A STRONGER RETIREMENT INCOME SYSTEM

MEETING THE EXPECTATIONS OF QUEBECERS OF EVERY GENERATION

Finances Québec

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2011-2012 Budget

A Stronger Retirement Income System
Meeting the Expectations of Quebecers of Every Generation

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INTRODUCTION

Quebecers enjoy one of the world's most effective retirement income systems. It is a model often cited as an example because of its diversified structure. Thanks to this system, most retirees in Québec:

— receive a retirement income that keeps them out of poverty;

— enjoy a standard of living similar to what they had before leaving the labour market.

Despite its strengths, over the coming years, Québec's retirement income will face challenges foremost among which is the aging of the population.

— The rapid increase in the number of people age 65 or over combined with improved life expectancy will generate significant financial pressure on pension plans that not only will have to pay a pension to more retirees but also have to pay these pensions over a longer period.

— This additional financial burden will be accentuated by a reduction in the number of individuals of working age who can contribute to pension plans.

To deal with this challenge, steps must be taken now to ensure that the retirement income system continues to meet its objectives, namely:

— that current and future retirees can continue to count on a stable and predictable basic income when they retire;

— further encourage voluntary saving so that workers who do not have access to an employer-sponsored pension plan can have enough income to maintain their standard of living in retirement.

To that effect, the Québec government intends to make changes to Québec's retirement income system. These changes will be made gradually to minimize their impact on workers and businesses. Accordingly, the 2011-2012 Budget stipulates that:

— adjustments will be made to the Québec Pension Plan, as of January 1, 2012, to guarantee a basic income to Quebecers at retirement;

— the government undertakes to allow the implementation of new voluntary retirement savings plans to foster the savings of Quebecers.

1. QUÉBEC'S RETIREMENT INCOME SYSTEM: CONVINCING RESULTS

1.1 A diversified system based on three pillars

Québec's retirement income system is based on three pillars:

- Pillar 1: the Old Age Security Pension (OASP) and the Guaranteed Income Supplement (GIS);
- Pillar 2: the Québec Pension Plan (QPP);
- Pillar 3: private savings, including supplemental pension plans (SPP) and registered retirement savings plans (RRSP).

Being based on compulsory and voluntary plans, the retirement income system offers Quebecers great flexibility. They can regularly adapt the amount they save to their career profile, lifestyle or planned retirement age. In addition, since the system is mixed (private and public savings), the various financial risks are shared among the state, employers and workers.

Lastly, in addition to these three pillars there are other assets such as real estate and equity in a business. These assets represent a significant patrimony on which Quebecers can count when they retire.

CHART 1

Pillars of Québec's retirement income system

	Three levels	Features
Pillar 3 Voluntary participation	**Private savings** Group pension plans Registered retirement savings plan (RRSP)	Group pension plans (2 million workers) Individual RRSPs (1.1 million workers)
Pillar 2 Compulsory participation	**Public plans** Quebec Pension Plan (QPP) Canada Pension Plan (CPP)	Plans funded by contributions by workers and their employers (roughly 3.9 million workers) Provide a pension that will replace up to 25% of earned income
Pillar 1 Funded by taxes	**Old Age Security** Old Age Security Pension (OASP) Guaranteed Income Supplement (GIS)	Basic pension granted to persons age 65 or over who have lived in Canada for at least 10 years (99% of seniors receive it)

Description of the pillars of Québec's retirement income system

Pillar 1: Old Age Security

The first pillar is designed to provide all retirees with a basic income. It consists of the Old Age Security Pension (OASP) and the Guaranteed Income Supplement (GIS) that are administered by the federal government.

The OASP was introduced in 1952. It provides a basic monthly pension to those age 65 or over, whether they have worked or not, provided they have lived in Canada for a certain number of years. In January 2011, the maximum monthly OAS benefit was $524.

The GIS was implemented in 1967. It provides low-income older people with an additional income. The maximum monthly GIS benefit is $662 in January 2011. It is paid to single persons and couples whose income, excluding the OASP, GIS and allowances, is less than $15 888 and $20 976 respectively. For a single person receiving both the OAS and the GIS, the maximum combined monthly benefit is $1 186.

Pillar 2: Québec Pension Plan

The Québec Pension Plan (QPP) was implemented in 1966. It is the result of the public's wish to obtain a more generous public pension plan.

The QPP provides for the payment of a retirement pension, a disability pension as well as benefits to survivors and orphans. It stipulates compulsory coverage of all workers and seeks to offer additional income to retirees age 65 or over. Under certain conditions, the pension may be applied for starting at age 60. The maximum QPP retirement pension corresponds to 25% of average career earnings, up to the year's maximum pensionable earnings (YMPE), i.e. $48 300 in 2011.

The maximum benefit for a person applying for the QPP pension at age 65 is $960 per month in 2011, i.e. $11 520 per year. Currently, 3.9 million workers contribute to the QPP while 1.4 million people receive a retirement pension.

Pillar 3: Private savings

The third pillar represents private savings and in particular includes supplemental pension plans (SPP), group or individual registered retirement savings plans (RRSP) and deferred profit-sharing plans (DPSP).

Private group pension plans cover roughly 2 million Quebecers. In addition, each year, about 1.1 million people contribute to an individual RRSP.

On top of the first two pillars, private savings enable Quebecers to maintain a standard of living at retirement that is comparable with that of the final years of their working life.

1.2 A system that satisfies expectations

The Canadian retirement income system, and consequently Québec's, is considered one of the most effective in the world. Many studies, in particular studies by the OECD and Mercer, a consultancy, confirm this.

By providing for the payment of a basic income, in addition to fostering the accumulation of assets, the retirement income system allows most Quebecers to maintain a standard of living at retirement similar to what they enjoyed at the end of their career.

Main conclusions of the Mercer and OECD studies

Melbourne Mercer Global Pension Index

In 2010, Mercer, a consultancy, published a study comparing the performance of retirement income systems in 14 countries. For this purpose, Mercer developed a global retirement index, the *Melbourne Mercer Global Pension Index*.

This index compares the retirement income systems of countries by considering three indicators, namely adequacy, long-term sustainability and integrity.

According to the study, the Canadian retirement income system ranks 5th among the 14 countries studied, in particular ahead of France, Germany, the United Kingdom and the United States. This rank places Canada in the category of countries with the most effective retirement income system.

Canada's Retirement-Income Provision: An International Perspective

In 2009, the OECD published a study comparing the retirement income systems of 12 OECD member countries, including Canada. The comparison was based on six indicators, namely coverage, level of income at retirement, financial viability and accessibility, economic efficiency, administrative efficiency and security.

The OECD analysis concludes by affirming that, compared to other member countries, Canada's retirement income system performs well:

- the poverty rate among older people is very low and the income of retirees is fairly comparable with that of the population as a whole;
- the system is very efficient and provides the entire population with a basic income;
- long-term projections show that Canada's retirement income system is financially more viable than those of many OECD member countries;
- the public plans provide less inducement for early retirement than those of other OECD member countries;
- the system is diversified (public plans, private plans and private savings), which offers security against many risks and uncertainties that can affect retirement income.

1.2.1 Public plans that provide a basic income for all Quebecers

Quebecers obtain their retirement income from a variety of public plans and programs such as the OASP, the GIS and the QPP. Each of these sources of income targets a specific group and plays a particular role.

Overall, Quebecers obtain almost 45% of their retirement income from these programs and plans that form pillars 1 and 2 of the system. Accordingly, they represent a very important source of retirement income.

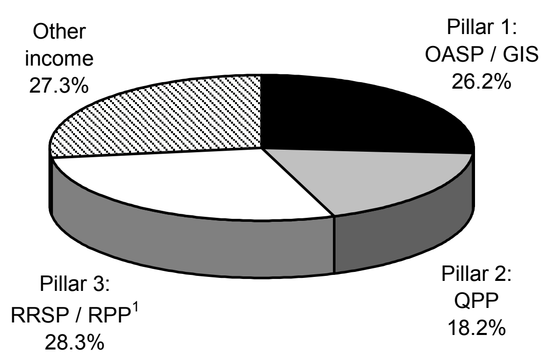
As shown by low-income rate of persons age 65 or over in Québec, these pillars have helped to substantially improve the situation of retired persons by guaranteeing stable income sufficient to maintain a basic standard of living.

