national union

pensions backgrounder #3

An Overview of Canada's Public Pension System

Part 3 in a Series

The full series of pension backgrounders are contained in the National Union's Pensions Manual, Fourth Edition—available from the National Office

Updated January 2008

BACKGROUNDER #3

An Overview of Canada's Public Pension System

••• The First Tier of Retirement Income in Canada

Previous generations of Canadians along with the labour movement fought hard to win universal public pensions both to recognize the contribution senior citizens have made to our society, and to provide the elderly some measure of comfort in their retirement years. Moreover, like all public programs and services, our pension system is an important tie that binds us together as a nation. It is an expression of our collective commitment to one another and to the fundamental democratic principle that all citizens have the right to services that enrich us all.

The main components of Canada's public pension system are three publicly administered programs: the Old Age Security program, the Guaranteed Income Supplement and the Canada Pension Plan. Some provinces also have a specific income supplement program for seniors.

Public pensions, unlike most private plans, are 100% portable and move with people from one job to another. They are fully indexed to inflation and offer survivors' benefits. And because public pensions are publicly run, administration costs are extremely low – about 1% of total benefits.

••• An Important Factor in Addressing Seniors' Poverty

Thanks to public pensions, Canada has made tremendous gains in overcoming poverty amongst elderly citizens, and providing our seniors with much better prospects for a dignified and secure retirement.

Until recently, the percentage of seniors with low incomes had been declining. It went from 21% in 1980, to 10% in 1990, to 7% in 2003. The National

Council of Welfare points out that this catch-up period is over. Since the middle of the 1990s, seniors' income has reached a ceiling and the gap between seniors' revenues and those of other Canadians is now increasing. Between 1997 and 2003, the mean income of senior households increased by $4,100, while the average income of other Canadian households increased by $9,000. The situation is even more pronounced for seniors living alone.

• • • Public Pensions are the Only Source of Income for the Majority of Seniors

Public pensions therefore have been especially important for lower and middle-income seniors. They are less likely to have been able to accumulate large private retirement savings during their working lives, and less likely to have worked in jobs that provided decent private pension plans.

Remember less than two in five Canadian workers are members of a registered pension plan and public pensions (OAS, GIS and CPP or QPP) accounted for over half of all income for six out of every ten seniors in 2001. Without these public pensions, poverty will once again become a fact of life for millions of seniors.

There is, of course, a need for changes to our public pension system. Benefits are still low and need to be strengthened.

The following is an overview of each of the components of Canada's public retirement income system:

Old Age Security (OAS)

The Old Age Security program is the first tier of Canada's public retirement income system. The *Old Age Security Act* came into force in 1952, replacing legislation from 1927 requiring the federal government to share the cost of provincially-run, means-tested old age benefits.

The Act has been amended many times. Among the most important changes have been:

- the drop in age of eligibility from 70 to 65 (1965);
- the establishment of the Guaranteed Income Supplement (1967);
- the introduction of full annual cost-of-living indexation (1972);
- quarterly indexation (1973);
- the establishment of the Spouse's Allowance (1975);
- payment of partial pensions based on years of residence in Canada (1977);

- the inclusion of Old Age Security in international social security agreements (ongoing);
- the extension of the Spouse's Allowance to all low-income widows and widowers aged 60 to 64 (1985);
- the introduction of a 'clawback' in the 1989 federal budget which put an end to the universality of the Old Age Security; maximum of one year of retroactive benefits (1995);
- the ability for an individual to request that their benefits be cancelled (1995); and
- the extension of benefits and obligations to same-sex common-law partners (2000).

The Old Age Security program is financed from Government of Canada general tax revenues. It is administered through the Income Security Programs Branch of Social Development Canada.

All benefits payable under the *Old Age Security Act* are adjusted in January, April, July and October if there are increases in the cost of living as measured by the Consumer Price Index.[1] As of January 2008, the maximum monthly OAS benefit was $502.31.

Since 1989, older Canadians with incomes above a threshold amount have been required to pay a surtax of 15% on incomes above the threshold, up to the amount of a full OAS benefit. Pensioners with an individual net income above $64,718 must repay part of the maximum Old Age Security pension amount. The repayment amounts are normally deducted from their monthly payments before they are issued. The full OAS pension is eliminated when a pensioner's net income is $104,903 or above.

