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Cutting CPP Contributions: Let's pop this trial balloon*

With summer here, there is plenty of hot air across the country – including certain social policy ideas circulating in Ottawa.

As widely advertised, Prime Minister Stephen Harper's government's fall agenda will include measures aimed at fixing the so-called fiscal imbalance between Ottawa and the provinces. One of the possible measures is an eye-catching trial balloon: reducing Canada Pension Plan (CPP) contributions from workers and employers by paying some of the federal government's surplus money directly into the CPP.[1]

This balloon should be popped – it puts our pensions at risk.

Since 1998, the CPP has had an investment fund and board of directors, operated at arm's length from governments, charged with investing program contributions in a diversified portfolio of domestic and international public and private equities. Contribution rates shared equally between employees and employers are set at a combined 'steady state' rate of 9.9 percent of contributory earnings, in effect since 2003.[2] Virtually all observers, including the financial community and conservative think tanks, accept the CPP is actuarially sound and does not require any further changes to its financing for several decades.[3]

The Harper government's trail balloon of shifting part of the federal supplies into the CPP fund is a danger because, as one observer notes, this "transaction would breach what has up to now been a solid wall between the CPP and the regular federal budget. Create a hole through which money repeatedly flows between the two, and the odds are high that one day the flow will go the other way."[4]

This proposal also threatens the arm's length relationship carefully established to ensure not only the integrity of the board of directors but also to enhance the long-term financial performance of the investments. A concern not to be

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lightly taken is that this proposal could politicize the selection process of future directors and, in turn, confuse the mandate and mission of the investment board.

A further risk, potentially, is the exclusion of the Plan's core participants – the millions of Canadians who contribute to and receive benefits from the CPP – from this reform process.

Still another hazard is that this proposal unduly narrows policy thinking and public considerations of pension reforms. It certainly adds little to our need as an aging population to reflect seriously upon the future role of various components of the retirement income system.

In reality, reducing CPP contributions does nothing to improve provincial financial balances. Even if pension contributions could be reduced, the provinces have no way to take up this vacated tax room, since they do not have a payroll tax equivalent to CPP contributions. The proposal also would do nothing for controlling the federal government's own spending, because CPP contributions and benefits are not part of Ottawa's revenue and expenditure budgets, but rather financed by earnings-related premiums.

This proposal was not presented in the last general federal election. It was not part of the Conservative party's election campaign book. There is no democratic mandate for a minority government to undertake a bold policy change never discussed in an election, which may have long-term ramifications for all Canadian workers.

It was only in the May 2006 Budget that the Harper government proposed the scheme of allocating a portion of unplanned federal surpluses at year-end (in excess of $3 billion a year) to the existing investment funds of the Canada Pension Plan and the Quebec Pension Plan. How frequent are these unplanned federal surpluses expected to be occurring over time? Should we be *planning* policy changes based on *unplanned* surpluses in the future?

Public discussion must involve not just the provinces and territories but also working Canadians of all ages, at the next general election. CPP spending already is focused, transparent and accountable, so how will this move clarify responsibilities? On the contrary, the move would blur roles and weaken accountabilities for this essential retirement income program. Why not allocate federal surpluses to enhancing the federal program of Guaranteed Income Supplement for low-income seniors?

Federal Finance Department officials advance a case for reducing CPP contribution rates in terms of improving the intergenerational fairness between current young workers and retired workers as regards their rate of return of benefits to contributions. Not surprisingly, Finance's only option for improving the intergenerational equity of the Plan is by lowering contributions. Conspicuously missing from Finance's analysis is the corresponding strategy of raising future benefits as existing investment funds of the CPP (and QPP) would actuarially support.

If Canadians are "overtaxed" at the federal level, as the Harper government claims, much more straightforward alternatives are readily available. Reducing federal income tax is one obvious option. Another is lowering Employment Insurance premiums further. Such moves like these will certainly enhance budget transparency.

Why go to the bother of allocating a portion of large federal surpluses to the CPP and QPP and then, in turn, lower contributions for employers and employees, if tax relief is the objective? Unless, perhaps, a longer-term aim is to limit the role of public retirement income supports in order to promote private sector investment schemes.

The last round of major reforms to the CPP in 1997 came after extensive public consultations as well as academic and expert discussions across the country.[5] Such an approach, at the least, should precede any future changes. Meetings between the Minister of Finance and his provincial and territorial counterparts are far too narrow and closed a process for consideration of reforms to this major income security program for Canadians. This process of social policy by stealth reduces the public's role to a passive and insignificant one in policy deliberation.[6]

The federal and provincial governments are joint stewards of the CPP. Major changes to the CPP require agreement of two-thirds of the provinces with two-thirds of the population, as well as the approval of Parliament.

We can therefore hope that provinces pop this ill-advised hot-air social policy balloon before it floats away from the public.

Michael J. Prince

Michael J. Prince is Lansdowne Professor of Social Policy, Faculty of Human and Social Development, University of Victoria.

Endnotes

1. Department of Finance Canada. (2006). *The Budget Plan.* Ottawa: Her Majesty the Queen in Right of Canada, pp. 56-57. See also, Laghi, B. and Chase, S., "Ottawa eyes cut in CPP premiums." *The Globe and Mail,* Toronto: June 21, 2006, pp. A1 and A7.

2. Prince, M. (2003). "Taking Stock: Governance Practices and Portfolio Performance of the Canada Pension Plan Investment Board," in G. B. Doern, ed., *How Ottawa Spends 2003-2004: Regime Change and Policy Shift.* Toronto: Oxford University Press, pp. 134-154.

3. Robson, W. (2006). *Many Happy Returns: Guarding the Integrity of the CPP Investment Board.* Toronto: C.D. Howe Institute.

4. Robson, p. 4.

5. See, for example, Lam, N., J. Cutt and M. Prince. (1997). "The Canada Pension Plan: Retrospect and Prospect," in K. Banting and R. Boadway, eds, *Reform of the Retirement Income System.* Kingston, Ontario: Queen's University, School of Policy Studies, pp. 105-134.

6. Prince, M. (1999). "From Health and Welfare to Stealth and Farewell: Federal Social Policy," in L. Pal, ed., *How Ottawa Spends 1999-2000: Shape Shifting: Canadian Governance Toward the 21st Century.* Toronto: Oxford University, pp. 151-196.

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1600 Scott Street, Suite 620
Ottawa, Ontario, Canada
K1Y 4N7

Phone: (613) 729-3340
Fax: (613) 729-3896
E-mail: caledon@caledoninst.org
Website: *www.caledoninst.org*