— This is shown by the fact that since the late 1970s, the low-income rate of persons age 65 or over in Québec has fallen from 32.7% to 9.2%.

CHART 2

Composition of total income before tax of persons age 65 or over in Québec – 2008

(per cent)

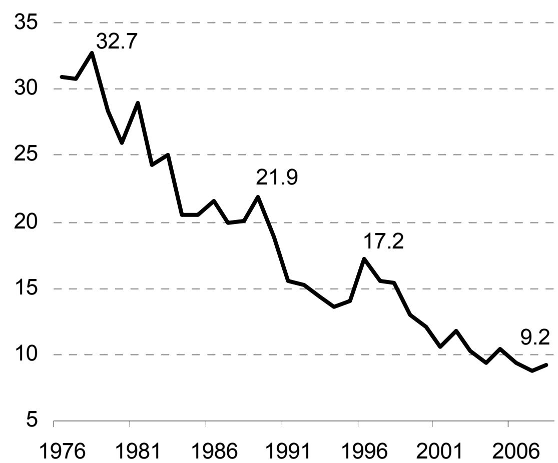


1 Registered pension plans (RPP) include pension plans subject to the Supplemental Pension Plans Act, those under federal jurisdiction as well as plans of Québec's public administration, the health and education sectors.

CHART 3

Low-income rate of persons age 65 or over in Québec according to the low-income cut-off[1] – 1976 to 2008

(per cent)



1 After tax.
Source: Statistics Canada.

Growth of Quebecers' assets

Over the last 40 years, Quebecers' retirement assets have grown substantially. Private savings (e.g.: supplemental pension plan and RRSPs), together with the Québec Pension Plan represented assets of $304 billion in 2008, compared with:

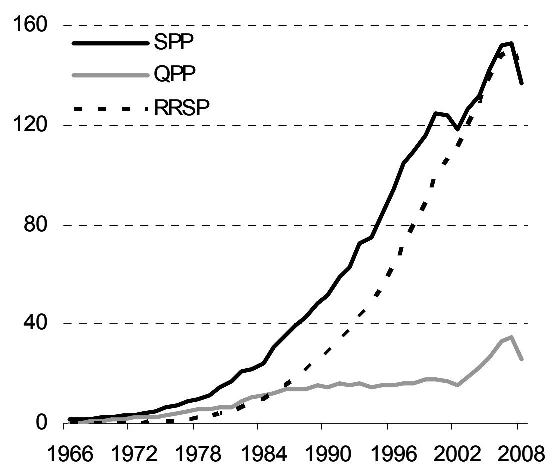
- $242 billion in 2000;
- $94 billion in 1990;
- $25 billion in 1980.

Moreover, retirement assets represent but a portion of the total assets an individual may accumulate over his working life and use at retirement to maintain his standard of living.

For example, real estate assets, such as a home or cottage, represented more than $375 billion in 2008, the largest pool of assets in Québec. While they are less liquid, they represent a significant patrimony on which retirees can count at the end of their working life.

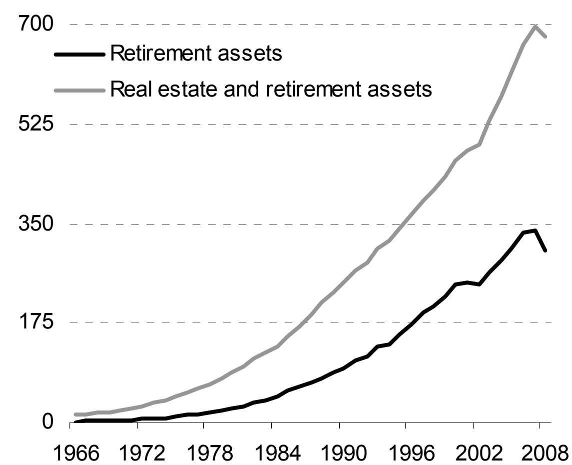
Total real estate and retirement assets amounted to $680 billion in 2008.

Growth of retirement assets in Québec – 1966 to 2008
(billions of dollars)



Source: Régie des rentes du Québec.

Growth of major assets in Québec – 1966 to 2008
(billions of dollars)



Sources: Régie des rentes du Québec and Statistics Canada.

1.2.2 A system that maintains the standard of living at retirement

The existing retirement income system enables Quebecers to receive adequate retirement income when they leave the labour market.

The average replacement level of earned income for Québec's population as a whole is slightly less than 70%,[1] i.e. the threshold that is generally targeted.

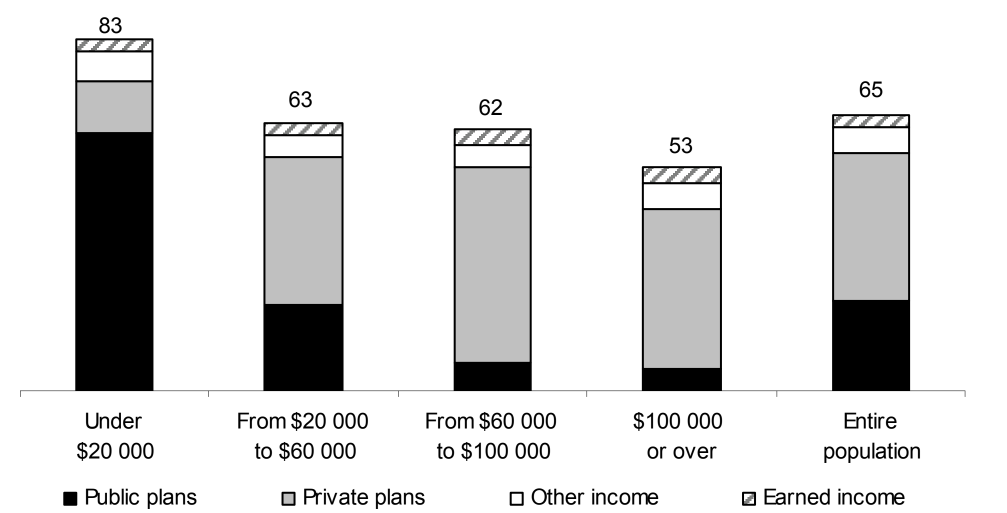
— Overall, the replacement rate for workers with pre-retirement income of less than $100 000 per year is close to the 70% threshold.

— In addition, workers whose income is less than $20 000 have a replacement rate that exceeds 80% thanks in particular to the level of coverage offered by public plans.

However, the average replacement rate provides only a partial portrait of the retirement savings situation of workers.

CHART 4

Average replacement of earned income at retirement in Québec
(as a percentage of earned income before retirement)



Source: Régie des rentes du Québec.

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1 The earned income replacement level is the ratio between the average income of the first three years after retirement and the average income of the last three years before retirement. Studies generally place the target replacement rate between 50% and 70%. Depending on the individual, the rate can vary with a variety of factors, including non-financial assets and lifestyle.

❑ Insufficient savings for some workers

Despite adequate average replacement rates, a certain proportion of retirees must come to terms with retirement income that is insufficient to maintain their standard of living. According to estimates by the Régie des rentes du Québec, the earned income replacement rate of between 30% and 40% of Québec workers will be less than 60%.

The situation is particularly worrisome for certain workers with earned income between $20 000 and $60 000.

— A relatively high proportion of workers in this income bracket have saved little for retirement.

— However, a low replacement rate for these workers means that they may be in financial difficulty at retirement, unlike higher-income households.

