OFFICE OF THE
PARLIAMENTARY BUDGET OFFICER

BUREAU DU
DIRECTEUR PARLEMENTAIRE DU BUDGET

CANADA

Cost Estimate of Bill C-215

Ottawa, Canada
April 20, 2012
www.parl.gc.ca/pbo-dpb

The *Parliament of Canada Act* mandates the Parliamentary Budget Officer (PBO) to provide an estimate of the financial cost of any proposal that relates to a matter over which Parliament has jurisdiction when requested to do so by a member or by a committee.

This report fulfills a request from the Standing Committee on Finance (FINA) with respect to Bill C-215: A*n Act to amend the Canadian Forces Superannuation Act and the Royal Canadian Mounted Police Superannuation Act (deletion of deduction from annuity).*

Prepared by: Jessica Strauss*

* The author would like to thank the Office of the Superintendent of Financial Institutions, Office of the Chief Actuary for their support, analysis and data as well as Peter Weltman for helpful comments. Mercer Canada was contracted by the PBO to provide actuarial analysis in support of this note. For further information please contact Jessica Strauss (jessica.strauss@parl.gc.ca)

Key Points

- Bill C-215 proposes to remove the deduction for the Canada Pension Plan (CPP) that occurs at age 65 for pension benefits received by certain annuitants of the *Canadian Forces Superannuation Act and the Royal Canadian Mounted Police Superannuation Act.*

    - Under the current provisions of the plan, pensions are reduced by 19.0% on average at time of integration.

- The Bill is projected to affect all 93,000 contributors, 85,000 pensioners, 16,000 disabled pensioners who participate in the plan with the exception of those who started receiving benefits prior to 1966, the inaugural eligibility year for receipt of benefits within the CPP and Quebec Pension Plan (QPP). Survivors are not affected because their benefits are not integrated with the Plan.

- The Government of Canada has provided PBO with a cost estimate of the Bill in the plan year 2012-13, assuming that the removal of the integration provision would apply as at March 31, 2012.

- It is expected that the removal of the integration provision would apply to all contributors, healthy pensioners and disabled pensioners. Moreover, it was assumed that Bill C-215 would have no retroactive impact for pensions in payment. PBO has reviewed the estimate together with an external firm and has found the estimate to be reasonable. If passed:

    - Bill C-215 is projected to add up to $138 million or an additional 2.03% of pensionable payroll in the plan year 2013 in pensionable contributions;

    - Further, the Bill is projected to add approximately $8.6 billion in accrued pension liability.

Introduction

The Standing Committee on Finance has requested a cost estimate of introducing amendments to the *Canadian Forces Superannuation Act* (CFSA) and the *Royal Canadian Mounted Police Superannuation Act* (RCMPSA) that would remove the deduction for the Canada Pension Plan (CPP) that occurs at age 65 for pension benefits.

The proposed amendments to the respective *Superannuation Acts* would result in significant impacts to the Government of Canada's Fiscal Framework and specifically to the respective superannuation plans.[1] The deletion of the provision to adjust the superannuation benefit by the amount of the CPP benefit will add two types of relevant costs:

A) Static Costs: These costs pertain to changes contained in the Bill assuming that the behaviour of all individuals participating in the system is unchanged and consist of costs incurred by accrued liability and increased annual contributions:

1) ***Accrued Liability***. These costs concern additional funds that may be required to be deposited into the relevant plans in order to meet increased future benefits.
2) ***Annual Contributions***. These costs concern the increased annual employer contribution required to meet the terms of the amended plan and are calculated on an annual basis.

B) Dynamic Costs: These costs pertain to changes contained in the Bill including impacts arising from behavioural responses of participants in the system. Since the proposed changes to the Superannuation Acts would be permanent, it is not unreasonable to expect a behavioural response. However, estimating the size and cost impact of these responses is difficult, and beyond the scope of the PBO's analysis.

[1] The pension obligation is split between the Pension Fund and the Superannuation Account as follows: 18.60% due to the Pension Fund and 81.82% to the Superannuation Account.

