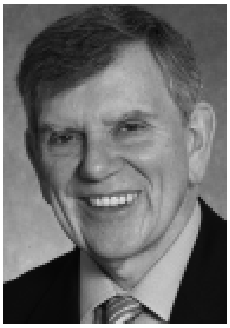

The CPP Proposed Changes

Patrick Longhurst

On May 25, 2009, the federal, provincial and territorial ministers of finance, as joint stewards of the Canada Pension Plan, announced the results of the Plan's latest actuarial review. Federal Minister Jim Flaherty indicated that, "The CPP remains on a firm financial footing. Canadians can count on an affordable CPP today and in the future." The finance ministers agreed that the annual combined contribution rate would remain at 9.9 percent of pensionable earnings. So, if you hear the Plan is in trouble and you will never receive your pension, please don't take any notice. The CPP should remain a core element in most people's retirement planning.

In addition to confirming the financial status of the CPP, the ministers also announced proposed changes which will take effect starting in 2011, following approval by the Parliament of Canada and provincial governments. These changes will have no impact on you if you are already receiving a retirement pension, disability benefits, survivor benefits or combined benefits, or if you will begin to receive these benefits before 2011. However, knowing that the changes are coming may have an impact on the decisions that some of you may take.

The proposed changes are far-reaching and come under three categories:

- Improved flexibility,
- Improved pension coverage, and
- Improved fairness.

My comments are based on the information paper which was posted on the Department of Finance Canada website. If you want to read the whole document, go to www.fin.gc.ca , select "News Releases" for May 25, 2009 and then click on "Information Paper".

Improved Flexibility

➠ **Removal of the Work Cessation Test** - At the present time, anyone aged under 65 who wishes to start receiving their CPP retirement benefit must have either stopped working or reduced their annual income to less than the maximum CPP benefit level. After having met these requirements for at least two months, the individual may then return to work and/or earn more. The new proposals will eliminate these rather artificial work cessation rules effective January 1, 2012, so that anyone aged over 60 can apply for their CPP without any earnings test being applied.

➠ **Increase in the General Low Earnings Dropout** - By way of explanation, the total span of time during your life when you may contribute to the Canada Pension Plan is called your contributory period. It is used in calculating the amount of any Canada Pension Plan benefit to which you become entitled. Your contributory period begins when you reach age 18 or January 1, 1966 (the start of the CPP) and continues until you begin receiving your retirement pension, reach age 70 or die (whichever is the earliest). So, if you have always made the maximum contributions throughout your contributory period, you are eligible for a full CPP pension payable at age 65 ($908.75 per month in 2009).

Most of us do not have a full contribution history for a number of reasons:

- We were out of the workforce for some of the contributory period.
- We had years of low earnings.
- We were disabled and unable to work.

To keep your pension as high as possible, the CPP drops out some parts of your contributory period from the calculation:

- Periods when you stop working or your earnings are lower while you raise your children under the age of seven.
- Months after the age of 65 (which can be used to replace any low-earning months before 65).
- Any month when you were eligible for a CPP disability benefit.
- The 15 percent of your contributory period in which your earnings were lowest.

So, you are not penalized if your years of low contributions are covered by the dropout rules.

The proposed changes would increase the 15 percent dropout to 16 percent in 2012 and 17 percent in 2014, allowing for greater periods of low earnings to be dropped out and increasing the potential for a member to receive a maximum pension at retirement.

Improved Pension Coverage

At the present time, if you do opt to start your CPP pension before age 65, then your contributions to the Plan are over, regardless of whether you subsequently return to the workforce or not. Under the new proposals, if you start your pension early, continue to work, and are aged under 65, then you and your employer will be obliged to continue to contribute to the CPP and you will earn additional pension benefits based on your rate of pensionable earnings. An individual earning in excess of the Years Maximum Pensionable Earnings (YMPE), $46,300 in 2009, will earn an additional pension equal to 1/40th of the maximum pension payable in that year. Presumably, self-employed individuals will be on the hook for both the employee and employer contributions.

Individuals who are still working after age 65 could opt to continue to contribute and earn extra pension benefits. If they do opt to contribute, then their employers will be required to contribute as well.

This change will be of particular benefit to new Canadians or those with no coverage under an employer-sponsored pension plan, in that it will provide a means to enhance their CPP entitlements, while complementing their lifestyle.

Improved Fairness in the Pension Adjustments for Early and Late CPP Take-up

At the present time, individuals who opt to receive their CPP pensions before age 65 are subject to a benefit which is reduced by 0.5 percent for each month prior to 65. Alternatively, those who opt to commence their pensions after age 65 are entitled to an increase of 0.5 percent for each month after 65. Planners like me have spent many hours trying to rationalize what option makes the most sense for various clients with different life expectancies and family situations.

The new proposals are supposed to provide greater equity between individuals retiring at different ages:

- The early retirement reduction would be gradually increased to 0.6 percent per month for each month before age 65. This would be phased in over a five-year period starting in 2012.
- The late pension augmentation would be gradually increased to 0.7 percent per month for each month that the pension is taken after an individual's 65th birthday, up to age 70. This would be phased in over a three-year period, starting in 2011.

In an effort to maintain equity in the future, the finance ministers will ask the Chief Actuary of the Plan to review these adjustments every nine years, starting in 2016.

Next Steps

There is a lot to digest in these proposed changes, and it may be that even the Department of Finance has not fully thought through all the implications. It does mean that the challenge of getting the best value out of the CPP just became a lot more complicated. But remember, if you have already retired, or plan to do so before 2011, these changes will not affect you.

If you let me know your questions about these proposals, I will be happy to research them and give you some answers in my next column.

On the lighter side, some commentators have hailed these proposals as a "sea-change" in government pension policy. As this is the latest cliché to be used by politicians and such, I wondered how many of them actually know where the expression comes from. According to *Brewer's Dictionary of Phrase and Fable,* a sea-change is apparently a magical change, as though brought about by the sea. The phrase comes from Ariel's song in the Tempest:

Full fathom five thy father lies;
Of his bones are coral made;
Those are pearls that were his eyes.
Nothing of him that doth fade
But doth suffer a sea-change
Into something rich and strange.

Shakespeare could have been talking about the Canada Pension Plan!

Patrick Longhurst, President, Longhurst & Jack Inc., Toronto, ON (416) 815-7200, enquire@longhustandjack.ca, http://www.longhurstandjack.ca