Accordingly, it appears important to bolster the incentive to save among these workers. However, the preferred approach must be flexible and take into account the various factors that may explain these relatively low earned income replacement rates, in particular:

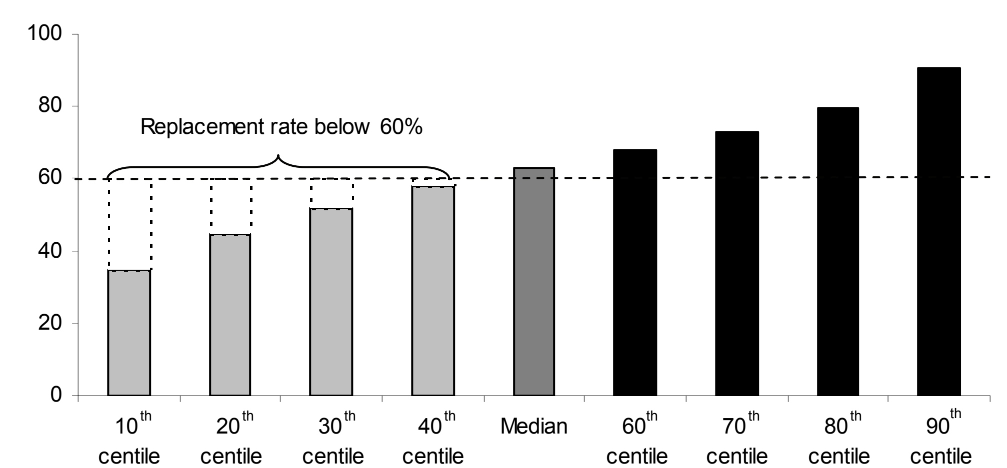
— early exit from the labour market;

— insufficient returns on savings;

— withdrawal of assets before retirement.

CHART 5

Distribution of replacement rates for workers with pre-retirement income between $20 000 and $60 000
(per cent)



Source: Régie des rentes du Québec.

2. A NEW CONTEXT THAT REQUIRES BOLSTERING OF QUÉBEC'S RETIREMENT INCOME SYSTEM

For the first time in its history, Québec will have to come to terms with an accelerated aging of its population because of improving life expectancy and a decline in the population of working age. That will have significant economic and financial consequences.

This demographic outlook will also raise important issues in terms of pension plan funding and workers' savings.

As a result of the aging of the population:

— retirement pensions will be paid over a longer period and to a greater number of retirees, leading to an increase in the cost of pension plans and of savings requirements;

— at the same time, the labour force will decline, leading to a reduction in the number of contributors and, consequently, the revenues of pension plans.

2.1 Accelerated aging of the population

Over the coming years, Québec's population will age at one of the fastest rates in the world. Consequently, the number of retirees will rise quickly while the number of people of working age will decline.

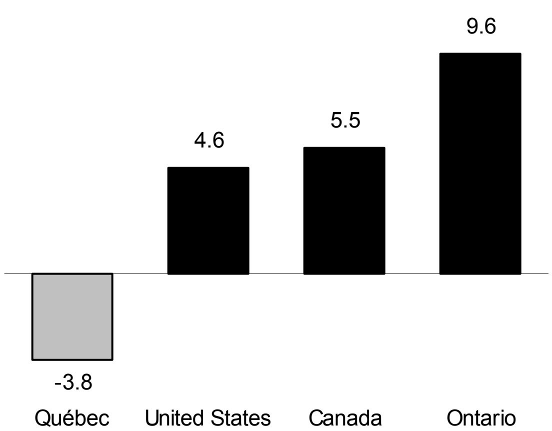
- In 2020, Québec will have 1.7 million people age 65 or over, three times more than in 1980, when there were 555 000.
- During the period 2013-2030, the working-age population in Québec will decline by 3.8% compared with an increase of 5.5% in Canada and 9.6% in Ontario. This comparison with our largest trading partners shows the magnitude of the challenge facing Québec.

Accordingly, in 2020, Québec will have only three people of working age for each retired person compared to eight in 1980.

The decline in the number of workers will thus limit contributions paid to pension plans while, at the same time, a larger number of retired persons will receive a retirement pension.

CHART 6

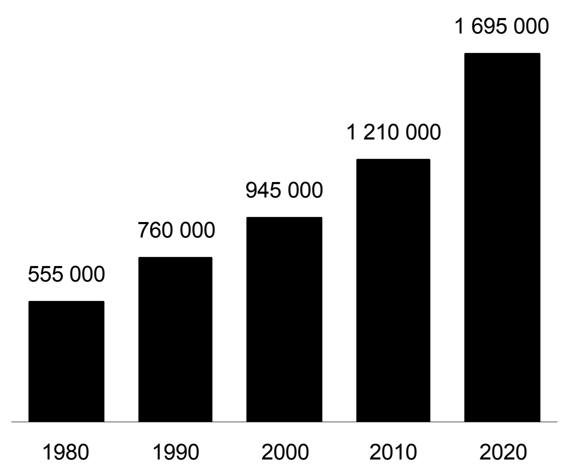
Change in the population age 15 to 64 – 2013 to 2030
(per cent)



Sources: Institut de la statistique du Québec, United States Census Bureau, Statistics Canada and Ontario Ministry of Finance.

CHART 7

Population age 65 or over in Québec – 1980 to 2020
(number)



Source: Institut de la statistique du Québec.

2.2 Longer retirement

Life expectancy at 65 is forecast to continue rising. Accordingly, Quebecers will spend a greater part of their life in retirement.

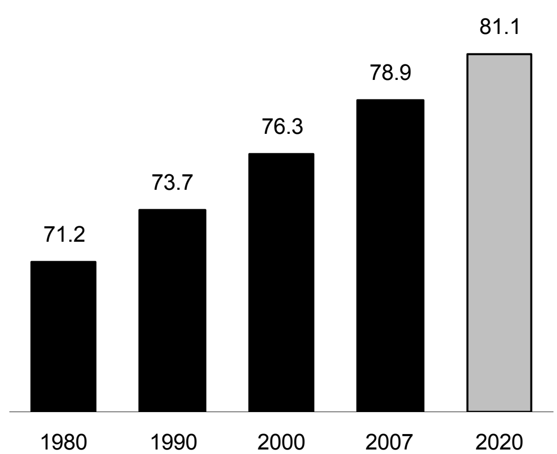
❑ Seven more years of retirement

- When the QPP was created in 1966, men received a pension for an average of 13 years.
- By way of comparison, in 2020, it is expected that men who retire at age 65 will receive a pension from the QPP for an average of 20 years, i.e. seven years more.

The structural changes stemming from the aging of the population and improving life expectancy will generate significant pressure on the cost of pension plans like the Québec Pension Plan. These plans will have to pay a guaranteed pension to a larger number of retirees over a longer period.

CHART 8

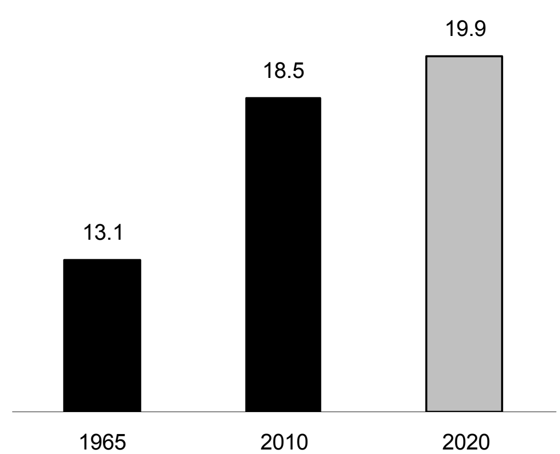
Life expectancy at birth for men in Québec – 1980 to 2020
(years)



Source: Institut de la statistique du Québec.

CHART 9

Life expectancy at age 65 for men in Québec – 1965 to 2020
(years)



Source: Régie des rentes du Québec.

❑ A context increasing pressure on savings

In addition to generating pressure on pension plans, the improving life expectancy means that Quebecers will have to save more to maintain their standard of living at retirement.

