Office of the Superintendent of Financial Institutions Canada
Bureau du surintendant des institutions financières Canada

Remarks by Chief Actuary Jean-Claude Ménard
Office of the Chief Actuary (OCA)
Office of the Superintendent of Financial Institutions Canada (OSFI)
to the
House of Commons Standing Committee on Finance
on the topic of:
Measures to Enhance Credit Availability and the Stability of the Canadian Financial System

Ottawa, Ontario
Tuesday, April 28, 2009

CHECK AGAINST DELIVERY

For additional information contact:

Jason LaMontagne
Communications and Public Affairs
jason.lamontagne@osfi-bsif.gc.ca
www.osfi-bsif.gc.ca

OSFI
BSIF

Canada

Remarks by Chief Actuary Jean-Claude Ménard
Office of the Chief Actuary (OCA)
Office of the Superintendent of Financial Institutions Canada (OSFI)
to the
House of Commons Standing Committee on Finance
on the topic of:
Measures to Enhance Credit Availability and the Stability of the Canadian Financial System

Ottawa, Ontario
Tuesday, April 28, 2009

Introduction

Good morning Mr. Chairman, members of the Committee. Thank you for the opportunity to appear before you today to discuss Canada's social security system and how it is faring in the face of today's economic turmoil.

Mandate and Activities of the OCA

The primary role of the OCA is to provide actuarial services to the federal and provincial governments who are Canada Pension Plan (CPP) stakeholders. While I report to the Superintendent of Financial Institutions, I am solely responsible for the content and actuarial opinions reflected in the reports prepared by my office.

The mandate of the OCA is to conduct statutory actuarial valuations of the CPP, the Old Age Security (OAS) Program and other pension and benefit plans covering the federal public service, the Canadian Forces, the RCMP, federally appointed judges and Members of Parliament. Since 2001, we have also performed an annual actuarial review of the Canada Student Loans Program.

Although OSFI is the regulator of approximately 7 per cent of all private pension plans in Canada, accounting for approximately 12 per cent of pension assets, OSFI has no role in regulating the Canada Pension Plan. As the Chief Actuary, my responsibility is not regulation of CPP; rather it is limited to providing regular actuarial assessments on the long-term sustainability of the CPP.

Current Economic and Financial Turmoil

The global financial turmoil has touched countries in all continents. The funded status of pension plans as well as fully or partially funded social security schemes has significantly deteriorated. The average pension fund return for OECD countries was negative 19% (nominal) for the first ten months of 2008. The CPP Fund declined by $13.8 billion over the final nine months of 2008. Still, the CPP assets of $111 billion represent four times the annual benefits paid. In comparison, ten years ago, the assets represented less than two times the annual benefits paid.

In this environment, it is important to reconfirm that the structure and design of the first two pillars of Canada's retirement income system is unique and will allow the OAS Program and CPP to fare better than many of their private pension counterparts. In addition, steady-state funding, which is the partial funding approach employed by the CPP, remains the optimal funding approach for the CPP.

Although the financial markets are currently quite volatile and the value of CPP assets will fluctuate over the short-term, it is the ongoing contributions made by working Canadians in addition to long-term investment performance that will determine the Plan's ability to meet its commitments to plan members.

Three pillars of Canadian retirement income system

At retirement, most Canadians will receive income from one or more of the following pension schemes. The first pillar is the OAS Program which is financed on a pay-as-you-go basis, meaning there is no fund. The second pillar is the CPP which is financed through contributions paid in equal parts by the employer and employees. The contribution rate of 9.9% in 2009 and thereafter will provide Plan assets equal to approximately 25% of the Plan's liability in about 15 years. Thus, the CPP is a partially funded plan. Finally, the Canadian retirement system allows employers and individuals to participate in occupational pension plans and Registered Retirement Savings Plans which make up the third tier.

A diversified funding approach allows Canada's retirement income system to be less vulnerable to changes in economic, market and demographic conditions than systems in countries that use a single funding approach. International organizations view the Canadian approach, based on a mix of public and private pensions, as an effective way to provide for retirement income needs.

According to a Statistics Canada study, as of year-end 2007, Canadian pension assets equalled 138% of gross domestic product. A comparable OECD/World Bank study identifies Canada as one of only seven countries in the world where pension assets exceed 100% of gross domestic product.

Old Age Security Program

The ratio of OAS expenditures to GDP is expected to increase from 2.2% in 2007 to a high of 3.1% in 2030, driven largely by the retirement of the baby boom generation. However, compared to other G7 countries, Canada has shown remarkable budgetary improvements since the mid-nineties. Balancing the budget and taking steps to put debt as a proportion of GDP on a downward track are effective ways to ensure sustainable financing of the OAS which is funded from the Consolidated Revenue Fund.

Despite Canada's return to a budget deficit this year and projections of further economic contraction, it is anticipated that these will be temporary and will not affect the Government's ability to pay future OAS benefits.

Canada Pension Plan

From 2000 to 2019, the net cash flows of the Plan, that is contributions less expenditures, have been and will continue to be positive, resulting in a rapid increase in the Plan's Asset/Expenditure ratio and funding status. These net cash flows will be invested by the CPPIB with a view to maximizing the rate of return without undue risk of loss. By stabilizing the asset/expenditure ratios over time, the partial funding approach helps to ensure that the CPP is affordable and sustainable for current and future generations of Canadians.

Conclusion

In these uncertain times, it is necessary to continue to monitor the financial health of social security systems. In Canada, the next CPP and OAS actuarial reports will be performed as at 31 December 2009 and will take into account the current economic environment as well as the long-term demographic outlook.

The combination of Old Age Security, the Guaranteed Income Supplement and the compulsory contributory pension plans (C/QPP) has contributed significantly to reducing poverty among seniors over the past three decades. The OECD and the Luxembourg Income Study Research Institute consider Canada to be the country which has the least difficulty ensuring the economic well-being of retirees. To quote the Research Institute "The choice of policy is crucial as shown for instance by the low cost but highly target-effective Canadian efforts in fighting elder poverty". With the Netherlands, Finland and Sweden, Canada is in an enviable group of countries where the incidence rate of low income seniors is less than 5%.

I hope that I have succeeded in providing you with a greater understanding of the ability of the OAS Program and CPP to weather the current economic and financial turmoil. I wish to thank you for the opportunity to appear before this Committee and will be pleased to answer any questions you may have.

Thank you.