Ontario Retirement Pension Plan

Key Design Questions

December 2014

Ontario

Associate Minister's Message

In the months since I have taken on the role of Associate Minister of Finance, I have had the chance to speak extensively with people across this province.

This engagement has led me to conversations with business, labour, organizations and associations as well as people, families and communities. While these conversations have produced a diversity of opinion across a variety of communities, there is a consistent, common thread that runs through each.

The undersaving problem is real. There is a gap between what people will need and what they will have.

At a community barbeque this summer, a woman approached me to say that this is the issue that families talk about at their kitchen tables. At roundtables with business, I hear from employers that have concerns for workers who are approaching retirement but haven't been able to save enough. Through conversations with retirees, I hear how their children don't have access to the pensions they did and how they worry about the next generation being prepared for their golden years.

Our current system, while strong, simply is not filling the gap.

In response, our government has taken a major step forward in strengthening our retirement income system. On December 8th, we introduced the Ontario Retirement Pension Plan Act, legislation that would, if passed, help us create a savings vehicle for the people of this province that would help give them the secure retirement future they deserve.

This legislation would lay the foundation for the Ontario Retirement Pension Plan (ORPP). With this paper, we are looking to build on that foundation through engagement on key design questions.

In January 2015, we will host a series of consultations where we will invite a variety of perspectives to provide input on the design details laid out in this paper.

The government is committed to address the retirement needs of a 21st century workforce. The ORPP will provide a predictable stream of income in retirement by pooling longevity and investment risk, and indexing benefits, similar to CPP. Its portability across participating employers will respond to the needs of an increasingly mobile workforce.

We are also placing a high priority on cost-effective administration. To do so, we will create an arm's length entity to administer the plan and leverage the experience of Ontario's highly regarded public pension plans and strong financial services sector.

We are committed to continued engagement leading up to implementation in January 2017. Plan design details, potential future integration with a CPP enhancement or expansion of the ORPP to other provinces and territories are top-of-mind issues. We will be looking for feedback at a later date on delivery, administration and the phased implementation. Ongoing dialogue will be critical throughout this process.

To be clear — our preferred option is still CPP enhancement, something this government has advocated for since 2010. Unfortunately, the federal government has unilaterally shut down discussions on this issue.

We know the cost of inaction is far too high. If the federal government is unwilling to step up, this government is prepared to take action to tackle the undersaving issue.

We know that establishing a strong, effective ORPP requires input from business, labour, associations, young workers, experts, individuals and families. It is essential that Ontarians have the opportunity to participate in designing a pension plan that will make a profound difference in the lives of millions in our province.

This is about securing our collective futures, so we can all retire with dignity. We're taking action now, to ensure a strong economy for the future.

Originally signed by

The Honourable Mitzie Hunter
Associate Minister of Finance (Ontario Retirement Pension Plan)

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About This Paper

The *2014 Budget* outlined the key features of the Ontario Retirement Pension Plan (ORPP) and highlighted that further consultation and analysis were required to finalize the design parameters. In this phase of the government's consultation, the following three key policy areas are discussed:

1. **"Comparable" workplace pension plan:** As indicated in the *2014 Budget,* those working Ontarians already participating in a "comparable" plan would not be required to enrol in the ORPP. A clear definition of what constitutes a comparable plan is required to clarify membership in the ORPP.

2. **Minimum earnings threshold:** The *2014 Budget* stated that the parameters of the ORPP would include a minimum earnings threshold below which contributions would not be required, and that the government would consult on whether this threshold should mirror the Canada Pension Plan's $3,500 minimum earnings threshold (known as the Year's Basic Exemption or YBE).

3. **Supporting the self-employed:** As noted in the *2014 Budget,* the self-employed would be exempt from participation in the ORPP. This is a result of the current rules relating to registered pension plans under the federal *Income Tax Act* and the unique status of the self-employed as both employee and employer. This government committed to consulting on how best to assist self-employed individuals, since achieving a secure retirement future is important for all working Ontarians, including the self-employed.

To guide the conversation, this paper discusses each of the issues and describes the government's preferred approach. It also sets out discussion questions to elicit feedback. Information received through this consultation process will help inform the final design parameters of the ORPP.

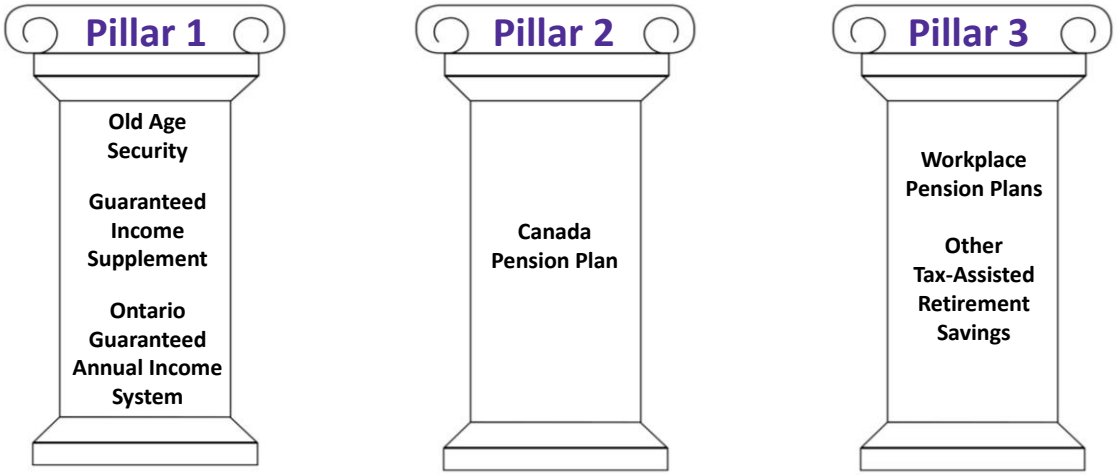
Feedback on any or all of these questions, as well as comments on the ORPP initiative more generally, can be submitted to ORPP@ontario.ca or mailed to:

Ontario Retirement Pension Plan: Key Design Questions
Budget Secretariat
Ministry of Finance
95 Grosvenor Street
3rd Floor, Frost Building North
Toronto, ON M7A 1Z1

Submissions must be received by **February 13, 2015**.

Context

Retirement experts recommend that workers aim to replace 50 to 70 per cent of their working income to maintain a living standard in retirement similar to the one they enjoyed in their working years. Canada's retirement income system is based on three "pillars" that help support seniors in retirement:



Pillar 1 includes publicly funded supplements for seniors. These benefits are based on residency and income eligibility criteria.

Pillar 2 is the Canada Pension Plan (CPP), a mandatory pension program for the employed and self-employed. The CPP is funded by employer/employee contributions as well as investment earnings generated by the Canada Pension Plan Investment Board.

Pillar 3 includes a range of tax-assisted voluntary retirement savings arrangements, such as defined benefit (DB) pension plans, target benefit (TB) multi-employer pension plans (MEPPs)[1], defined contribution (DC) pension plans, registered retirement savings plans (RRSPs and Group RRSPs), pooled registered pension plans[2] (PRPPs) and deferred profit sharing plans (DPSPs).

See *Appendix: Canada's Current Retirement Income System* for more information on each of these retirement saving arrangements.

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[1] Currently in Ontario, many MEPPs offer target benefits, which allow accrued benefits, including pensions in pay to retirees, to be reduced to address funding shortfalls. Single-employer pension plans (SEPPs) may offer target benefits if employer contributions are fixed in a collective agreement, but no such plans currently operate in Ontario. Also, while no distinct TB regulatory framework exists, the government has stated its intention to develop a TB framework for both MEPPs and SEPPs.

[2] The Province introduced the Pooled Registered Pension Plans Act, 2014, on December 8, 2014. This legislation provides a legal framework for the establishment and administration of pooled registered pension plans in Ontario.

The Undersaving Challenge

Canada's retirement income system is working reasonably well for today's retirees. However, a number of studies from pension experts, academics and public policy institutes show that future retirees may not be saving enough for retirement and this gap will likely worsen over time.[3] Recent Conference Board of Canada and Manulife studies show that a growing number of people recognize they are not saving enough for their retirement. There are a number of key factors contributing to the undersaving challenge.

Low Workplace Pension Plan Coverage

In 2012, only 34 per cent of workers in Ontario had a workplace plan, also known as a Registered Pension Plan (RPP). In the private sector, pension coverage was even lower, with only 28 per cent benefiting from membership in an RPP. The reasons for this vary. Many employers — particularly small and medium-sized businesses — have found that workplace pension plans, especially defined benefit plans, are costly and difficult to administer. Other employers have seen their plans hit by low long-term interest rates and poor investment returns, and have had to manage market volatility and unpredictability.