- A worker earning $40 000 at the end of his career and who wants to retire at age 65 and maintain his standard of living for 13 years must have saved $75 000 over 30 years,[2] i.e. an average of $2 500 per year. After 30 years, these savings will have grown to roughly $145 000.
- Should the same worker live to age 85, i.e. seven years more, he must save $95 000 over 30 years[2] to maintain his standard of living. This represents savings of $3 200 on average per year, i.e. $700 more. After 30 years, these savings will have grown to roughly $190 000.

This change in the demographic structure implies that Quebecers must save more to maintain the same standard of living at retirement.

In addition to longer life expectancy, financial returns have been lower in recent years, particularly because of the recent recession. By generating additional pressure on savings, low rates of return mean that to enjoy the same standard of living at retirement, Quebecers must save more.

The combined effect of the aging of the population, longer life expectancy at retirement and lower financial returns means that steps need to be taken now to make changes to our retirement income system. These changes will both secure its financial stability and further encourage savings.

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2 This amount takes into account retirement income from public plans (OASP, QPP).

3. ACT NOW TO SECURE AN ADEQUATE RETIREMENT INCOME FOR ALL GENERATIONS

Since its creation, the retirement income system in Québec has performed very well. It has offered an adequate earned income replacement level to the vast majority of Quebecers and thus has helped reduce poverty among the elderly.

In view of the demographic and economic outlook, the Québec government must ensure that the system continues to achieve its objectives. To do so, it is essential that:

- the stability of the QPP's financial situation be secured so that retirees can count on stable and predictable income;
- voluntary saving be encouraged so that workers have enough income to maintain their standard of living in retirement.

❑ Steps to bolster Québec's retirement income system

Steps need to be taken now to enable current and future retirees to enjoy a retirement income system that performs as well. Accordingly, the 2011-2012 Budget stipulates that:

- as of January 1, 2012, gradual adjustments will be made to the Québec Pension Plan;
- the government undertakes to allow the implementation of new voluntary retirement savings plans.

These steps are designed, on the one hand, to secure Quebecers' pensions by stabilizing the long-term funding of the Québec Pension Plan and bolster the incentive for experienced workers to remain at work.

On the other hand, they seek to increase voluntary household savings by setting up voluntary retirement savings plans. These plans will help simplify the decision to save and will seek to improve the returns on savings for all Quebecers.

3.1 Stabilize the financial situation of the Québec Pension Plan

For a number of years now, the QPP has faced increased financial pressure stemming chiefly from the aging of the population and the continuing improvement in life expectancy.

Accordingly, based on the actuarial report of the QPP as at December 31, 2009, the steady-state contribution rate, i.e. the rate needed to secure the plan's long-term financial stability, is currently 11.02%.

- With the current contribution rate of 9.9%, the benefits paid by the plan will exceed contributions as of 2013. In the short term, the Plan will then have to draw on its investment income and, as of 2023, tap its reserve to fund benefits for retirees.
- If there is no adjustment to the Plan, the reserve will be depleted in 2039. It is important to maintain a reserve since it generates investment income that helps maintain a lower contribution rate.

❑ Adjustments that will bolster the financial situation of the Plan

To maintain the Plan's reserve in the long run and thus bolster its financial situation, the Québec government favours a gradual approach that limits the impact on the economy, increases the incentive to work and encourages fairness among generations. Accordingly, the 2011-2012 Budget stipulates:

- a gradual rise over six years of the contribution rate from 9.9% to 10.80% in increments of 0.15 percentage point per year;
- adjustment of the amount of pension to encourage later retirement;
- implementation of an automatic contribution rate adjustment mechanism.

The steady-state contribution rate will continue to be reassessed every three years. To that effect, the Plan's next actuarial report is scheduled to be tabled in the fall of 2013.

In the event the steady-state contribution rate is revised downward, the government will suspend the increases in the contribution rate that prove to be no longer needed to restore the Plan's equilibrium. If the steady-state rate is adjusted upward, the government may then decide on alternative measures to maintain the Plan's financial stability.

Ultimately, these adjustments will restore the financial situation of the Plan. The difference of 1.12 percentage points between the steady-state contribution rate and the Plan contribution rate will be filled by:

- raising the contribution rate from 9.9% to 10.80%;
- reducing the steady-state contribution rate from 11.02% to 10.80%, in particular as a result of adjusting the pension, to encourage later retirement.

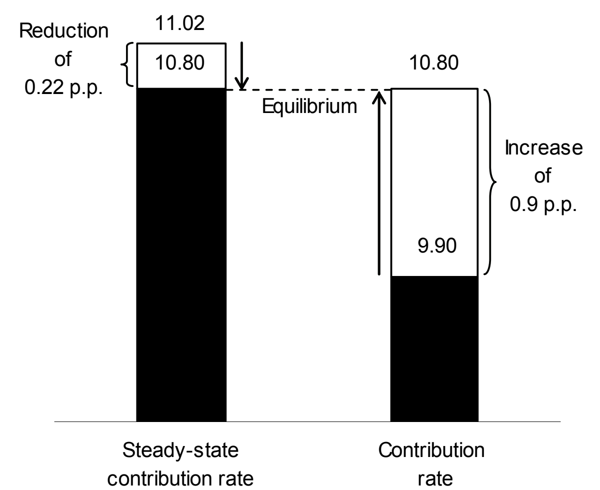
Accordingly, as of 2017, the Plan's contribution rate is forecast to be equivalent to its steady-state contribution rate,[3] which will stabilize its financial situation and ensure that a reserve is maintained in the long run.

- Thanks to the adjustments that will be made to the plan, it is expected that in 2039, i.e. when the reserve was expected to be depleted, it will amount to some $125 billion.

CHART 10

Comparison of the QPP contribution rate and the steady-state contribution rate

(per cent)

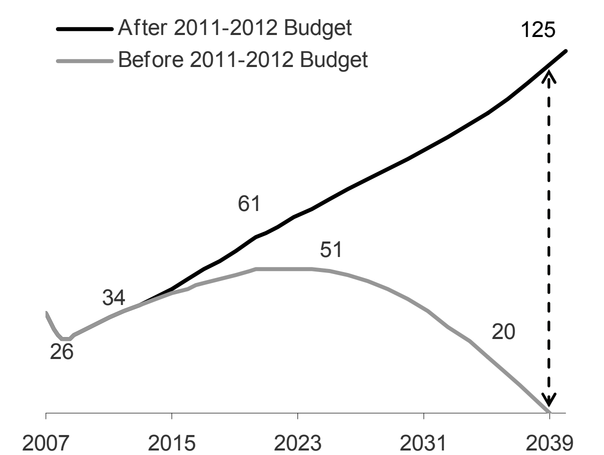


Source: Régie des rentes du Québec.

CHART 11

Impact of the measures of the 2011-2012 Budget on the QPP reserve

(billions of dollars)



Source: Régie des rentes du Québec.

3 The steady-state contribution rate will continue to change between 2011 and 2017. Any delay in applying the 10.80% contribution rate pushes the steady-state contribution rate up. On the other hand, favourable factors, such as returns above expectation, would cause this rate to decline.

Comparison of the financial situation of the Québec Pension Plan and the Canada Pension Plan

The Québec Pension Plan (QPP) and the Canada Pension Plan (CPP) are equivalent plans. They both operate similarly in terms of general objectives, structure, funding and benefit levels. However, the steady-state contribution rate of the QPP is now estimated at 11.02% while that of the CPP is 9.86%. This difference is attributable to a variety of factors.

The population is aging faster in Québec

Over the coming years, Québec's population will age at a much faster rate than that of the other provinces. This situation is attributable to three factors:

- a larger baby boom in Québec;
- the drop in fertility following the baby boom was more pronounced;
- our neighbours receive a larger proportion of immigrants.

