:

- Decreasing benefits

This means many more seniors will live in poverty. In turn, this will cost taxpayers more money for health care services, long-term care facilities, publicly funded home care and subsidized housing. In addition to a straight cut in benefits, other cuts are being proposed. These include reducing disability benefits, and penalizing their recipients by reducing the pension benefits they receive, and introducing partial indexing of benefits and exemptions, rather than the full indexation that now exists. Proposals to reduce survivor and spousal benefits are also on the table.

- Lowering the minimum income exemption

This means the lowest income earners would have to pay a larger share of their earnings in CPP/QPP premiums.

- Ending universality

The government is proposing to roll Old-Age Security and the Guaranteed Income Supplement into one targeted, income-tested benefit, turning it into more of a social assistance/welfare program for those deemed needy.

- Calculating OAS/GIS benefits on combined household income

This would mean that many senior women, who are less likely to have a private pension, might no longer have an independent financial source. This also means that seniors who live with their children may have to be financially dependent on them.

- Reducing drop-out provisions

Currently, pension contributors are allowed to drop from their earnings record 15% of their non-working or low-income years, and an unlimited amount for time spent out of the workforce to care for children. Reducing or capping the amount of years would again disproportionately hurt women and other low-income earners.

- Increasing the eligibility from age 65 to age 67 or 70

Although this is being called "a last resort", it should remain a cause for concern. If this happens, young people who already have a tough time entering the labour market may remain unemployed longer. Furthermore, it will penalize low-income earners unfairly, since those who can afford to retire early will, while others will have to work even longer to qualify for full benefits. For seniors with no other alternative, increasing the eligibility age may also mean they will have to rely on provincial social insurance programs.

- Privatizing

Discussion on privatizing the CPP is ongoing. Some, like the Reform Party and some financial companies, would like to see CPP wound down, and a fully privately funded program emerge. Although this is not likely in the immediate future, it is possible, if not probable, that privatizing some aspects of the CPP is being considered.

If the government doesn't cut benefits, don't contributions to CPP/QPP need to increase?

Yes, CPP/QPP contribution premiums will have to rise. However, even with the proposed increases, public pension premiums in Canada will still be among the lowest of any country in the OECD. And we can moderate the increase by focusing on some alternatives the government has not considered.

What are the alternatives?

- Raise the Yearly Maximum Pensionable Earnings (YMPE)

The government could choose to raise the maximum income amount so those higher income earners would be paying premiums on more of their earnings. This would give the CPP an immediate boost and spare low-income workers from paying more premiums.

- Phase-in retirement

The government could allow individuals to start claiming part of their CPP benefits while reducing their working hours as they approach full retirement. This would allow people to phase into retirement and would have the advantage of maintaining contribution revenue for the CPP for longer periods, while reducing the full payouts of benefits. This would also reduce working hours for older workers, allowing younger unemployed individuals access to jobs.

- Focus on job creation

Unemployment levels, particularly for young Canadians, remain shamefully high. If the Liberal government lived up to its Red Book promises to make job creation its priority, then there would be more people working and contributing to the CPP. This would also mean more people paying taxes to fund the OAS, GIS, and SPA.