Low Personal Savings

On top of low workplace pension plan coverage, Ontarians are not able to take full advantage of voluntary individual retirement savings vehicles. Only 34 per cent of Ontario workers participated in a workplace pension plan in 2012. Sixteen per cent did not participate in a workplace pension plan but contributed to an individual or group RRSP. In 2012, there was approximately $730 billion in unused RRSP room in Canada, including $280 billion in Ontario alone. Together, this leaves approximately 50 per cent of Ontario workers who did not contribute to either a workplace pension plan or an RRSP.

[3] Kevin D. Moore, William Robson and Alexandre Laurin, "Canada's Looming Retirement Challenge: Will Future Retirees Be Able to Maintain Their Living Standards Upon Retirement?", C.D. Howe Institute Commentary, no. 317 (December 2010), http://www.cdhowe.org/pdf/Commentary_317.pdf; Michael C. Wolfson, "Projecting the Adequacy of Canadians' Retirement Incomes: Current Prospects and Possible Reform Option," Institute for Research on Public Policy, no. 17 (April 2011), http://irpp.org/wp-content/uploads/2014/05/Wolfson-No17.pdf; Benjamin Tal and Avery Shenfeld, "Canadians' Retirement Future: Mind the Gap," CIBC World Markets Inc., In Focus, (February 20, 2013).

Longer Life Expectancy

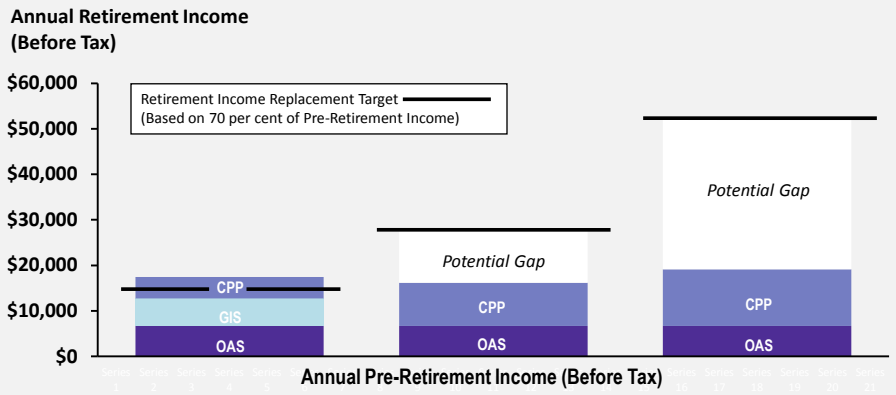
Average lifespans have been increasing in Canada for some time, and this trend is likely to continue.

- Ontario men currently aged 65 can expect to live, on average, another 19 years. By 2035, they will live, on average 23 more years.
- For women aged 65, life expectancy is currently 22 more years. This will rise to 25 years by 2035.
- The Office of the Chief Actuary of Canada has estimated that about half of people who are 20 years old today can expect to live to 90 years of age or older.

Increasing life expectancy is a sign of higher living standards and better health outcomes. However, this has put pressure on personal savings and workplace pension plans' capacity to ensure lifelong income over a retirement period that can last decades.

Retirement experts recommend that people aim to replace 50 to 70 per cent of their pre-retirement earnings to maintain a similar living standard in retirement. Without the benefit of a workplace pension plan, individual or group RRSPs, or other savings as a source of retirement income, more Ontarians will need to rely more heavily on Pillar 1 and Pillar 2 programs. These retirement benefit programs alone will not replace enough income for most Ontarians. Without additional retirement savings, a significant gap will develop between the income they will need and the income that will be available to them in retirement.

Retirement Income Targets and Potential Gaps (Single Person)



	At $20,000	At $40,000	At $75,000
Retirement Income Target	$14,000	$28,000	$52,500
Potential Gap	$0	$11,830	$33,363

Notes: CPP amounts assume the individual contributes for 40 years, begins collecting CPP at age 65 and had steady career before-tax earnings of $20,000, $40,000 and $75,000, expressed in 2014 dollars. OAS and GIS are based on 2014 benefit amounts and assume the individual has been a resident of Canada for 40 years after the age of 18, and begins collecting benefits at age 65. The target income levels are based on 70 per cent of pre-retirement income. Figures do not take into account the impact of income tax.
Source: Ontario Ministry of Finance.

The risks of inaction are significant. For Ontario workers this may mean a decline in their standard of living after retirement. For the broader economy, insufficient savings would lead to a decline in the future spending of retired individuals at a time when slower labour force growth will result in fewer workers and more retirees. For government, this would mean greater pressure on social programs with implications for taxpayers.

Ontario has advocated for an enhancement to the CPP since 2010, and this remains the province's preferred approach to strengthening the retirement income system. However, following the federal government's decision to end discussions on a CPP enhancement, the Ontario government determined that it could not wait to take action and is taking a leadership role in addressing this pressing issue by establishing the ORPP.

Key Features of the Ontario Retirement Pension Plan

The government is moving forward with the ORPP, a first-of-its-kind mandatory provincial pension plan that would expand pension coverage for more than three million working Ontarians.[4]

The ORPP would build on the strengths of the CPP and assist millions of working Ontarians in achieving a more secure retirement future.

Similar to the CPP, the ORPP would:	
✔	**Offer a predictable stream of income in retirement for life, and index benefits to inflation:** Predictable benefits would make it easier for people to plan for their retirement, while indexation would protect the benefit from eroding over time.
✔	**Pool longevity and investment risk:** These features would help to ensure that members do not outlive their savings, and lessen the impact of volatility on investment returns.
✔	**Require equal contributions to be shared between employers and employees, not exceeding 1.9 per cent each**: Employer contributions are required for all registered pension plans. This would help to boost individuals' retirement savings, which in turn, provides benefits to the broader Ontario economy.
✔	**Aim to replace 15 per cent of an individual's earnings:** Contributions would be required on earnings up to $90,000 (in 2014 dollars). Contributions would not be required below a minimum earnings threshold.
✔	**Require benefits to be earned as contributions are made:** This ensures that the system is fair, and that younger generations would not be burdened with additional costs associated with older workers' benefits.
✔	**Require "locked-in" contributions and accumulated benefits:** Individuals would not be able to withdraw retirement income to help them meet short-term financial pressures before reaching retirement age.

The ORPP is intended to assist those most at risk of undersaving. As a result, enrolment in the ORPP would be mandatory for eligible workers employed in Ontario, excluding those who work in federally regulated sectors, such as telecommunications and banking, those who participate in a comparable workplace pension plan and the self-employed. (See page 27 for a discussion on the self-employed.)

[4] The actual number of contributors will depend on detailed design elements, such as the definition of a comparable plan, the minimum earnings threshold and the administration of payroll contributions. This estimate uses data from 2011 and will change as a result of the growth in the pool of potential contributors by the time the ORPP is implemented starting in 2017.

Cost-effective administration and a plan that is simple for employers and plan members are key priorities. The ORPP will be administered by an arm's length entity with a strong governance structure and investment strategy to ensure efficient management, accountability, transparency and fairness. The entity will work hard to leverage the expertise and capacity of Ontario's highly regarded public sector pension plans and the province's strong financial services sector to help make ORPP administration and investment management effective and efficient. The assets of the ORPP will be managed for the benefit of workers and will not be included as part of overall government revenues.

Issue 1: Definition of Comparable Workplace Pension Plan

> "Since the ORPP is intended to assist individuals most at risk of undersaving, particularly middle-income earners without workplace pensions, those already participating in a comparable workplace pension plan would not be required to enrol in the ORPP."
>
> *2014 Ontario Budget*

The undersaving problem is complex and requires a range of tools, both mandatory and voluntary, and collaboration from all sectors. Canada's current retirement income system, through its three pillars, recognizes the need for a multi-faceted approach to this challenge. That is why Ontario is pursuing a three-pronged strategy to strengthen the retirement income system, and has recently introduced legislation providing a legal framework for the establishment and administration of PRPPs in Ontario.

The ORPP focuses on enhancing the mandatory aspect of retirement savings, by creating a savings vehicle for Ontarians employed in provincially regulated sectors without a comparable workplace pension that will complement voluntary savings and Pillar 1 and 2 benefits. Mandatory enrolment of eligible working Ontarians who do not otherwise participate in a "comparable" plan will help to provide these individuals with a secure savings floor in retirement.

Ontario's Preferred Approach: Define "Comparable" Plan as Defined Benefit and Target Benefit Multi-Employer Pension Plans

The government's preferred approach to the undersaving challenge remains a CPP enhancement. Therefore, the ORPP is being designed to mirror the key features that have made the CPP a successful pension program for working Canadians. The following section outlines how each of the key features of the CPP and the ORPP play an important role in ensuring a secure retirement future.