Consequently, the number of retirees will rise more quickly than elsewhere in Canada while the number of people of working age will start to decline in 2014. The combined effect of aging and a decline in the number of workers will have a major impact on the funding of the QPP since there will be fewer people on the labour market to pay contributions and more retirees will receive a pension.

The general exemption has a greater impact on the QPP

In both plans, there is a general exemption of $3 500 on which no contribution is collected. This exemption reduces earnings for the purposes of calculating the contribution, without reducing the earnings on which benefits are calculated. Since average salaries are lower in Québec, the impact of the general exemption is proportionally greater on the QPP than the CPP.

The QPP is more generous for certain benefits

The eligibility conditions for a disability pension under the QPP are more flexible than those of the CPP. In addition, the QPP provides more generous benefits than the CPP for surviving spouse under age 65.

The necessity of stabilizing the financial situation of the QPP

Overall, the QPP is facing increased financial pressure stemming chiefly from the aging of the population, which is occurring faster in Québec than elsewhere in Canada.

That is why steps must be taken now to stabilize the QPP's financial situation so that Québec retirees can count on stable and predictable basic income that is comparable with those of other Canadians at retirement.

3.1.1 A gradual rise in the contribution rate

To restore the equilibrium of the QPP while limiting the impact on workers and businesses, the 2011-2012 Budget stipulates:

— that the Plan contribution rate will be raised gradually from 9.9% to 10.80% over six years in increments of 0.15 percentage point per year.

The contribution rate will be raised as of January 1 of each year, starting January 1, 2012 and continuing until January 1, 2017.

❑ A gradual increase that limits the impact on the economy

The QPP pension paid to retirees is funded evenly by employee and employer contributions. To avoid an excessive shock to the economy, the rate will be adjusted gradually, over six years. The total increase, from now until January 1, 2017, will be 0.45 percentage point for both employees and employers.

TABLE 1

Increases in the contribution rate announced in the 2011-2012 Budget
(per cent)

	Adjustment to the contribution rate	Contribution rate		
		Employee rate	Employer rate	Total
Current situation	—	**4.950**	**4.950**	**9.90**
January 1, 2012	+ 0.15	5.025	5.025	10.05
January 1, 2013[1]	+ 0.15	5.100	5.100	10.20
January 1, 2014	+ 0.15	5.175	5.175	10.35
January 1, 2015	+ 0.15	5.250	5.250	10.50
January 1, 2016[1]	+ 0.15	5.325	5.325	10.65
January 1, 2017	+ 0.15	5.400	5.400	10.80
ULTIMATELY	+ 0.90	5.400	5.400	10.80

1 An actuarial report on the QPP is scheduled to be tabled in the fall of 2013 and 2016.

❑ Impact on employees and employers

A rise of 0.15 percentage point in the contribution rate will cause the employee contribution to rise by:

- $0.33 per pay[4] for employment income of $15 000;
- $0.76 per pay[4] for employment income of $30 000;
- $1.29 per pay[4] for employment income of $48 300 or more.

TABLE 2

Impact of an increase in the QPP contribution rate of 0.15 percentage point according to an employee's income
(dollars)

Employment income	Annual increase			Increase per pay[1]	
	Employee	Employer	Total	Employee	Employer
15 000	8.63	8.63	17.25	0.33	0.33
20 000	12.38	12.38	24.75	0.48	0.48
30 000	19.88	19.88	39.75	0.76	0.76
35 000	23.63	23.63	47.25	0.91	0.91
40 000	27.38	27.38	54.75	1.05	1.05
48 300[2] or more	33.60	33.60	67.20	1.29	1.29

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.
1 Based on 26 pays per year.
2 Corresponds to the 2011 maximum pensionable earnings.

4 On the basis of 26 pays per year.

At the end of the six-year period, i.e. in 2017, the worker contribution will have risen by:

- $1.99 per pay[5] for employment income of $15 000;
- $4.59 per pay[5] for employment income of $30 000;
- $7.75 per pay[5] for employment income of $48 300 or more.

TABLE 3

Ultimate impact of the increase in the QPP contribution rate according to an employee's income
(dollars)

Employment income	Annual increase			Increase per pay[1]	
	Employee	Employer	Total	Employee	Employer
15 000	51.75	51.75	103.50	1.99	1.99
20 000	74.25	74.25	148.50	2.86	2.86
30 000	119.25	119.25	238.50	4.59	4.59
35 000	141.75	141.75	283.50	5.45	5.45
40 000	164.25	164.25	328.50	6.32	6.32
48 300[2] or more	201.60	201.60	403.20	7.75	7.75

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.
1 Based on 26 pays per year.
2 Corresponds to the 2011 maximum pensionable earnings.

For employees and employers, the contribution increase will total roughly $85 million each in 2012, i.e. an average of $0.80 per pay.

In 2017, the approximate impact will be $625 million each for an average of $5.80 per pay.

TABLE 4

Impact of the increase in the QPP contribution rate for employees and employers
(millions of dollars)

	2012	2013	2014	2015	2016	2017
Employees	85	175	280	385	500	625
Employers	85	175	280	385	500	625
TOTAL	**170**	**350**	**560**	**770**	**1 000**	**1 250**

5 On the basis of 26 pays per year.

3.1.2 Change to the adjustment factors to encourage later retirement

The QPP pension is generally paid as of age 65. However, it is possible to receive it starting at age 60 or to postpone its payment until age 70. The pension is then adjusted for each month between the 65th birthday and age at the first payment. It is currently:

- raised by 0.5% per month, when applied for after age 65;
- reduced by 0.5% per month, when applied for before age 65.

Like the adjustments made to the Canada Pension Plan designed to encourage experienced workers to stay in the labour market, the 2011-2012 Budget stipulates that:

- the monthly increase in the QPP pension applied for after age 65 will rise from 0.5% to 0.7% as of January 1, 2013;
- the monthly reduction in a pension applied for prior to age 65 will be raised, in proportion to the amount of the QPP pension, from 0.5% to 0.6% in the case of a maximum pension;
  - the adjustment will be phased in over three years beginning January 1, 2014;
  - in addition, the increase will be proportional to the amount of the pension to limit the impact on lower-income workers.

The objective of these adjustments is the same as those of the CPP, i.e. encourage workers to remain in the labour market longer. The adjustments to the CPP started January 1, 2011 and will end January 1, 2016. At that time, the adjustment factors that apply in the QPP will be similar to those that apply in the other provinces.

TABLE 5

Increase in maximum monthly adjustment factors
(per cent)

		As of January 1			
Age at first payment	**Currently**	**2013**	**2014**	**2015**	**2016**
Over age 65[1]	+ 0.50	+ 0.70	+ 0.70	+ 0.70	+ 0.70
Age 65	—	—	—	—	—
Under age 65[2]	– 0.50	– 0.50	– 0.53[3]	– 0.56[3]	– 0.60[3]

1 Maximum reached at age 70.
2 Possibility of receiving the QPP pension as of age 60.
3 According to the amount of the pension, the monthly adjustment factor varies between – 0.5% and the rate indicated.

Changes made to the Canada Pension Plan

The Canada Pension Plan (CPP), to which workers in the other provinces and territories contribute, is a pension plan equivalent to the Québec Pension Plan. Maintaining the equivalence of these plans is a key factor for encouraging worker mobility. It enables workers who have participated in both plans to receive the same benefits and claim their pensions as though they had always contributed to a single plan.

As with the QPP, an actuarial valuation of the CPP is carried out every three years. The federal, provincial and territorial Finance Ministers then undertake an examination of the CPP to determine if benefits or the contribution rate should be changed to maintain its financial stability.

Following the work completed in 2009, the Finance Ministers decided to make changes to the CPP. The objectives of these changes were in particular to facilitate the transition from work to retirement, eliminate disincentives to remaining in the labour market and improving fairness. To do so, it was stipulated that:

- the requirement to stop working before applying for a retirement pension will be eliminated;
- workers who receive a pension will be required to contribute until age 65 and, like the QPP, such workers will have the opportunity to enhance their pension;
- the adjustment factors of the pension (before and after age 65) will be increased to encourage workers to remain on the labour market longer;
- the number of low-earnings months excluded from the calculation of the pension will be increased.