Despite its history as a universal program for older Canadians, it has clearly taken on an income-tested character. The income threshold at which OAS benefits begin to be taxed back is just over 1.4 times average wages and salaries, and the full amount is taxed back at 2.25% of average wages and salaries.

Guaranteed Income Supplement (GIS)

The Guaranteed Income Supplement (GIS) is a monthly benefit paid to residents of Canada who receive a basic Old Age Security (OAS) pension and who have little or no other income. In law, the GIS is a component of the OAS program.

The GIS was created in 1966 as a small program to compensate the elderly of that time for the fact they would not get to participate in the earnings-related Canada Pension Plan that was being created at that time. Like the OAS, the GIS is administered by the Government of Canada. It is paid for out of the general revenues of the Government of Canada, and GIS expenditures show up as expenditures in the federal government's budget.

GIS payments may begin in the same month as OAS pension payments. Recipients must re-apply annually for the GIS benefit by filing an income statement or by completing an income tax return by April 30. Thus, the amount of monthly payments determined for the year may increase or decrease according to reported changes in a recipient's yearly income.

Unlike the basic OAS pension, the GIS is not subject to income tax. The GIS is not payable outside Canada beyond a period of six months, regardless of how long the person has lived in Canada.

To receive the Guaranteed Income Supplement benefit, a person must be receiving an Old Age Security pension.

The GIS is an income-tested benefit. A maximum benefit is created for a single elderly person and for elderly couples. The maximum benefit for couples is less than twice that for the single elderly.[2] Maximum benefits are paid to the elderly with no income except OAS. Then benefits are reduced by 50 cents per dollar of income from sources other than OAS.

As of January 2008, the maximum benefit for the single elderly is $634.02 per month. The maximum benefits are adjusted quarterly to reflect changes in consumer prices. GIS benefits are not taxable.

Under the GIS program, there is also a Spousal Allowance and a Survivor Allowance for seniors aged 60 to 64 with low incomes. They are designed to bridge the gap until these people become eligible for the OAS pension.

A **Spousal <u>Allowance</u>** is available to 60 to 64 year-old low-income spouses or common-law partners of OAS pensioners who receive the GIS. The maximum monthly Spousal Allowance benefit is $921 as of January 2008. The benefit is reduced according to a couple's yearly income; if a couple's combined yearly income, not including their OAS / GIS pension, exceeds $28,176 the 60 to 64 year-old spouse or common-law partner is not eligible for the Spousal Allowance.

A **Survivor <u>Allowance</u>** is available to 60 to 64 year-old low-income spouses or common-law partners whose spouses or common-law partners have died. The maximum monthly Survivor Allowance benefit is $1,020.91 as of January 2008. The benefit is reduced according to an individual's yearly income; if the yearly income exceeds $20,520 she / he is not eligible for the Survivor Allowance.

If a person is receiving the Allowance and her / his spouse or common-law partner dies, she / he will be switched to the Allowance for the survivor.

In combination, OAS and GIS provide a minimum income floor for older Canadians. For the single elderly, the floor currently amounts to $13,635.96 per year (as of January 2008). This is $3,934 below the 2006 low income line for a single person in a large urban centre as established by Canada's national statistical agency, Statistics Canada. For an elderly couple, the minimum income guarantee is $23,107 (as of January 2008), which is $1,723 above the 2006 low income line for a large city. As is commonly the case elsewhere, too, the single elderly in Canada are overwhelmingly women.

Maximum Old Age Security benefit rates as of January 1, 2008

Type of Benefit	Maximum Monthly Rate January – March 2008
Basic Old Age Security pension	$502.31
Guaranteed Income Supplement Single Spouse/Common-law partner of • a pensioner • a non-pensioner • an Allowance recipient	 $634.02 $418.69 $634.02 $418.62
The Allowance • regular • survivor	 $921.00 $1,020.91

Canada / Quebec Pension Plan (CPP / QPP)

CPP / QPP is a government-sponsored pension plan funded solely by contributions made by employees, employers and self-employed people and from interest earned from the investment of the funds. These plans came into effect on January 1, 1966 and provide very similar benefits. The goal is to provide working Canadians with an income related retirement pension of 25% of a worker's earned income to a maximum of 25% of the average industrial wage.

Supplementary benefits include contributor disability pension, benefits to dependent children of deceased or disabled contributors, surviving spouse's pension and a lump sum death benefit.