Income for Life Addresses the Risk of Outliving Savings

People saving for retirement face a number of key questions, such as**: How long am I likely to live? How long will my savings need to last?** To help individuals deal with these uncertainties, the ORPP would provide members with a predictable stream of retirement income that is paid for life, similar to the CPP. This is also similar to the type of benefit provided by DB and TB multi-employer pension plans (MEPPs).

By contrast, benefits provided by DC plans, PRPPs and Group RRSPs are limited to the value of accumulated contributions and investment returns. As a result, they are not necessarily provided for life; retirees must decide how quickly to draw down their savings and bear the risk of living longer than their savings can comfortably support them. This is often referred to as "longevity risk".

Individuals can lessen the risk of outliving their retirement income by purchasing life annuities from an insurance provider. Annuities provide a predetermined amount of annual income for the life of an individual and, if desired, their spouse. However, this option is not widely used.

Indexing to Inflation Protects Purchasing Power

Inflation is the sustained increase in the level of prices for goods and services. When planning and saving for retirement, individuals have to take into account the effect that inflation can have on the purchasing power of their retirement income over time. Similar to the CPP, ORPP benefits would be indexed to inflation, ensuring these benefits maintain their purchasing power through retirement.

Some, but not all, DB plans and TB MEPPs index benefits to inflation. How benefits are indexed vary by plan.

DC plans, PRPPs, Group RRSPs and DPSPs do not adjust benefits to inflation since the benefits are made up of contributions and investment returns accumulated up to the time of retirement. People with these retirement savings plans must ensure they save enough during their working years to pay for the ongoing cost of living increases in retirement.

Mandatory Employer Contributions Reflect a Shared Responsibility

Employer contributions to retirement savings arrangements reflect a shared responsibility for retirement security that recognizes the impact of retirement income levels on the broader economy and society. The ORPP would adopt this principle and, similar to the CPP, require equal contributions from both employer and employees.

RPPs require regular contributions by employers. Other retirement savings arrangements, such as Group RRSPs and PRPPs, do not require employer contributions, although some employers choose to make voluntary contributions. Only employers are able to make contributions to a DPSP, however, contributions are made at the discretion of the employer and are often linked to the company's financial performance.

Pooling Investment Risk Lessens the Impact of Lower-than-Expected Market Returns

Pooling resources allows individuals to share the "investment risk" of lower-than-expected market returns. While many plans such as DC plans, PRPPs and Group RRSPs allow members to tailor their investment strategy to reflect their risk tolerance, individual members of these plans typically bear the risk. Lower-than-expected returns or a sudden and unexpected market downturn may require plan members to continue working longer or accept a lower standard of living in retirement.

The ORPP would help to mitigate this risk by pooling the investment risk across all plan members. Pooling of investment risk — also offered by DB plans and TB MEPPs — is a significant advantage since it allows plan members to spread the effect of volatile returns across age groups and, in DB plans, with the employer. While many DC plans and PRPPs are able to pool investments in order to access the economies of scale enjoyed by large pension plans, they do not pool the investment risk. As a result, members are more vulnerable to the effect of a sudden and unexpected market downturn.

Locked-In Funds Ensure Savings are Available in Retirement

Short-term financial pressures, such as buying a house or car, can compromise long-term retirement goals, as families are tempted to dip into their retirement savings accounts to address their short-term needs.

Recognizing this, the benefits of the CPP, workplace pension plans and PRPPs are "locked-in" meaning that plan members cannot withdraw retirement income before reaching retirement age. ORPP benefits would similarly be locked-in, ensuring short-term financial pressures are not prioritized over retirement income security.

How Retirement Savings Options Compare

Many Ontarians have access to a range of tax-assisted voluntary retirement savings arrangements through their employers. By providing a secure retirement income floor, the ORPP is intended to complement these workplace-based savings vehicles while ensuring they continue to play an important role in maintaining standards of living in retirement.

A fully implemented ORPP would be cost-effective and portable across participating employers, features that are generally not available in existing retirement savings vehicles. However, a comparison of available retirement savings vehicles against the ORPP's key features shows that DB plans and TB MEPPs closely align with the criteria described above.

DB Plans and TB Multi-Employer Plans are Most Comparable to the CPP and ORPP							
Key Features of the ORPP	**Canada Pension Plan (CPP)**	**Defined Benefit Pension Plan (DB plan)**	**Target Benefit Multi-Employer Pension Plan (TB MEPP)**	**Defined Contribution Pension Plan (DC plan)**	**Pooled Registered Pension Plan (PRPP)**	**Group Registered Retirement Savings Plan (RRSP)**	**Deferred Profit Sharing Plans (DPSP)**
1. Benefit provided for life (longevity pooling)	✔	✔	✔	✖	✖	✖	✖
2. Indexed to inflation	✔	Varies by Plan	Varies by Plan	✖	✖	✖	✖
3. Mandatory employer contributions	✔	✔	✔	✔	✖	✖	✖
4. Pooled investment risk	✔	✔	✔	✖	✖	✖	✖
5. Locked-in funds	✔	✔	✔	✔	✔	✖	✖

Implications of the Preferred Approach

Greater Opportunity to Support a Modern, Mobile Workforce

Restricting the definition of "comparable" plan to only DB plans and TB MEPPs would have many advantages for ORPP members. In particular, a narrower definition would:

- Expand the number of employers offering the ORPP to employees, giving Ontarians greater opportunity to participate in the plan.
- Allow the ORPP to be available in a broader range of workplaces, resulting in a more portable plan to which plan members would contribute and accumulate the corresponding benefits as they move between participating employers throughout their working lives. This is particularly important for younger workers, who are likely to change employers frequently throughout their careers. It is also important for workers holding part-time or temporary jobs who are frequently unable to access a workplace pension plan.[5]

[5] Katherine Marshall (2003) "Benefits of the Job" *Perspectives on Labour and Income, Statistics Canada*.

- Create a more stable ORPP membership, which would likely result in lower compliance costs and administrative complexity, as there would be fewer members entering and leaving the plan in any given year.
- Enable the plan to spread investment and longevity risks across a greater number of individuals, contributing to a more stable and sustainable plan over the long term.

While the ORPP is an Ontario solution, expanding the ORPP to other provinces would further extend portability of the plan across provincial borders, allowing employees to move between participating employers across Canada while still accruing ORPP benefits. The government will continue to work with the provinces to examine whether the ORPP could be expanded outside Ontario, and to continue to explore integration with a potential for future CPP enhancement.

Impact on the Broader Retirement Savings Landscape

The government is mindful that the definition of "comparable" plan may have an impact on the current retirement savings landscape. Contributions to retirement savings are often part of an employer's approach to total compensation. With the introduction of the ORPP, some employers may take stock of their current approaches, and make decisions about the right compensation mix going forward and plan for transition. In some cases, this may require negotiation through the collective bargaining process with employee organizations.

The government recognizes the need to understand fully the potential impact of the definition on the broader retirement savings landscape. While this paper has outlined a preferred approach, the government is committed to consulting with businesses, labour, organizations, associations, as well as individuals, families and communities across the province to understand and consider their views.

DISCUSSION QUESTIONS

1. The government's preferred approach remains a CPP enhancement. Therefore, the definition of "comparable" should be determined with a view to maintaining the potential for integration with the CPP in the future. With this in mind, should the definition of a "comparable" workplace pension plan mirror the key features of the CPP and ORPP?

2. Which features of the CPP and the ORPP would be the most important to capture in a "comparable" plan?

    a. For example, how important is protection against longevity risk in a mandatory retirement savings vehicle?

    b. Similarly, how important is protection against investment risk in a mandatory retirement savings vehicle?

3. Are there circumstances under which other retirement savings vehicles such as DC plans should be considered comparable?

    a. For example, would establishing a minimum employee/employer contribution rate (that would provide for a similar benefit to the ORPP) for DC plans help make DC plans comparable?

    b. Similarly, would requiring members to convert a portion of savings in a DC plan to an annuity upon retirement help make DC plans comparable? If so, would Ontario's insurance industry have the capacity to offer affordable annuities on this scale?

4. Employers may have multiple and complex retirement savings arrangements.

    a. How would employers currently offering non-comparable plans expect their plans to work alongside the ORPP?

    b. How much time would employers need to take stock of their current approaches and make decisions about the right compensation mix going forward?