These changes will be implemented gradually, over a period of six years beginning January 2011 and ending January 2016.

The changes announced to the QPP as part of the 2011-2012 Budget will ultimately maintain the equivalence of the pensions between the two plans except for the additional reduction applied to pensions applied for before age 65. Lower-income workers will be assessed a higher penalty under the CPP than under the QPP.

Changes to the CPP adjustment factors according to the year of entry into force

	Adjustment factors for a pension applied for	
Year	**before age 65**	**after age 65**
2011	– 0.50%	+ 0.57%
2012	– 0.52%	+ 0.64%
2013	– 0.54%	+ 0.70%
2014	– 0.56%	+ 0.70%
2015	– 0.58%	+ 0.70%
2016	– 0.60%	+ 0.70%

❑ Additional enhancement for retiring after age 65

For pensions applied for after age 65, the 2011-2012 Budget stipulates that as of January 1, 2013, the monthly increase will be enhanced and will rise from 0.5% to 0.7%, i.e. 8.4% per year.

Accordingly, a pension applied for at age 70 will be enhanced by a maximum of 42% compared with 30% currently.

— The maximum amount of a pension applied for at age 70 will reach $16 358 per year, an increase of $1 382 per year, or $115 per month.

In other words, a worker who decides to delay his retirement will receive a pension that may reach almost one and a half times the pension he would have received had he retired at age 65.

TABLE 6

Impact of the enhancement of the adjustment factor on late retirement pensions applied for after age 65 - full effect in 2013
(dollars)

Age at first payment	Current maximum pension	Maximum pension after the change	Impact of the change	
			Annual	Monthly
Age 70	14 976	16 358	+ 1 382	+ 115.20
Age 69	14 285	15 391	+ 1 106	+ 92.16
Age 68	13 594	14 423	+ 829	+ 69.12
Age 67	12 902	13 455	+ 553	+ 46.08
Age 66	12 211	12 488	+ 276	+ 23.04
Age 65	11 520	11 520	—	—

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.

As an illustration, a person who applies for a pension at age 70 would receive a pension increased by:

- $35.78 per month for career average employment income of $15 000;
- $71.55 per month for career average employment income of $30 000;
- $115.20 per month for career average employment income of $48 300 or more.

TABLE 7

Ultimate impact of the increase in the adjustment factor for a pension applied for at age 70
(dollars)

Career average employment income	Current pension	Pension after the change	Impact of the change	
			Annual	Monthly
15 000	4 651	5 080	+ 429	+ 35.78
20 000	6 201	6 774	+ 572	+ 47.70
30 000	9 302	10 160	+ 859	+ 71.55
40 000	12 402	13 547	+ 1 145	+ 95.40
48 300[1]	14 976	16 358	+ 1 382	+ 115.20

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.
1 Employment income equivalent to the 2011 maximum pensionable earnings.

❑ An adjustment to the pension before age 65 to foster labour market participation

With the improvement in life expectancy, the period during which Québec Pension Plan benefits are paid is longer and generates upward pressure on the contribution rate. The earlier the pension is applied for, i.e. on the 60th birthday, the more it contributes to lengthening the benefit period and accentuating pressure on the Plan.

To increase in the incentive to continue working beyond age 60 and mitigate the impact of early retirement on the QPP, the 2011-2012 Budget stipulates that:

— the monthly reduction rate for pensions applied for prior to age 65 will be raised by a maximum of 0.1 percentage point, rising from 0.5% to 0.6% in the case of a maximum pension;

— the increase in the reduction will be proportion to the amount of the pension to limit the impact on lower-income workers;

— the increase in the monthly reduction will be spread over three years in increments of a maximum of 0.03 percentage point for pensions applied for in 2014, a maximum of 0.06 percentage point for those applied for in 2015 and 0.1 point for those applied for in 2016.

Since the QPP pension represents a significant percentage of the retirement income of lower-income workers, the increase in the monthly reduction rate will be adjusted to limit its impact for such persons. For example, the monthly reduction rate for a pension applied for prior to age 65 will rise, ultimately, from 0.5% to:

— 0.525% for career average employment income of $12 075;

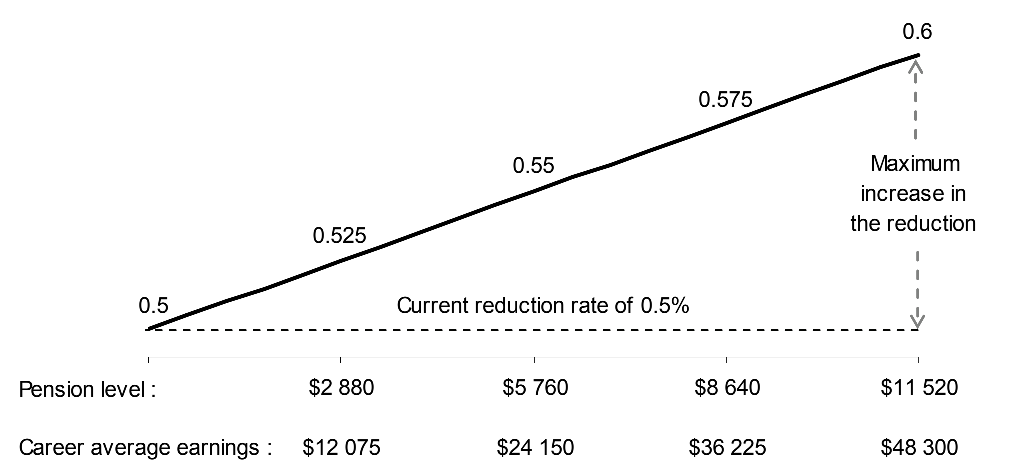
— 0.550% for career average employment income of $24 150;

— 0.575% for career average employment income of $36 225;

— 0.600% for career average employment income of $48 300 or more.

CHART 12

Monthly reduction rate for a pension applied for prior to age 65, according to the amount of pension – full effect in 2016
(per cent)



Note: The reduction rate is shown taking the 2011 parameters of the Québec Pension Plan into account. Career average earnings are in 2011 dollars.

Currently, the reduction is 6% per year, with a maximum of 30% at age 60. The maximum reduction rate applicable will be:

- in 2014, 6.36% per year, i.e. 31.8% at age 60;
- in 2015, 6.72% per year, i.e. 33.6% at age 60;
- in 2016, 7.2% per year, i.e. 36% at age 60.

The adjustment to the monthly reduction will have no impact on current retirees and its gradual implementation, starting in 2014, will leave workers enough time to adjust their retirement planning.

- The full impact for a pension applied for at 60 will apply to workers currently age 55 or under.

On average, a worker who applies for a pension at age 60 would receive a pension reduced by:

- $6.43 more per month, if it is applied for in 2014;
- $12.86 more per month, if it is applied for in 2015;
- $21.43 more per month, if it is applied for in 2016.

TABLE 8

Impact of the increase in the adjustment factor for a pension applied for at age 60 according to the year
(dollars)

Career average employment income	Current pension	2014		2015		2016 and following	
		Annual	Monthly	Annual	Monthly	Annual	Monthly
15 000	2 504	– 20	– 1.67	– 40	– 3.33	– 67	– 5.56
20 000	3 339	– 36	– 2.96	– 71	– 5.93	– 119	– 9.88
Average[1]	**4 919**	**– 77**	**– 6.43**	**– 154**	**– 12.86**	**– 257**	**– 21.43**
30 000	5 009	– 80	– 6.67	– 160	– 13.33	– 267	– 22.22
40 000	6 678	– 142	– 11.85	– 284	– 23.70	– 474	– 39.50
48 300[2]	8 064	– 207	– 17.28	– 415	– 34.56	– 691	– 57.60

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.