Benefit calculations are based on how much and for how long a contributor has paid into the CPP.[3] Benefits are not paid automatically – everyone must apply and provide proof of eligibility. However, once eligibility is determined, CPP benefits are paid even if the beneficiary also receives income from other sources.

Benefits are adjusted in January of each year as needed to reflect increases in the average cost of living, as measured by the Consumer Price Index. Participation is compulsory for eligible individuals and covers practically all employees and self-employed persons.

Contributions to the CPP are paid on earnings between a minimum and a maximum amount. The minimum earnings in any year on which no contributions are paid, known as the **Year's Basic Exemption (YBE)**, are $3,500 and have remained frozen at that amount since 1998.

The maximum, known as the **Year's Maximum Pensionable Earnings (YMPE)**, is adjusted annually to reflect the growth in the average Canadian industrial wage. The YMPE for 2008 is $44,900. Contributions stop once a contributor reaches the age of 70 or begins to receive a CPP retirement pension or disability benefit. The contribution rates for 2008 are 4.95% for employees and 4.95% for employers. People who are self-employed pay both portions, for a total of 9.9%. Employers and employees make approximately 94% of contributions and the remaining 6% comes from the self-employed.

The amount of each contributor's pension depends on how much and how long he or she has contributed and at what age he or she begins to draw the benefits. The monthly maximum retirement pension for a person who retires at age 65 as of January 2008 is $884.58 and the average payment in October 2007 was $481.46.

The CPP offers flexibility with respect to the age of retirement. Seniors can take their pension as early as the age of 60 or as late as 70. The CPP permanently reduces the pension by 0.5% per month for those who take their benefit before their 65th birthday, reflecting the fact that these seniors will, on average, receive their benefit longer than someone who retires at the age of 65. For those who take their benefit after their 65th birthday, the CPP permanently increases the pension by 0.5% per month, reflecting the fact that these seniors will receive their benefit for a shorter amount of time on average. The adjustments are intended to ensure there is no advantage or disadvantage from taking the retirement benefit at a particular age.

Disability Benefits – An individual is eligible to collect disability benefits if that person "… is determined in a prescribed manner to have a severe and prolonged mental or physical disability …" according to the CPP Act. The term 'prolonged' means that a person's disability is expected to continue for a significant period after the time of application, and that its duration cannot be predicted with any certainty, or is likely to result in death. A 'severe' disability is defined as one that impairs to such an extent that a person is "… incapable regularly of pursuing any substantially gainful occupation….". A person qualifies on medical grounds only when the 'severe' and 'prolonged' criteria are met simultaneously at the time of application. However, the severity of a disability is assessed first. If an applicant does not meet the 'severe' criteria, the question of whether the disability is prolonged is not considered.

The maximum monthly disability benefit as of January 2008 is $1,077.52; the average payment in October 2007 was $785.77.

On top of that benefit, the disabled pensioner will receive an additional children's monthly benefit for each child under the age of 18. If the child is between the ages of 18 to 25 and still attending a post-secondary educational institution, the benefit is paid directly to him / her. As of January 2008 the children's monthly benefit was a flat rate of $208.77.

Survivor Benefits – Survivor benefits are paid to the surviving spouse or common-law partner of the contributor and his / her dependent children. The amount of the spouse's portion of the monthly survivor benefit varies depending on a number of factors, including the age of the spouse or common-law partner at death and whether the beneficiary also receives other CPP benefits. The maximum monthly survivor benefit for those age 65 and over was $530.75 and the average payment in October 2007 was $313.14.

The children's monthly benefit is also paid on top of the spouse's benefit. The eligibility criteria and the amount of the benefit is the same as the children's monthly benefit under CPP disability benefits.

Death Benefits – The death benefit is a one-time payment to, or on behalf of, the estate of a deceased Canada Pension Plan contributor. As with most Canada Pension Plan benefits, the amount of the death benefit depends on how much, and for how long, an individual pays into the Canada Pension Plan. CPP first calculates the amount that one's Canada Pension Plan retirement pension is, or would have been if one had been age 65 when death occurred. The death benefit is equal to six months' worth of this 'calculated' retirement pension, up to a maximum of $2,500. The average payment in October 2007 was $2,237.81.

Other Provisions – The CPP includes provisions that compensate for periods of low earnings, namely the child-rearing drop-out provision (CRDO) and the 15% general drop-out provision. The CRDO allows the CPP to drop up to seven years of low or zero earnings (due to child rearing) from the calculation of a contributor's CPP disability, survivor and / or retirement benefit.