5. In your view, what would be the best definition of "comparable" workplace pension plans?

Issue 2: The Right Minimum Earnings Threshold

> "To reduce the burden on lower-income workers, earnings below a certain threshold would be exempt from contributions, similar to the Canada Pension Plan (CPP). The government will consult on whether the ORPP's lower-income threshold would mirror that of the CPP at $3,500."
>
> *2014 Ontario Budget*

For working-age adults, employment is the key to reducing poverty. However, having a job does not guarantee that individuals or families will have sufficient income to escape poverty. About six per cent of Ontario's workforce has income that is below the Low Income Measure (LIM). Many workers face a precarious labour market and must work part-time in temporary jobs or take on multiple jobs in order to make ends meet. Many of these workers do not have access to a workplace pension plan or other employment benefits. This is a particular problem for recent immigrants, persons with disabilities and youth who face barriers to securing well-paid jobs.

As part of Ontario's Poverty Reduction Strategy (PRS), the government has undertaken a number of actions:

- Increasing the minimum wage to $11 per hour and indexing it to the Ontario Consumer Price Index to ensure that it keeps up with the costing of living.
- Increasing the Ontario Child Benefit (OCB) to a maximum of $1,310 per child per year, which will be indexed to the Ontario Consumer Price Index starting in July 2015. The OCB enhances the incomes of over 500,000 low- to moderate-income families and helps families participate in employment by reducing the financial barriers to leaving social assistance.
- Providing dental benefits for children in low-income families and committing to expanding this coverage by providing prescription drugs and other health benefits for children in low-income families. Moving forward, the government will consult with stakeholders to explore options to extend health benefits to all low-income Ontarians.
- Providing full-day kindergarten so parents living in poverty will have more time in the day to pursue education, training or employment while reducing their child care costs.
- Investing $295 million over two years in Ontario's Youth Jobs Strategy to help young Ontarians find jobs and gain valuable skills. This initiative has helped to create more than 20,000 youth job opportunities.
- Calling on the federal government to partner with Ontario to help reduce poverty.

Building on these initiatives, there is an opportunity to help ensure that today's low-income workers and seniors are well supported in their retirement.

Ontario's Preferred Approach: Mirror the CPP's $3,500 Minimum Threshold

The CPP's minimum annual earnings threshold exempts workers in limited employment or with minimal attachment to the labour force from participating in the plan. Referred to as the Year's Basic Exemption (YBE), this threshold is set at $3,500.

- Workers with annual earnings below this threshold (and their employers) do not contribute to the CPP and do not accumulate or receive CPP benefits in respect of these earnings.
- Workers with annual earnings above this threshold (and their employers) do not contribute on their first $3,500 of earnings, but still accumulate CPP benefits on their earnings below $3,500. These benefits are funded by slightly higher contribution rates paid by all CPP contributors on earnings above $3,500.

The government's preferred approach to a minimum earnings threshold for the ORPP is to mirror the CPP's YBE of $3,500 in the ORPP. This approach would:

- Maximize participation and benefits for workers over the long term, including those in non-standard employment or who experience temporary periods of low earnings, such as many youth and recent immigrants.
- Reduce administrative complexity for employers.

The government recognizes that this approach may have implications for workers with persistently low incomes, leading some experts and stakeholders calling for a minimum earnings threshold for the ORPP that is higher than $3,500. However, as will be discussed in this section, a higher minimum earnings threshold would reduce workers' ability to participate in, and benefit from, the ORPP.

With this in mind, this section includes analysis of earnings patterns. It also presents strategies outside of the ORPP design that could better address the needs of current low-income workers and future low-income seniors.

Who is at Risk of Oversaving?

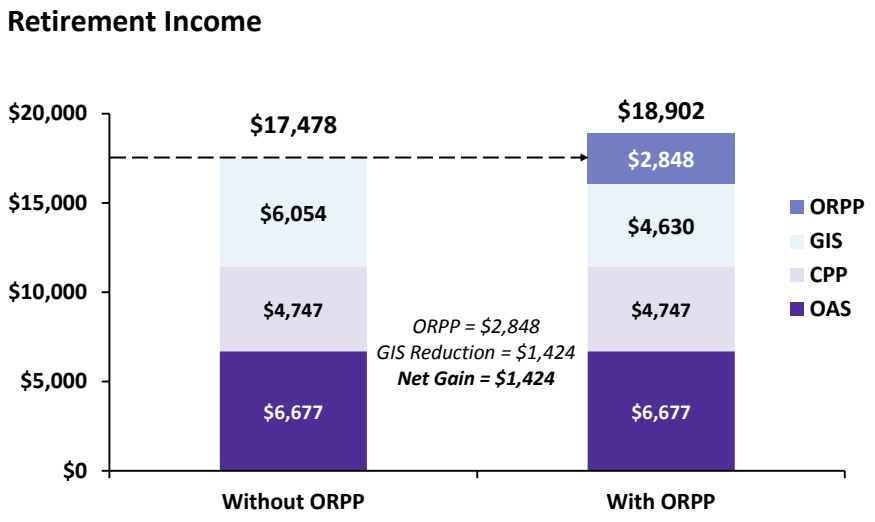
Further retirement savings may not be necessary for individuals with persistently low incomes throughout their working years.

- When combined with the CPP, Pillar 1 benefits for low-income seniors can provide a high level of income replacement for those with a history of low income due to persistently low employment earnings, lengthy periods of unemployment or reliance on income supports such as social assistance. As such, further retirement savings may not be needed for these individuals.

- Given the current design of Pillar 1 supports, individuals receiving GIS and GAINS who have contributed to the ORPP in their working years would likely be subject to a clawback of these benefits when they retire. Since GIS and GAINS are income tested, the benefits are reduced for every dollar of additional income the senior receives from other sources, including employer pensions, CPP benefits and, in the future, likely the ORPP.[6]

Example: Potential Change in Retirement Income due to ORPP Benefits[7]

- The chart below shows the potential impact of the ORPP on the retirement income of a single senior who earned $20,000 per year before retirement.
- Without the ORPP, this senior would receive about $17,000 per year from OAS, GIS and CPP, replacing about 85 per cent of their pre-retirement income.
- If the senior had contributed to the ORPP, they would be entitled to an ORPP benefit of $2,848 per year, reducing their GIS benefit by 50 per cent of the ORPP benefit.
- This senior's income would be increased by $1,424 per year by contributing to the ORPP and would have an income replacement rate of 95 per cent.



Sources: Service Canada and Ontario Ministry of Finance.

[6] Although the federal government has not indicated how it would treat ORPP benefits for the purposes of determining GIS eligibility, it is likely that ORPP income would be treated the same as income from the CPP and workplace pensions.

[7] This example assumes the senior contributed for 40 years to the CPP and ORPP with annual steady career earnings of $20,000 (before tax). The example also assumes a single senior that has no other sources of income beyond OAS, GIS, CPP and ORPP. ORPP benefits are based on Budget 2014 parameters. All figures are expressed in 2014 dollars.

Low Earners Are Not Necessarily At Risk of Oversaving

The chart on page 18 illustrates the risk of oversaving for persistently low-earning individuals contributing to the ORPP during their working life. However, in considering where to set a minimum earnings threshold in designing the ORPP, it is important to take into account that, while earnings and household income are related, *the majority of workers with low earnings in a particular year will not experience persistently low earnings over their entire career and do not belong to a low-income household*.

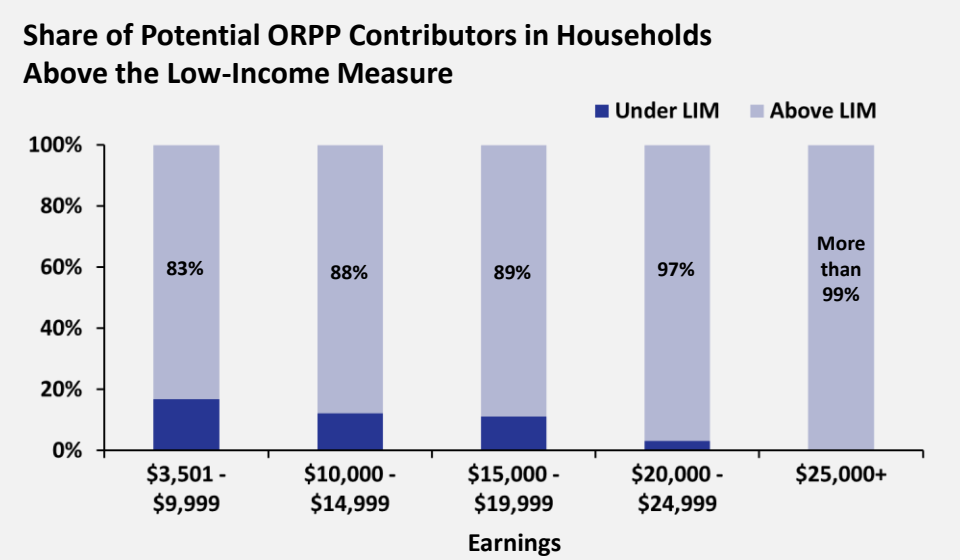
Low Earnings vs. Low Income

- "Low earnings" are based on an individual's earnings from employment in a given year from a specific employer that falls below a threshold, such as $15,000.
- "Low income" refers to individuals whose total household income from all sources falls below a measure of low income, such as the Low-Income Measure (LIM) or Low-Income Cut-Off. This paper uses the LIM and after-tax and transfer income to identify low-income households.

