*Intelligence* MEMOS


From: Idan Shlesinger, Michelle Loder, and Gavin Benjamin

To: Canadian Pension Plan Sponsors, Policymakers and Other Stakeholders

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Re: **Shift in Focus to Improve Retirement for Canadians**

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With innovations emerging to address the shortcomings of defined-contribution (DC) pension plans and Group Registered Retirement Savings Plans, it is time for these capital accumulation plans to shift their focus from building assets to providing lifetime retirement income for retirees.

With more than $1.5 trillion in assets as well as a growing membership and annual contributions, DC pension plans and Group RRSPs can significantly improve the retirement security of Canadians over the coming decades. Critically, DC plans and Group RRSPs need to help retirees meet the challenges encountered during the decumulation phase, the time when employees stop accumulating capital and start drawing down on assets.

Our new C.D. Howe Institute report examines the challenges of this important phase, current practices as well as emerging new options.

The time is right for program sponsors, regulators and industry stakeholders to embrace a more comprehensive vision for DC plans and Group RRSPs, beyond capital accumulation. New tools and emerging options in the marketplace can help improve the post-retirement income security of Canadians.

Canadians have three main options to draw down their accumulated capital in retirement:

i. An investment account with withdrawal options such as life income funds (LIFs) and registered retirement income funds (RRIFs) for assets originating from DC pension plans or Group RRSPs respectively.

ii. Variable benefits accounts within DC registered pension plans that allow for gradual income withdrawals on a similar basis to LIFs, a relatively new option taking advantage of the scale and legal structure of DC pension plans.

iii. Annuities sold by insurance companies, which have been purchased by relatively few retirees. Individual annuities insure against longevity and investment risk, but the full protection comes at a cost and often limited flexibility.

Other options are emerging. Notably, recent amendments to the *Income Tax Act* add two new vehicles that can significantly enhance Canadians' available choices: Variable Payment Life Annuities (VPLAs) and Advanced Life Deferred Annuities (ALDAs).

VPLAs pool retired employees' investment and longevity risk. Within a DC pension plan (but not available for a Group RRSP), a VPLA fund converts the account balance of a retiring employee into a monthly pension payable for the remainder of the retiree's life, based on assumptions about investment and mortality experience, and is adjusted periodically to reflect the pool's experience.

Meanwhile, an ALDA provides a guaranteed lifetime annuity, with payment beginning as late as the end of the year an individual turns age 85. The *Income Tax Act* limits the purchase size to no more than 25 percent of an individual's DC account and no more than $150,000 (indexed to inflation) from an individual's registered account balances.

Many employers already sponsor DC plans for their employees, in which case they already have the infrastructure in place to add features such as variable benefits and VPLAs in an efficient and cost-effective manner.

Employers are also well positioned to advocate for innovation from service providers and for legislative changes that enhance the decumulation landscape in Canada.

Five actions policymakers can take to improve and simplify access to effective decumulation strategies and improve retirement outcomes include:

i. Regulatory harmonization of locking in and unlocking rules across jurisdictions to allow a single set of rules to apply to DC assets during retirement, irrespective of the jurisdiction under which the accumulation has taken place;

ii. The regulatory harmonization of variable benefit payment, variable payment lifetime annuity and LIF maximum withdrawal rules irrespective of the jurisdiction in which the assets have accumulated;

iii. Legislative and regulatory support for pooled decumulation vehicles that permit transfers of retirement assets including those derived from employer sponsored pension plans, personal RRSPs, etc;

iv. Specific decumulation guidelines for program sponsors to provide support for the adoption of decumulation frameworks; and

v. Support and guidance for the provision of decumulation-specific retirement advice for retiring members.

With so much to be gained, all stakeholders should grasp the opportunity that is before us to enhance our retirement system as well as improve the financial and total wellbeing of Canadians, during both their working years and in retirement.

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