1 On average, the amount of pension paid by the QPP at age 60 corresponds to roughly 61% of the maximum pension, i.e. a career average income of roughly $29 500 in 2011 dollars.

2 Employment income equivalent to the 2011 QPP maximum pensionable earnings.

Illustration of the impact of adjustment factors on the QPP pension

Additional enhancement for late retirement

Anne-Marie hopes to retire at age 65. With career average earnings of $35 000 per year in 2011 dollars, she will receive an annual QPP pension of $8 348.

Should Anne-Marie decide to wait until age 70 to receive her QPP pension, it would increase by $2 504 per year, to $10 852.

However, following the adjustments announced in the 2011-2012 Budget:

- her retirement pension will be increased by roughly $200 more per additional year of work, after age 65;
- should she decide to wait until age 70, here annual pension would amount to $11 854, a gain of $1 002 for every year of retirement;

This adjustment will provide an even greater reward, by increasing the pension, for workers to opt for late retirement.

A greater adjustment before age 65 to encourage workers to remain at work

According to his career plan, Réjean expects to retire after 35 years of service. Since he started working at age 25, he will retire when he turns 60. At that age, he will be eligible for a reduced QPP pension because he wants to receive it before age 65.

Since he earned an average income of $35 000 per year in 2011 dollars, he will receive an annual pension of $5 843. By retiring at age 60, Réjean's annual pension is reduced by $2 505.

Consequently, had he waited until age 65 to retire, his pension would have been $8 348.

As a result of the adjustments stipulated in this budget:

- Réjean's annual pension will be $5 481 if he retires at age 60, $363 less than currently.
- should Réjean delay his retirement until age 65, his pension would rise by $573 for each additional year of work.

This adjustment will accordingly provide workers with more of an incentive to retire less early in order to receive a larger pension.

Annual QPP pension according to age of first payment[1] – before and after the 2011-2012 Budget
(dollars)

	60	61	62	63	64	65	66	67	68	69	70
Before the budget	5 843	6 344	6 845	7 346	7 847	8 348	8 849	9 350	9 850	10 351	10 852
After the budget[2]	5 481	6 054	6 627	7 201	7 774	8 348	9 049	9 750	10 451	11 153	11 854
DIFFERENCE	**– 363**	**– 290**	**– 218**	**– 145**	**– 73**	**—**	**+ 200**	**+ 400**	**+ 601**	**+ 801**	**+ 1 002**

Note: The impact is shown taking the 2011 parameters of the Québec Pension Plan into account.

1 For a worker whose career average earned income is $35 000, in 2011 dollars.

2 When the increase in the reduction rate is complete, i.e. in 2016.

3.1.3 Implementation of an automatic contribution rate adjustment mechanism

Maintaining the financial stability of the Québec Pension Plan is the very reason for the changes announced in this Budget. Accordingly, the 2011-2012 Budget stipulates, like the Canada Pension Plan, that an automatic adjustment mechanism will be put in place to secure such stability in the long run.

Accordingly, the mechanism will engage automatically following publication of the QPP actuarial report every three years. Where the steady-state contribution rate exceeds the contribution rate in effect by 0.1 percentage point:

— the contribution rate will automatically be increased by 0.1 percentage point per year as of the following January 1, until the steady-state contribution rate is reached or the publication of the next actuarial report.

However, this automatic mechanism will not apply before 2018 since a contribution adjustment is planned for the next six years. Also, the government may suspend the automatic application of the increase in the contribution rate by otherwise stipulating alternative measures to maintain the Plan's equilibrium.

TABLE 9

Illustration of the operation of the automatic adjustment mechanism
(per cent)

	Steady-state contribution rate	Contribution rate in effect	Difference	Contribution rate set for the following year
2018	10.80	10.80	—	10.80
2019[1]	**10.95**	**10.80**	**– 0.15**	**10.90**
2020	10.95	10.90	– 0.05	10.90
2021	10.95	10.90	– 0.05	10.90
2022[1]	**11.00**	**10.90**	**– 0.10**	**11.00**
2023	11.00	11.00	—	11.00

1 Assuming the QPP actuarial report is tabled in the fall of 2019 and 2022.

3.1.4 Bill to be tabled in the spring of 2011 to follow up on the measures contained in the budget

Over the coming weeks, the Minister of Finance will table an omnibus bill in the National Assembly containing provisions to implement the measures designed to restore the financial situation of the QPP. The bill will seek:

— a gradual rise over six years of the contribution rate from 9.9% to 10.80%;

— an adjustment of the amount of pension to encourage later retirement;

— implementation of an automatic contribution rate adjustment mechanism.

Furthermore, other adjustments to the QPP will be made public in the near future by the Minister of Employment and Social Solidarity further to the public consultation on the QPP held in 2009. Provisions will be made, in particular, to:

— eliminate the requirement to have stopped working in order to receive the QPP pension starting at age 60;

— increase the amount of the orphan pension.

3.2 Encourage saving by setting up voluntary retirement savings plans

A large number of Québec workers are not covered by an employer-sponsored pension plan. Accordingly, they must turn to complex individual savings products offered by financial institutions.

The complexity of these vehicles is often reflected in:

— a lower savings rate among workers who do not understand the products offered, or;

— lower returns for savers who often are unaware of the high management costs associated with certain investments.

Many workers then reach the end of their career with retirement savings substantially below what they anticipated and accordingly are incapable of maintaining a standard of living comparable with what they enjoyed during their final years of active participation in the labour market.

❑ Implementation of voluntary retirement savings plans

In this context, the federal and provincial governments have worked to determine ways to facilitate access to retirement savings, on the one hand, and to improve the returns on savings, on the other. As a result of this work, a framework has been developed presenting pooled registered pension plans.

In this regard, the Québec government is announcing, as part of the 2011-2012 Budget, that it is committed to:

— making the necessary amendments to Québec's legislative and regulatory frameworks to allow the development of new voluntary retirement savings plans (VRSP) in Québec based on the pooled registered pension plans framework;

— continuing to work with the other provinces to harmonize the operation of VRSPs with the pooled registered pension plans that will be offered elsewhere in Canada to foster labour mobility and their large-scale development;

— holding consultations to ensure that the application rules of VRSPs in Québec meet the needs of Quebecers.

3.2.1 Basic principles of VRSPs

The government's willingness to foster the implementation of VRSPs in Québec stems from the importance of improving the level of retirement savings, in particular for employees with no employer-sponsored pension plan and self-employed workers.

To achieve this objective, it is imperative that the foundations on which VRSPs rest ensure the participation of a large number of workers so that they benefit from low-cost pension plans that perform well.

Accordingly, VRSPs in Québec must:

- be accessible to all;
- make it easy for participants to make decisions by featuring simplified membership and operating terms and conditions;
- provide default investment options with low management costs to improve investment returns;
- spare the employer from the bulk of the administrative operations tied to the management of a pension plan.

In addition, employers that satisfy certain criteria that remain to be determined will be responsible for:

- choosing a VRSP that they will have to offer to their employees;
- deciding whether they contribute to the VRSP;
- automatically enrolling all their employees eligible for a VRSP who are not covered by a pension plan;
- withholding at source the amounts contributed by their employees.

Employees will be able to:

- on a voluntary basis, make a contribution net of tax automatically deducted from salary, into a pre-established investment vehicle or one of their choice;
- If need be, change the default provisions of the plan (choice of investment, contribution rate, etc.);
- if they do not wish to participate, opt out from the plan by notifying their employer in accordance with the details stipulated to that effect.

❑ A simple and flexible plan accessible to all

Simple and easy to access, VRSPs will be accessible to every citizen age 18 or over whether they are:

- employees;
- self-employed workers;
- savers.

For individuals, VRSPs will have a set of default provisions that will simplify the decision-making process.

- The default provisions will cover in particular contribution rates and investment choices.
- Participants will always have the option of changing the provisions of the plan to adapt it to their needs.