About one-third of workers who would potentially contribute to the ORPP have annual earnings under $15,000. However, of these workers, about 85 per cent were members of a household with income above the LIM.[8] The remaining 15 per cent had low income.

[8] Ontario Ministry of Finance and Statistics Canada. Potential ORPP contributors are workers aged 18-64 in 2011 excluding those who were participating in a workplace pension plan, were self-employed or had annual earnings below $3,500. The actual number and characteristics of contributors will depend on detailed design elements, such as the definition of a comparable plan, the minimum earnings threshold and the administration of payroll contributions. These estimates use data from 2011 and will change as a result of growth in the pool of potential contributors by the time of ORPP implementation, starting in 2017. The income of potential contributors is calculated based on household income after taxes and transfers.

The chart below shows that the majority of potential ORPP contributors in every earnings range have total household income above the LIM.



Notes: Potential ORPP contributors are workers aged 18-64 in 2011 excluding those who were participating in a workplace pension plan, were self-employed or had annual earnings below $3,500. The actual number and characteristics of contributors will depend on detailed design elements, such as the definition of a comparable plan, the minimum earnings threshold, and the administration of payroll contributions. These estimates use data from 2011 and will change as a result of growth in the pool of potential contributors by the time of ORPP implementation, starting in 2017. The income of potential contributors is calculated based on total household income after taxes and transfers.
Sources: Statistics Canada and Ontario Ministry of Finance.

There are a variety of reasons why low earners may not be living in low-income households. For example, a part-time worker may have a higher-earning spouse or a younger earner may live with higher-income parents. Also, federal and provincial children's benefits may lift a low-earning family with children above the LIM threshold.

In addition, low earnings in a particular year do not necessarily mean an individual will experience low income in retirement and receive GIS. Researchers have investigated the incidence of GIS receipt by the retired population and found that periods of low earnings during working years do not necessarily indicate whether a worker will receive a GIS benefit in retirement.[9]

[9] Uppal et al. (2009) "Pathways into the GIS"; Finnie, Gray & Zhang (2013) Perspectives, Statistics Canada. "Guaranteed Income Supplement (GIS) Status Amongst the Retired Population: An Analysis of the Incidence," *Canadian Public Policy, Volume 39.*

The Ontario Ministry of Finance analyzed seniors aged 66 or 67 in 2011 and found that:

- about two-thirds of those who had earned less than $15,000 during their early 50s (considered an individual's "prime-earnings age") did not go on to receive GIS benefits (see table below); and
- about one-fifth of those with earnings between $15,000 and $60,000 during their prime-earnings age did go on to receive GIS, suggesting that having relatively higher earnings also does not necessarily mean a person will not receive GIS in retirement.

Relationship Between Earnings and Future Receipt of GIS

Average Earnings During Prime-Earnings Age (Aged 51 – 56)	Share Receiving GIS at Age 66/67	Share Not Receiving GIS at Age 66/67
Less than $15,000	32%	68%
Between $15,000 – $60,000	22%	78%
More than $60,000	7%	93%

Notes: Includes individuals aged 66 or 67 in 2011 for whom information on earnings from 1996 to 2000 is available, who were not participating in a workplace pension plan and had annual earnings above $3,500.
Source: Ontario Ministry of Finance

Low earnings in a particular year do not necessarily correlate to persistently low incomes. Therefore, adopting a higher minimum earnings threshold may not necessarily assist all those at risk of oversaving and facing a clawback of GIS in retirement.

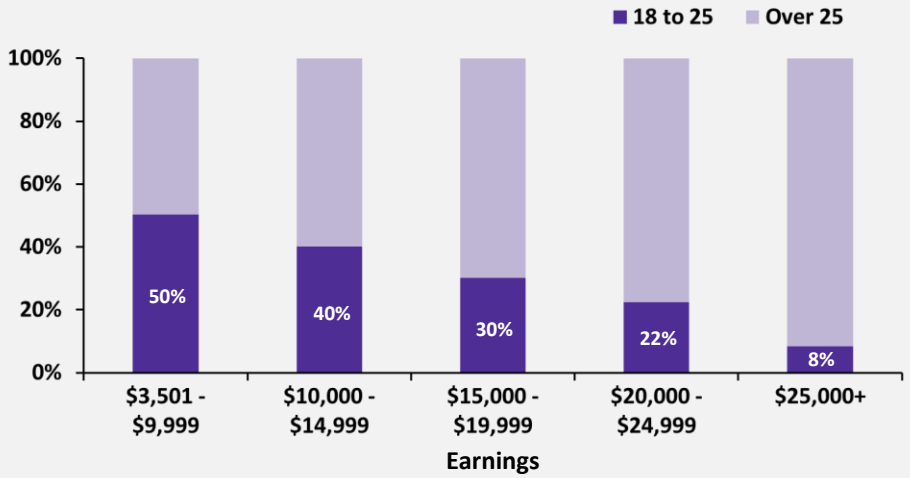
A $3,500 Threshold: Maximizing Participation and Benefits for Workers

The ORPP design should take into account the dynamics of today's labour market and maximize participation and benefits for workers over the long term. While a higher minimum earnings threshold, such as $15,000, would reduce contributions for many persistently low-income workers, it would also reduce the ability of many more workers to benefit from the ORPP.

Making Benefits More Accessible for Those with Temporary Periods of Low Earnings

For most workers, periods of low earnings are temporary.[10] Over the longer term, most people who experience a period of low earnings will have higher average earnings when their entire career is taken into account. This is particularly the case for youth, who typically experience a period of low earnings but go on to have higher earnings later in their working life.[11] As shown in the chart below, significant shares of workers with lower earnings who are potentially eligible for the ORPP are under age 25.

Share of Youth Among Potential ORPP Contributors by Earnings



Notes: Potential ORPP contributors are workers aged 18-64 in 2011 excluding those who were participating in a workplace pension plan, were self-employed, worked in a federally regulated industry or had annual earnings below $3,500. The actual number and characteristics of contributors will depend on detailed design elements, such as the definition of a comparable plan, the minimum earnings threshold, and the administration of payroll contributions. These estimates use data from 2011 and will change as a result of growth in the pool of potential contributors by the time of ORPP implementation, starting in 2017.
Source: Ontario Ministry of Finance.

[10] Beach and Finnie (2004) "A Longitudinal Analysis of Earnings Change in Canada"; *Analytical Studies Branch research paper series*, Statistics Canada; Ren and Xu (2011) "Low-Income Dynamics and Determinants under Different Thresholds: New Findings for Canada in 2000 and Beyond," *Income Research Paper Series, Statistics Canada.*

[11] Beach and Finnie (2004).

Older workers also experience temporary periods of low earnings. The Ontario Ministry of Finance examined earnings patterns over the period of 2002 to 2011 of workers between the ages of 41 and 50 in 2011.[12] Over the 10-year period, about:

- 53 per cent experienced at least one year of earnings below $15,000;
- 33 per cent experienced at least three years of earnings below $15,000; and
- five per cent had earnings consistently below $15,000 every year over the entire 10-year period.

If a higher minimum earnings threshold, such as $15,000, were established, individuals experiencing temporary periods of earnings below the threshold would not be required to contribute and would not accumulate ORPP benefits for that period. This would reduce benefits over the longer term for these individuals. Young people and other groups such as recent immigrants, entering the labour market may be particularly disadvantaged over the long term by a higher threshold.

Making Benefits More Accessible for Those in Non-Standard Employment

Potential ORPP contributors would include workers employed in a wide range of sectors and with different work arrangements and earnings levels. The ability to support Ontario's diverse workforce is one of the greatest strengths of the ORPP.

Workers in non-standard or precarious[13] employment are less likely to have access to a workplace pension plan, and represent a significant portion of potential ORPP contributors.

Preliminary estimates of the more than three million potential ORPP contributors[14] indicate that, in a given year:

- one-quarter will hold multiple jobs;
- one-quarter will experience at least one job interruption; and
- one-quarter will be employed part-time.

[12] Estimates include potential ORPP contributors and therefore exclude workers who were participating in a workplace pension plan, were self-employed, worked in a federally regulated industry or had earnings below $3,500. The results shown in this example are based on the latest 2002-2011 tax administration data. The $15,000 threshold has been adjusted for inflation over the 10-year period.

