



# More Thoughts on Pension Plans

Raising the age of eligibility is just one solution to the problem of pension sustainability

**W**hen do you want to retire? After the turmoil in the financial markets of the last two years, perhaps the better question is *When can you afford to retire?*

Most Canadians can forget about Freedom 55. Polls taken in the last year have shown that anywhere from one-quarter to one-third of all Canadians plan to delay their retirement by at least a few years. So forget Freedom 55. Let's talk *Freedom 65*. But is that such a bad thing, considering the state of our pension plans?

## The Problems with Pension Plans

All pension plans work on the belief that contributions and investment returns will be more than sufficient to cover payouts to participants. But the economic realities of the last few years have wreaked havoc on that model and the future is hardly promising.

The financial crisis of 2008 hit pension plans hard. Canadians saw an average 20 per cent loss in their portfolios. The subsequent recession has kept interest rates low and suppressed investment returns.

Meanwhile, the underemployed or unemployed make little or no contribution to pension plans, including the Canada Pension Plan. Three-quarters of private sector employees do not have an occupational pension plan. The number of employers offering defined benefit plans is on the decline while defined contribution plans have seen investment erosion and slow growth.

Yet Canadians in general live longer, healthier lives — and have the added benefit of stronger social services — than ever before. A population that lives longer puts an added burden on pension plans as it draws upon benefits for longer periods. You might say we're about to be victims of our own good health. So now is the time for strategies that provide sustainable retirement income to Canadians.

## Re-Thinking Retirement

When Canadian life expectancy rates were in the low 70s, retiring at 65 made sense. But today's 65-year-old man can expect to live to age 83. Today's 65-year-old woman can expect to live to 86.

To demonstrate how radically the life expectancy of the average Canadian has changed, consider this: when today's 83-year-old woman was born, her life expectancy was actually 55. The extra 30 years of longevity are due entirely to changes in nutrition, exercise and healthcare. Two generations ago, the typical 60-year-old spent a lot of time in a rocking chair; today's 60-year-olds are still out there "rockin'" — or "zooming," as the case may be.

But not all. I know many older people who are afraid to retire because they don't know what they'll do with their time, don't have

enough money to retire, or are afraid that their savings won't last for very long. The prospect of retiring at 55 and living for 30 years without something productive to do is a scary one. If you've worked hard all your life then you're used to keeping busy and being productive. Retirement for you does not mean vegetating.

## Time for Adjustments

The federal and provincial governments are making significant changes to adjust to the new reality. The feds have moved the mandatory age to convert RRSPs into annuities from 69 to 71. Ontario has abolished its mandatory age of retirement.

The Canada Pension Plan has been tweaked to discourage early retirement and "incentivize" a longer working life. Upcoming changes, which kick in fully by 2016, raise the premium for later retirees and add an extra 42 per cent to pension payments for those who take their retirement pension at 70. The changes also see an increase to the penalty for drawing one's pension early.


Expect to see a lot more of this in the coming years, as governments use public policy to decrease liabilities through their own version of the carrot and the stick.

The private sector is also taking measures to increase capital and decrease liability. Contributions are rising, eligibility and payouts tightening. Currently, a popular trend in Europe is to offload longevity risk to insurance companies, enabling companies to transfer pension liabilities to third parties. The insurer runs the scheme and pays out pensions to members as they become due. This year, for example, BMW unloaded more than four billion dollars in pension risk to Deutsche Bank, one of the largest deals ever of its kind.

## Affordable Retirement

Ultimately, the quality of our retirement will depend upon factors at both the macro and micro levels.

At the macro level, mandatory ongoing sustainability planning to ensure the combination of investment income, reasonable pension contributions and affordable retirement benefits. At the individual level (the micro level), sound retirement planning, including financial and lifestyle planning, with plans to supplement income by working part-time or withdrawing only partial retirement benefits.

So when can you afford to retire? Well, now that I've given you a few more of my thoughts on pension plans, let's rephrase that question again: *What kind of retirement can you afford?* 

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