In addition, like RRSPs, contributions to a VRSP may be deducted from income and the amounts accumulated in the plan will not be taxed as long as they are not withdrawn. VRSPs will also make it easy to transfer assets from one plan to another where, for example, a worker decides to change jobs.

Businesses will be spared from the administrative operations tied to the management of a pension plan.

- VRSPs will be capital accumulation plans administered by third parties, such as financial institutions.
- At the administrative level, employers will only have to choose a plan and remit contributions to the VRSP administrator.

❑ A plan that seeks to improve return on investment

One of the main reasons for implementing VRSPs is to reduce management expenses by achieving economies of scale. To do so:

- each establishment authorized to offer VRSPs will have to offer default investment options to foster the accumulation of a critical mass of assets and thus reduce management expenses;
- oversight will be put in place regarding the level of management expenses, investment policies offered and minimum information to be supplied to participants;
- the law will foster better disclosure of information to participants, in particular regarding management expenses.

Lower management expenses will be reflected in higher net returns on investment and greater accumulation of retirement assets.

For example, a worker who saves $5 000 annually for 30 years and is charged management expenses of 2% on a gross return or 5% could save over 30 years:

— $20 236 if management expenses are lowered by 0.5 percentage point;

— $42 548 if management expenses are lowered by 1.0 percentage point;

— $67 158 if management expenses are lowered by 1.5 percentage points.

TABLE 10

Retirement savings gains arising from lower management expenses[1] – over a period of 30 years
(dollars)

	Gross value of the investment	Management expenses	Value of the investment	Gain for the saver	
				($)	(%)
Base situation	332 194	– 94 317	237 877		
Gain stemming from lower management expenses					
Reduction of 0.5 p.p.	332 194	– 74 081	258 113	**+ 20 236**	**+ 8.5**
Reduction of 1.0 p.p.	332 194	– 51 770	280 425	**+ 42 548**	**+ 17.9**
Reduction of 1.5 p.p.	332 194	– 27 159	305 035	**+ 67 158**	**+ 28.2**

1 It is assumed that the investments earn a return of 5% per year, reduced by management expenses of 2%. The net rate of return is 3%.

❑ A plan that will increase retirement coverage

To guarantee greater retirement coverage, employers that currently do not offer a pension plan and that satisfy certain criteria that remain to be determined will have to offer a VRSP to their employees. In this case, they may:

— automatically enrol their employees in the VRSP and allow them to opt out if they so wish; or

— require their employees to participate in a VRSP, where they contribute to the plan, provided an agreement is reached with the employees.

Employers will not be required to contribute to a VRSP. They will, however, have to make source deductions of the contributions of employees who wish to participate.

Since VRSPs will be administered entirely by third parties such as financial institutions, the administrative burden on participating employers will be considerably reduced. In addition, employer contributions will be exempt from payroll taxes. As a result of the features of this type of plan, they will be a more attractive vehicle for employers.

TABLE 11

Illustration of the responsibilities, options and advantages for the employer and employee related to the implementation of a VRSP

	Employer that currently does not offer a pension plan	Eligible employee
Responsibilities	– Choose a VRSP for its employees – Present the VRSP to its employees and describe the provisions of the plan – Automatically enrol eligible employees – Make source withholdings of employee contributions and remit them to the administrator	– Send the necessary personal information to the plan administrator – If he does not wish to participate, exercise his right to opt-out from the VRSP
Options	– If it wishes, make contributions to the VRSP for its employees – If it contributes, the plan can be made compulsory, subject to an agreement with the employees	– If need be, change the default provisions (choice of investment, contribution rate, etc.) – Make additional voluntary contributions
Advantages	– Exemption from the bulk of the administrative duties related to the management of the VRSP – Makes employment more attractive and fosters employee retention – Employer contributions are deductible from taxable income and are not subject to payroll taxes	– Participates in a low-cost pension plan – Simplifies the decision-making process – Contributions are deducted from pay net of tax and are taxed only upon withdrawal – Participation can continue even if the relation with the employer is broken – Possibility of transferring assets from one plan to another

3.2.2 Ongoing work with the other provinces and the federal government

A high degree of harmonization of legislation at the federal and provincial levels is desirable for these new pension plans to grow in size and thus significantly reduce management expenses.

Greater harmonization will simplify the transfer of assets, thus allowing workers to contribute to their pension plan regardless of their employment status and province of residence. That will foster labour mobility.

To implement VRSPs, the federal government must first amend its tax laws to:

- no longer require the existence of an employee-employer relation to contribute to a private pension plan;
- withdraw the requirement of a minimum employer contribution in a private pension plan in which the employees participate.

At the last meeting of Finance Ministers, in December 2010, the federal government undertook to amend its legislation. In this regard, the Québec government hopes the federal government will announce the changes necessary for the implementation of VRSPs in its March 22, 2011 budget.

Over the coming months, the Québec government will continue to work with the federal government and the other provinces to make VRSPs available as soon as possible.

3.2.3 Consultations on application details in Québec

Many points still need to be clarified regarding the terms and conditions of VRSPs. At the federal-provincial level, an initial series of consultations began in February and will end in April. Once these consultations are over, a framework will be prepared jointly by the provinces and the federal government.

Subsequently, the Québec government will hold consultations to specify the features of VRSPs so that they meet the needs of Quebecers. These consultations will cover a number of themes, in particular:

- choice of investments;
- locking-in of contributions;
- liquidation of savings at retirement;
- the fiduciary role of VRSP administrators;
- types of VRSP participation;
- the default contribution rate;
- harmonization of terms and conditions among the provinces;
- the possibility of transferring accumulated funds between plans.

Expanding the Canada Pension Plan and the Québec Pension Plan

At the June 2010 meeting of Finance Ministers, it was agreed to examine reform options that would foster retirement savings in Canada, including a modest, gradual and fully-funded enhancement of the Canada Pension Plan (CPP) and the Québec Pension Plan (QPP).

Existing CPP and QPP retirement pensions

The CPP and QPP retirement benefits are calculated based on a replacement rate and a cap on pensionable earnings.

- The replacement rate of the CPP and QPP is 25%. The pension paid by these plans is thus equivalent to 25% of average career earnings.
- The earnings used to calculate the pension are those not currently in excess of $48 300, i.e. year's maximum pensionable earnings (YMPE).
- The YMPE is raised each year to reflect the rise in average pay.

Possible options

The possible expansion of the CPP and QPP could involve either an increase in the replacement rate, an increase in the cap on pensionable earnings or both. Accordingly, three options can be considered:

- a modest increase in the replacement rate beyond the existing 25% rate;
  - This option would imply higher benefits for all workers.
- an increase in the cap on pensionable earnings, currently $48 300 in 2011;
  - Raising the cap would increase the pension only of those workers earning more than the YMPE, covering roughly 30% of workers in Québec.
- a combined increase in the replacement rate and the cap on pensionable earnings;
  - This scenario would imply higher benefits for all workers, including those with earnings above the YMPE.

The impact on the economy must be taken into account

With the economic recovery still fragile, the proposed changes to the retirement income system will have to take into account the impact they may have on the economy. Some of the scenarios analyzed could have a significant impact on households and businesses. For instance:

- a rise in the income replacement rate from 25% to 35% and in YMPE from $48 300 to roughly $70 000 would imply for Québec an increase in contributions of about $4 billion per year;
- a rise in the income replacement rate from 25% to 50%, as some stakeholders are proposing, would imply for Québec an increase in contributions of up to $6 billion per year.

In addition to representing a substantial impact, the proposed expansion would be fully funded, implying that workers would not reap the full benefit until after 40 years.

Québec's priorities for improving the retirement income system

Québec's priorities concerning the retirement income system are:

- to secure the financial stability of the QPP in the long run by restoring balance between the plan's contribution rate and its steady-state contribution rate;
- to encourage saving by establishing voluntary retirement savings plans.