[13] Non-standard employment includes part-time and temporary work (contract or seasonal), self-employment as well as holding multiple jobs. Precarious employment is a subset of non-standard work in which workers are particularly insecure due to (among other things) low income or lack of access to workplace health benefits or pension plan. See Vosko, Leah (2010) *Managing the Margins: Gender, Citizenship and the International Regulation of Precarious Employment*. Oxford, UK: Oxford University Press.

[14] Potential ORPP contributors are workers aged 18-64 in 2011, excluding those who were participating in a workplace pension plan, were self-employed or had earnings below $3,500. The actual number and characteristics of contributors will depend on detailed design elements, such as the definition of a comparable plan, the minimum earnings threshold and the administration of payroll contributions. These estimates use data from 2011 and will change as a result of growth in the pool of potential contributors by the time of ORPP implementation, starting in 2017.

Individuals holding multiple jobs at the same time over the course of a year would be subject to the earnings exemption separately for each full or part-time job. Adopting a higher earnings threshold, such as $15,000, would mean that a large portion of their total earnings would be exempt from contributions. As a result, they would not be able to accumulate benefits on their earnings below the threshold, reducing their ORPP benefits over the longer term.

A higher minimum earnings threshold, such as $15,000, would also exclude many part-time workers whose total earnings are below the threshold.

By contrast, a threshold of $3,500 helps ensure that workers in non-standard jobs are able to accumulate benefits on more of their earnings over the course of their working lives.

Allowing All Workers to Contribute on a Wider Range of Earnings

Under a higher minimum earnings threshold, such as $15,000, all contributors — including those with earnings above the threshold — would experience lower benefits and replacement rates since the range of pensionable earnings would be reduced, compared to the preferred approach (see illustrative examples the table on page 23).[15] This is a general effect of a minimum earnings threshold and would impact all contributors in both standard and non-standard employment.

[15] The CPP uses a slightly higher contribution rate to fund benefits on earnings below $3,500. The illustrative examples of the preferred approach mirror the CPP. However, the illustrative example of a $15,000 minimum earnings threshold does not allow contributors to accumulate benefits on earnings below $15,000. To provide benefits on earnings below $15,000 would be very costly, requiring a much higher contribution rate and create significant cross-subsidies between contributors.

Mirroring the CPP's relatively low threshold of $3,500 allows all plan members to contribute more and receive a larger benefit as a result.

Illustrative Examples of Different Minimum Earnings Thresholds			
Total Earnings in a given year		**Preferred Approach ($3,500)**	**Illustrative Example of A Higher Threshold ($15,000)**
$10,000	**1 job**	• Contributes on **$6,500** ($10,000 minus $3,500) • Accrues benefits on **$10,000**	• Does not contribute or accrue benefits because earnings are below threshold
	2 jobs, each paying $5,000	• Contributes on $1,500 in each job ($5,000 minus $3,500) for **$3,000** in total • Accrues benefits on **$6,500**	• Does not contribute or accrue benefits because each job has earnings below threshold
$20,000	**1 job**	• Contributes on **$16,500** ($20,000 minus $3,500) • Accrues benefits on **$20,000**	• Contributes on **$5,000** ($20,000 minus $15,000) • Accrues benefits on **$5,000** of earnings
	2 jobs, each paying $10,000	• Contributes on **$6,500** in each job ($10,000 minus $3,500) for **$13,000** in total • Accrues benefits on **$16,500**	• Does not contribute or accrue benefits because each job has earnings below threshold
$40,000	from **1 job**	• Contributes on **$36,500** ($40,000 minus $3,500) • Accrues benefits on **$40,000**	• Contributes on **$25,000** ($40,000 minus $15,000) • Accrues benefits on **$25,000**
	2 jobs, each paying $20,000	• Contributes on $16,500 in each job ($20,000 minus $3,500) for **$33,000** in total • Accrues benefits on **$36,500**	• Contributes on $5,000 in each job ($20,000 minus $15,000) for **$10,000** in total • Accrues benefits on **$10,000**

Notes: The CPP contribution rate allows all contributors to accumulate benefits on $3,500 per year without paying contributions on this exempted amount. A person with concurrent jobs will be exempted from contributions on $3,500 by each employer. However, they are only entitled to accumulate benefits on $3,500 once per year and miss out on $3,500 of pensionable earnings they could have contributed on if they worked one job. They may be able to accumulate benefits on the missed $3,500 of earnings if they elect to contribute to both the employee and employer shares when they file their tax return.
Source: Ontario Ministry of Finance.

A $3,500 Threshold: Reducing Administrative Complexity

Mirroring the CPP's $3,500 earnings threshold would reduce administrative complexity, as it would be relatively simple for employers to implement and for contributors to understand. Employers already have systems in place to determine and deduct appropriate CPP payroll contributions. An ORPP payroll deduction approach that is consistent with that of CPP would make it easier for employers to integrate ORPP contribution deduction with their existing business practices.

An ORPP minimum earnings threshold that parallels the CPP could also make potential integration of the ORPP with the CPP easier if the CPP is enhanced in the future.

Strategies to Assist Those at Risk of Oversaving and Future Low-Income Seniors

There are a number of good reasons why mirroring the CPP minimum earnings threshold of $3,500 makes sense. However, it remains important to understand and manage impacts on workers with persistently low incomes.

There are a number of limitations to using a minimum earnings threshold as a way to assist these workers. There may, however, be other strategies outside of the design of the ORPP that the government can consider to better address the oversaving risk.

Assisting Low-Income Individuals and Families during their Working Years

Ontario has taken steps to improve income security for working individuals and families through the Poverty Reduction Strategy. However, further supports are needed.

One area in which action should be taken is with the federal Working Income Tax Benefit (WITB).

The WITB is a refundable tax credit intended to supplement the incomes of working individuals and families. However, the 2014 maximum benefit for working individuals is only $998, and individuals stop receiving the WITB once their income exceeds $17,985. For families, the maximum benefit is $1,813, and families no longer receive WITB benefits once their income exceeds $27,736. Given its modest maximum benefit and the low level of income at which it phases out, enhancements to WITB are needed.

An enhancement to the WITB would provide additional support to low-income workers so they can better manage their living expenses, while also allowing them to save for their future retirement through the ORPP.

The Poverty Reduction Strategy calls for enhancements to the WITB. Ontario is not alone in calling on the federal government to take action; others include the House of Commons' Standing Committee on Finance.

Recommendation to Enhance the Working Income Tax Benefit

"…that the federal government formally review the Working Income Tax Benefit to determine how it could be expanded or modified to further benefit Canadians and further incent workforce attachment, subject to the government's stated intention to balance the budget in the medium term."

Income Inequality in Canada: An Overview, Report of the Standing Committee on Finance, December 2013.

Enhancing Future Low-Income Seniors' Retirement Income Security

There is a critical need to consider reforms to the Pillar 1 system of supports (OAS, GIS and GAINS).

The risk of a clawback of existing federal GIS benefits for those low-income seniors that will have contributed to the ORPP has been outlined earlier in this paper. Low-income individuals should be better rewarded for increasing their level of retirement savings.

In addition, for some low-income seniors, in particular single seniors, Pillar 1 benefits are not sufficient to ensure they are living above the LIM.

Ontario could advocate for reforms to low-income seniors' benefits to enhance their security in retirement. These reforms could include:

- Revising the federal GIS reduction rate to better support low-income seniors with modest alternative income sources, including the ORPP and the CPP.
- Improving the level of supports provided, for example, by federal GIS and CPP survivor benefits to low-income unattached seniors, who are disproportionately women.

DISCUSSION QUESTIONS

1. Does mirroring the CPP minimum earnings threshold strike the appropriate balance between contributing and accruing benefits?

2. If not, what should be the minimum earnings threshold for the ORPP? What are the potential tradeoffs?

3. There will be administrative complexities if the minimum earnings threshold is different than that of the CPP. How might this affect different employers?

4. Are there other potential implications of a $3,500 minimum earnings threshold that are not addressed in this paper?

5. Are there other ways that Ontario could help address concerns about the ability of persistently low-income workers to contribute and accumulate benefits?

6. Should Pillar 1 supports, including the GIS and GAINS, be changed so that future low-income seniors do not experience reduced benefits as a result of higher ORPP benefits?

Issue 3: Addressing the Needs of the Self-Employed

> "The government recognizes the unique status of self-employed individuals in the labour market as both employee and employer. The government will consult to determine how best to assist self-employed individuals in achieving a secure retirement future."
>
> *2014 Ontario Budget*

Self-employed individuals will not be able to participate in the ORPP, given the current rules under the federal *Income Tax Act* (ITA).