Maximum Canada Pension Plan benefit rates as of January 1, 2008

Type of CPP Benefit	Maximum Rates for 2008
Retirement pension (at age 65)	$884.58
Disability pension	$1,077.52
Death benefit	$2,500.00
Survivor's pension (under age 65)	$493.28
Survivor's pension (age 65 & over)	$530.75
Combined pensions: Survivor/Retirement (at age 65) Survivor/Disability	 $884.58 $1,077.52
Disabled contributor's child benefits Deceased contributor's child benefits	$208.77 $208.77
Yearly Maximum Pensionable Earnings (YMPE)	$44,900.00
Year's Basic Exemption (YBE)	$3,500.00
Employer / Employee CPP Contribution Rate	4.95% each up to a maximum of $2,049.30 annually
Self-Employed CPP Contribution Rate	9.9% up to a maximum of $4,098.60 annually

The 15% general drop-out provision is for low or zero earning years and applies to all contributors. The Plan has other provisions under which married or common-law spouses may either share their pension (if the union is intact), or split their credits (if the union has dissolved).

••• Provincial and Territorial Income Supplement Programs

Several provincial governments and both territories have recognized the inadequate living conditions of those relying primarily on OAS or GIS and SPA for support and provide their own supplement programs. Such programs exist in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Northwest Territories and Yukon. All these are income tested and therefore only available to the poorest seniors and are not indexed to the inflation rate.[4]

In addition, provinces and territories provide other kinds of benefits to seniors such as prescription drug plans, heating oil subsidies and home care assistance programs, with eligibility based on receipt of the GIS. Eligible seniors who do not receive the GIS may also be eligible for, but not receiving, a variety of other supports, which could significantly improve their quality of life and standard of living.

••• Integration of Private and Public Pension Plans

Private and public plans are closely integrated. When an individual receives a pension from one plan, this may have an impact on the benefits that person is entitled to receive from other plans.

Income-based benefits, such as the Guaranteed Income Supplement, the Allowance and the Allowance for the Survivor, as well as benefits received from provinces and territories, take into account any CPP / QPP benefits and other income received by the beneficiary.

CPP / QPP benefits are never reduced, but when they begin to be paid out, they may have an impact on the level of other benefits to which an individual is entitled.

Some workplace pension plans are integrated into the CPP or QPP. In such cases, the level of benefits of the workplace pension plan will take CPP / QPP benefits into account. It is important for workers to check whether their pension plan is integrated and, if so, what the impact will be on the monthly amount they will receive throughout their retirement years.

The integration with CPP / QPP may be achieved through a direct or an indirect reduction method. The indirect reduction method is more common. In most cases, it consists of two contribution or benefit rates – a lower rate for incomes lower than the yearly maximum pensionable earnings (YMPE), and a higher rate for incomes above that level. For example, the pension amount per year of service may be 6.0% of earnings up to the YMPE level, and 8.0% of earnings above that level.

Under the direct reduction method, contributions or benefits are lowered by an amount equal to a portion or the total amount of CPP / QPP contributions or benefits. For example, a worker may be retired prior to being eligible for CPP benefits but is entitled to receive benefits from her / his workplace pension. Once the worker is entitled to receive CPP benefits, his / her workplace pension benefits are lowered by an amount equal to the CPP benefits the worker is entitled to receive.

CPP / QPP benefits may also have an impact on the level of benefits received from a private-sector disability insurance plan. In addition, most workers' compensation plans take into account income from the Canada Pension Plan.

[1] For the most current benefit rates for the Old Age Security program, visit the following website - http://www.sdc.gc.ca/en/isp/oas/oasrates.shtml

[2] For the most current maximum benefit rates for elderly singles and couples under the Guaranteed Income Supplement (GIS) program, visit the following website - http://www.sdc.gc.ca/en/isp/oas/oasrates.shtml

[3] For the most current maximum benefit rates under the Canada Pension Plan (CPP) program, see Table at the end of this chapter or visit the following website - http://www.sdc.gc.ca/en/isp/pub/factsheets/rates.shtml

[4] For details on each of these provincial and territorial-based programs visit the following website - http://chp-pcs.gc.ca/CHP/index_e.jsp/pageid/4005/odp/Top/Health/Seniors/Publications/Provincial_Guides_to_Programs_and_Services