Intelligence MEMOS

From: William B.P. Robson

To: Members of Parliament

Date: October 11, 2018

Re: **PENSIONS OF FEDERAL EMPLOYEES ARE WAY UNDERFUNDED – INCLUDING YOURS**

The House of Commons Committee on Government Operations and Estimates recently held hearings about the pensions for federal government employees. That is good. The federal government provides pension benefits to its employees that are worth more than three times what other Canadians can save for retirement – neither wise nor fair. Worse, the plans that provide those benefits – the MPs' pension plans being a case in point – are badly underfunded. The burden that paying future benefits will impose on taxpayers and future contributors will stress the plans themselves and federal finances more generally.

It may not be news that MP pensions are generous – but still…. The plan for MPs accrues entitlements, indexed to inflation, at the rate of 3 percent annually to a maximum of 75 percent of the best five years of pay to any MP or senator who serves for six years or more. That promise is as good as the most senior federal government debt: value it at its equivalent in indexed bonds, and it is worth almost $100,000 *annually* to the average sitting MP. That might surprise the average Canadian, who can't defer taxes on more than $26,000 odd in an RRSP or defined-contribution pension plan.

What would certainly surprise most people – including most MPs – is that there is no money in their plan to back those promises. The most recent report from Canada's Chief Actuary on the plan showed "account balances" that look like assets to offset the plans' liabilities. But those balances are just book-keeping entries. The "contributions" MPs believe they are making to the plan flow into general government revenue, and Ottawa's contributions as an employer are a fiction. The plan's status in reality is:

- Total amount needed to pay the plan's promises at today's yields: $1.15 billion
- Actual assets in the plan: zilch
- Unfunded liability, or money yet to be raised to pay the promises: $1.15 billion.

While the MPs' plan stands out for being particularly lavish and completely unfunded, its defects have parallels in other federal employee plans that collectively represent a major – and heavily disguised – transfer from taxpayers to public employees. A key common element is that these plans understate their costs by using high discount rates when valuing the payments they will make in the future. Discounting future payments at a high rate shrinks the liability reported on a pension plan's balance sheet, and therefore the federal government's reported debt. It also shrinks the accruing benefit reported on a plan's statement of operations, and therefore the cost that appears in the federal budget.

As Alex Laurin and I have pointed out, the unfunded pension liability reported in the federal government's financial statements for 2017 – which, at $150 billion, was already a big chunk of Ottawa's debt – should have been at least $246 billion. The value of pension benefits accrued by federal government employees that year was more than double what a reader of Ottawa's statement of operations would conclude. Although 2012 reforms established a general principle that employee contributions should cover about half of accruing benefits, the fact that reported benefit accruals are too low means that employee contributions are in reality well short of half the cost.

The pension plan for MPs is a particular problem. Not only because it is lavish and totally unfunded. Also because it is the plan for our elected representatives – the people who ought to be leading the charge for better, and better funded, retirements for all Canadians. MPs should ensure that the pensions for other federal employees are part of an effective overall compensation package, and that all promises to pay future benefits are properly funded. They should support meaningful financial reporting of the value of pension promises and the assets that back them. They should improve the *Income Tax Act* and other federal laws and regulations to support saving, in registered pension plans and in other arrangements, that will let Canadians maintain their standards of living in retirement. When their own plan provides benefits far beyond what other Canadians can obtain or provide for themselves, and – contrary to what its published statements would suggest – leaves responsibility for paying those benefits entirely on future taxpayers, they are ill placed to do any of those things.

Many Canadians will need better, and better funded, retirements than they can currently obtain. Their MPs, already far ahead themselves, should lead the way to sustainably improving the system for everybody.

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