The ORPP is being designed as a MEPP, and Ontario will work with the federal government to ensure that this plan can be registered under the ITA. However, currently, individuals who are not in an employment relationship and do not receive a salary or wages as compensation are currently precluded under the ITA from participating in RPPs.

Who Are the Self-Employed?

The term "self-employed" is broad and has the potential to capture a wide class of individuals who operate their businesses in different ways and use different structures. For example, an individual may choose to operate his or her business through various means, but the most common are: as a sole proprietor, through a partnership, or through a corporation.

With respect to self-employed individuals not eligible to participate in the ORPP, the term self-employed would refer only to those individuals who either:

- own and operate unincorporated businesses (i.e., sole proprietors, partnerships and some independent contractors); or
- own and operate incorporated businesses but are not employees and do not receive a salary or wages as compensation (e.g., an individual who receives distributions from the corporation that are not considered salary or wages, such as dividends).

By contrast, an individual who owns and operates an incorporated business and earns a salary or wages as an employee of the business would not be considered self-employed for the purposes of ORPP eligibility. As a result, these incorporated owner-operators *would* be required to participate in the ORPP, to the extent that they are considered eligible employees.

On average, incorporated owner-operators receive two-thirds of their annual income from wages and salaries.[16] In the event that these individuals receive other types of income (e.g., dividends), they would not make contributions to the ORPP on this other income.

Unique Status of the Self-Employed

The self-employed occupy a unique position in the labour market with financial circumstances and needs that are often more complex than those in traditional employer-employee relationships. For example, self-employed individuals are often required to strike a balance between business expenditures and personal income, with one outlay often coming at the expense of the other. The self-employed may feel that investing in their business, rather than contributing to a mandatory savings plan, would be a more effective retirement savings strategy. This is complicated by the fact that the annual earnings of self-employed individuals can fluctuate considerably.

Notwithstanding their unique status, evidence suggests that self-employed individuals may also be undersaving for retirement. In fact, research indicates that self-employed individuals are less likely to be financially prepared for retirement when compared with paid employees. According to Statistics Canada, in 2011, approximately 74 per cent of the self-employed stated that they were taking steps to prepare financially for retirement, compared with 85 per cent of paid employees.[17]

Although the self-employed under current ITA rules would not be able to enrol in and make contributions to the ORPP, there may be interest among self-employed individuals in participating in the ORPP, as they do in the CPP. Ontario could engage in discussions with the Government of Canada to amend the relevant ITA rules to allow individuals who are not in an employment relationship and who do not report income from salary and wages to participate in the ORPP, as is the case with the CPP.

Regardless of the retirement savings strategy pursued by self-employed individuals — whether through savings vehicles such as RRSPs, PRPPs, non-registered savings or investment in their businesses — an understanding of their own retirement income security goals and the financial tools available to achieve those goals are critical to planning. This includes the ability to articulate lifestyle goals, knowledge of public and private sources of retirement income and an ability to assess appropriate financial products in light of the individual's risk tolerance, financial market conditions and demographic factors, such as life expectancy.

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[16] Statistics Canada, "The financial well-being of the self-employed," September, 2011.

[17] Statistics Canada, "The financial well-being of the self-employed," September, 2011. Data are drawn from three surveys: the 2009 Survey of Labour and Income Dynamics (SLID), the 2008 Survey of Household Spending (SHS), and the 2009 Canadian Financial Capability Survey (CFCS). Although these surveys differ in scope and content, in each the self-employed are defined as those who reported that they were self-employed in their main job or said that self-employment constituted their main source of income during the survey reference period.

Financial literacy initiatives tailored to meet the needs of self-employed individuals may be particularly helpful in ensuring they have the knowledge to save sufficiently for retirement.

Strengthening the retirement income system for all Ontarians is a vital part of the government's plan to invest in people and to help working families build a more secure retirement future. Recognizing that self-employed individuals have unique financial circumstances and needs compared to those in traditional employee-employer relationships, the government is interested in receiving feedback on how best to assist the self-employed in achieving a secure retirement future.

DISCUSSION QUESTIONS:

1. Self-employed individuals will not be able to participate in the ORPP, given the current rules under the federal *Income Tax Act* (ITA). Should Ontario engage in discussions with the Government of Canada to amend the ITA rules in order to allow the self-employed participate in the ORPP?

2. What more can be done with regards to improving financial literacy among the self-employed? What role can the financial services sector play in educating the self-employed?

3. How else could the government assist self-employed individuals in achieving a secure retirement future?

Appendix: Canada's Current Retirement Income System

Pillar 1

Pillar 1 includes benefits for seniors intended to provide a base income floor; namely the federal OAS and GIS. In Ontario, these are supplemented for low-income seniors by the province's GAINS program. These benefits are publicly funded through general government revenues, rather than through payroll contributions and are based on residency and income eligibility criteria.

- The OAS pension is a monthly payment currently available to most Canadians aged 65 or older, regardless of whether they are currently working or have ever worked. About two million Ontario seniors, or 94 per cent, receive OAS. The maximum annual OAS payment is indexed to CPI and is about $6,765 per year (annualized as of December 2014). The average annual OAS benefit in Ontario was about $6,340 (annualized as of October 2014).
- Seniors can have a net income of up to $71,592 before their OAS is reduced by 15 per cent for each additional dollar of private income.

The GIS is an income-tested program that provides additional money, on top of the OAS benefit, to seniors who live in low-income households and reside in Canada. About 510,000 Ontario seniors, or 25 per cent of OAS pensioners, also receive GIS.

- The GIS is indexed to CPI and the maximum annual payment in 2014 is about $9,175 for single seniors and about $12,165 per year for senior couples (based on December rates).
- A single senior no longer qualifies for GIS if their household's income from other private sources[18] exceeds $17,088. For seniors with partners, this amount is $22,560. Benefits are reduced at 50 per cent for each dollar of houshold private income.[19]

The Ontario GAINS benefit is provided as a top-up to the federal OAS and GIS benefits. The sum of OAS, GIS and GAINS benefits provides a minimum income level for eligible low-income seniors in Ontario, referred to as the GAINS guarantee. Currently, there are about 140,000 GAINS' recipients, accounting for about seven per cent of Ontario seniors.

- The current annual GAINS guarantee is about $16,935 for single seniors and about $27,685 for senior couples where both are OAS pensioners (based on the monthly rates in effect from October to December 2014).
- The maximum GAINS benefit per eligible senior is $996 per year.
- Benefits are reduced by 50 per cent for each dollar of household private income.[20]

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[18] Other sources of private income include pensions, RRSP withdrawals, CPP and likely the ORPP. Other sources of "private income" do not include OAS, GIS and GAINS, and up to $3,500 of earned income per recipient in a household. A household for the purposes of GIS and GAINS is composed of a recipient and, if applicable, their spouse or common-law partner.

[19] GIS also includes a "Top-up" supplement for very low-income seniors. The GIS top-up is reduced by 25 per cent of private income over $2,000 for single seniors and $4,000 for couples.

Pillar 2

Pillar 2 includes the CPP, which is a mandatory pension program for the employed and self-employed. The CPP is funded by employer/employee contributions as well as investment earnings generated by the Canada Pension Plan Investment Board. The CPP contribution rate is 9.9 per cent of the year's maximum pensionable earnings (YMPE), shared equally between employers and employees.

The CPP is intended to replace 25 per cent of pensionable earnings for an individual who contributes to the CPP over their working career. Pensionable earnings are capped at the YMPE, which is adjusted annually. The YMPE threshold in 2014 is $52,500. The current maximum CPP retirement benefit is about $12,500 per year, while the average benefit paid in Ontario is about $6,800.

> The CPP's YBE was originally established in 1966 at 12 per cent of the maximum earnings threshold (referred to as the Year's Maximum Pensionable Earnings (YMPE)), or $600. In 1976, the YBE was reduced to 10 per cent of the YMPE.

During reforms to the CPP in 1997, the YBE was frozen at $3,500 in order to reduce costs and improve the sustainability of the plan. Because it is so low, the CPP's YBE only exempts workers in marginal employment or with minimal attachment to the labour force from participating in the plan.

Pillar 3

Pillar 3 includes a range of tax-assisted voluntary retirement savings arrangements, as follows:

Registered Pension Plans (RPPs)

All RPPs (also known as workplace pension plans) in Ontario are subject to legislative minimum standards set out in Ontario's *Pension Benefits Act* and the federal *Income Tax Act* (ITA). These include rules that require employers make contributions to the plan. The benefit provided by an RPP varies significantly depending on the type of pension plan. RPPs are not available to the self-employed since there is no employer-employee relationship, which is required under the ITA. RPPs can include the following types of pension plans:

- **Defined Benefit Pension Plan (DB plan).** A DB plan guarantees a monthly lifetime pension benefit at retirement. The benefit is determined by a formula that is usually based on the employee's years of service and/or earnings (e.g., a percentage of average annual salary multiplied by years of service.)

  Contributions on behalf of all employees are made to one fund, and investment and longevity risk are pooled.

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[20] The benefit reduction does not include OAS income, GIS income and the first $3,500 of earned income.

This means that members do not bear the risk of decreased savings due to poor investment returns or of outliving their savings. In Ontario, DB plans are subject to the *Pension Benefits Act* (PBA), which sets minimum standards for the funding and administration of DB plans, as well as the rights and benefits of plan members, retirees and other beneficiaries.

DB plans must also comply with the federal *Income Tax Act (*ITA), which provides favourable tax treatment to RPPs and sets maximum contribution and benefit limits.

Subject to certain exceptions as set out in the PBA, an employee's DB benefit is locked in until retirement, to ensure the funds are used for retirement purposes.

DB plans can be either contributory or non-contributory:

- In contributory plans, an employee contributes amounts as required by the plan text (usually determined as a percentage of earnings), and the employer is responsible for the balance of the cost.
- In non-contributory plans, the employee does not contribute and the employer bears the full cost of the benefits.

Employer contributions to a DB plan are based on actuarial recommendations. The actuary makes a number of assumptions about the plan's future experience, demographics and salaries, among other things, which determines the cost of the plan and the associated contribution requirements.

- **Defined Contribution Pension Plan (DC plan).** In a DC plan, the pension benefit is dependent upon the value of accumulated contributions and investment returns allocated to each employee's individual account at the time of retirement. Unlike in a DB plan, a member bears the risk that the accumulated amount may not be sufficient to fund his or her retirement.

  At retirement, the funds in an employee's DC account are typically transferred to a locked-in vehicle (e.g., a Life Income Fund) or used to purchase a life annuity.

  Similar to DB plans, DC plans are subject to Ontario's PBA, as well as to the tax requirements for registered pension plans as set out above. Because DC plan members are only entitled to benefits that can be provided by their individual account, DC plans are not subject to the same funding obligations as DB plans.

  DC plans can also be contributory or non-contributory. In either case, contribution rates are fixed in the plan text and are usually based on a percentage of the member's earnings. Canada Revenue Agency guidelines require a minimum employer contribution of one per cent.

- **Target Benefit Pension Plan (TB plan).** TB plans generally require fixed contributions and are able to address funding deficits by reducing accrued benefits, including pension benefits being paid to retirees. TB plans can be contributory or non-contributory.

  TB plans combine features of DB and DC plans:

  - Similar to DB plans, TB plans "target" (but do not guarantee) a specific benefit level based on a formula and feature monthly lifetime benefits that are paid out of the plan.
  - Similar to DC plans TB plans require fixed contributions and allow plan members to share in the funding risk (i.e., by reducing accrued benefits to address a funding shortfall).

  The PBA currently permits multi-employer pension plans (MEPPs) to offer target benefits. Single-employer pension plans (SEPPs) may offer target benefits if employer contributions are fixed in a collective agreement, but no such plans currently operate in Ontario. No distinct TB framework exists.

  As a result, while certain regulations apply specifically to TB MEPPs and SEPPs, they are treated as DB plans under the PBA and subject to DB rules, including DB plan funding requirements.

  Bill 120, the *Securing Pension Benefits Now and for the Future Act, 2010*, amended the PBA by adding a definition of target benefits to differentiate them from defined benefits. However, this amendment has not yet been proclaimed.

  The Ministry of Finance is in the process of drafting a consultation paper for public feedback on the requirements for a regulatory framework for TB MEPPs.

  For the purposes of the ITA, most TB MEPPs are treated like DC plans.

Pooled Registered Pension Plans (PRPPs)

PRPPs are a new type of tax-assisted individual retirement savings plan offered by licensed financial institutions to workplaces, as well as to the self-employed. Similar to a DC plan, the benefit received out of a PRPP would be dependent upon the value of accumulated contributions and investment returns allocated to each employee's individual account at the time of retirement.

Similar to other tax-assisted savings vehicles, individuals' annual PRPP contributions are deductible in calculating their annual taxable income. However, unlike Registered Retirement Savings Plans (RRSPs) and Group RRSPs, employers' tax deductible contributions are not subject to payroll taxes, and CPP contributions and EI premiums.

After two years of federal-provincial-territorial collaboration in the development and design of PRPPs, the federal government implemented PRPPs for sectors under federal jurisdiction, such as employees in the banking, interprovincial transportation and communications sectors.

The federal legislation also applies to persons employed in Yukon, the Northwest Territories and Nunavut, including the self-employed.

Legislation must be passed in each province before PRPPs can be made available to individuals in provincially regulated sectors and self-employed individuals working in the provinces. Following consultations, in *Budget 2014*, the government committed to moving forward with a legislative framework for PRPPs in Ontario that would be broadly consistent with the model introduced by the federal government and adopted by various provinces.

Consistent with this commitment, the government introduced the Pooled Registered Pension Plans Act, 2014 (PRPP Act) on December 8, 2014.

In particular, Ontario's proposed PRPP Act incorporates many of the features of the federal model, including:

- **Voluntary participation and contributions by employers** — Employers would choose whether to offer their employees a PRPP and whether to contribute to their employees' PRPP;
- **Automatic enrolment of employees** — Where an employer elects to offer a PRPP, enrolment of employees would be automatic unless an employee chooses to opt out within a specified period;
- **Locked-in contributions** — Subject to certain exceptions, an individual would not be able to access his or her PRPP retirement savings, subject to certain prescribed exceptions, until an age prescribed by regulation; and
- **Low cost** — Administrators would be required to provide PRPPs at a low cost to plan members.

Ontario's proposed PRPP Act also includes Ontario-specific features where appropriate (e.g., where provincial law and/or processes are required to apply, for added clarity, or for consistency with Ontario's minimum pension standards legislation). For example, valuation and division of a member's PRPP funds on marriage/spousal relationship breakdown would be consistent with the *Family Law Act* and the PBA, as would the definition of spouse. This approach is consistent with that taken by other provinces.

Registered Retirement Savings Plans (RRSPs)

An RRSP is a tax-assisted, individual retirement savings account offered by a financial institution.

Contributions to RRSPs are deductible from taxable income, reducing income tax payable for the year in which the contributions are claimed. Similar to a DC plan, the benefit received out of an RRSP would be dependent on the value of accumulated contributions and investment returns allocated to an individual's account at the time of retirement.

Similar to DB plans, DC plans and PRPPs, payments from an RRSP are taxed as income when they are withdrawn. Funds in an RRSP are not locked in; one is able to make withdrawals at any age. A group RRSP is sponsored by an employer to encourage retirement savings. Participation in a group RRSP may be voluntary or compulsory depending on the plan text, and contributions (including employer contributions, if any) would also be set out in the plan text.

Contributions are tax deductible for both employers and employees. However, any contributions made by employers would be considered salaried compensation, and are therefore subject to payroll taxes and CPP contributions and EI premiums.

Deferred Profit Sharing Plans (DPSPs)

A DPSP is an employer-sponsored profit sharing arrangement registered as a trust with the CRA and subject to the ITA. A DPSP allows the plan sponsor to share business profits with the plan members by contributing to the DPSP on the plan members' behalf. Member contributions are not permitted.

Contributions are generally linked to the profitability of the business and there is no required minimum contribution. There are, however, maximum contribution limits set by the ITA.

Employer contributions are tax deductible and members do not pay income tax on the funds until they are withdrawn. DPSPs can be offered in conjunction with group RRSPs, whereby the employee contributes to the group RRSP and the employer's matching contributions are deposited to the DPSP.

Withdrawals are taxed as income. Under the ITA, partial withdrawals are permitted while the member is employed, although the employer is permitted to restrict employee withdrawals until termination of employment.

Retirement Savings Landscape

In 2012, the breakdown of the retirement savings landscape was as follows:

- Almost 50 per cent of Ontario workers did not participate in either an RPP or RRSP.
- 34 per cent of Ontario's working population were members of an RPP.
    - 77 per cent of public sector workers participate in an RPP while only 28 per cent of private sector workers participate in an RPP.
- 16 per cent of Ontario workers did not have a pension plan but contributed to a RRSP.

Defined Benefit (DB) and Defined Contribution (DC) Breakdown:

- 70 per cent of RPP members in Ontario have a DB plan.
- 16 per cent of RPP members in Ontario have a DC plan, and 14 per cent have a hybrid/other plan.

DC Plans:

- In 2013, almost 400,000 Ontarians participated in a DC plan.