Methodology

PBO drew from reports provided by the Office of the Superintendent of Financial Institutions (OSFI) to construct the estimated costs of Bill C-215.[2]

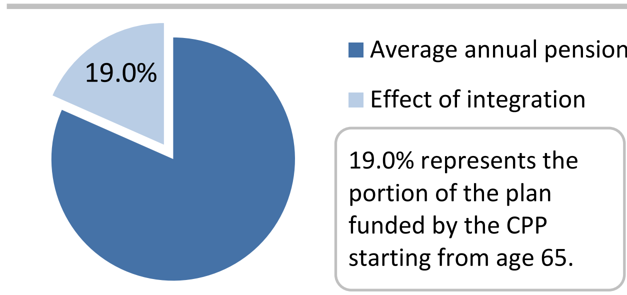
In addition, the PBO engaged Mercer Canada (Mercer) to provide actuarial analysis to support the review of materials and the reasonableness of the cost estimates of the proposed changes that were prepared by OSFI.[3]

Population data and associated pensionable earnings were gathered from the Canadian Forces and from the RCMP to determine the populations for contributors as well as for pensioners and survivors to each plan.

OSFI reviewed the population statistics for contributors, retirement pensioners and disability pensioners and further examined pensionable earnings and annual pension pay. As seen in Table 1, OSFI determined that under the current provisions of the plan, pensions are reduced by 19% on average for both the Canadian Forces and the RCMP at the time of integration.[4]

Table 1

The effect of integration on annual pensions



Source: OSFI Report. Accessed March 2012.

[2] Public Safety delivered reports furnished by OSFI, dated 10 November 2011 (Canadian Forces) and 20 December 2011 (RCMP). Accessed March 2012. Included as Annex A.

[3] Mercer: Review of the Cost Estimates of Removing the Integration Provision of the CFSA and RCMPSA, as proposed under Bill C-215, February 17, 2012. Accessed March 2012. Included as Annex B.

[4] The valuation reflects the reduction in the applicable Canada Pension Plan coordination factor that was reduced from 0.7% to 0.625% over five years (ultimate level first attained in 2012). Data for both the Canadian Forces and for the RCMP was projected to March 31, 2012.

OSFI Results

The Canadian Forces Superannuation plan (CFSA) and the Royal Canadian Mounted Police Superannuation plan (RCMPSA) were each deemed amended to remove the integration provision, for the purpose of examining this Bill.

As seen in Table 2, OSFI determined that the accrued liability, projected as of 31 March 2012, would increase by $6.5 billion for the CFSA and by $2.1 billion for the RCMPSA as a result of removing the integration provision.

Table 2

Accrued liability as of 31 March 2012

($ billions, projected)

CFSA	Contributors	Pensioners & Survivors	Combined
Current Plan	19.50	38.50	58.00
Proposed Bill C-215	21.00	43.60	64.60
Net Change	**1.50**	**5.10**	**6.60**
RCMPSA			
Current Plan	6.60	10.60	17.20
Proposed Bill C-215	7.20	12.00	19.20
Net Change	**0.60**	**1.40**	**2.00**
TOTAL	**2.10**	**6.50**	**8.60**

Source: OSFI Calculations. Accessed March 2012.

As seen in Table 3, OSFI further determined that annual contributions are projected to increase by $93 million for the CFSA and by $45 million for the RCMPSA for the plan year 2013 in each case.[5]

Table 3

Annual contributions for the plan year 2013

($ millions, projected)

CFSA		% of pensionable payroll
Current Plan	$ 1,066	23.10%
Proposed Bill C-215	$ 1,159	25.10%
Net Change	**$ 93**	**2.00%**
RCMPSA		
Current Plan	$ 442	20.60%
Proposed Bill C-215	$ 487	22.70%
Net Change	**$ 45**	**2.10%**
TOTAL	**$ 138**	**2.03%**

Source: OSFI Calculations. Accessed March 2012.

[5] Figures provided in Tables 2 and 3 reflect total increases in actuarial liabilities and in the current service cost. In the event that costs are to be shared, it will be the employer's decision to split these increases between the employer and participants to the plan.

External Review

Mercer assessed the reasonableness of the cost estimates prepared by OSFI. For that purpose, Mercer reviewed and confirmed the following:

- The approach used by OSFI regarding the plan change, membership data and assumptions used for the purpose of the estimates;
- The process used by OSFI to validate the cost estimates and the order of magnitude; and,
- No significant events occurred since the last statutory valuations which would affect the result of this analysis.

Mercer's validation of the results is summarized here:

- For recipients of benefits which do not currently integrate with the CPP, there is no impact as a result of this proposed Bill. This category includes contingency benefits for healthy and disabled pensioners and benefits for widows and children as well as for pensioners who retired prior to 1966, the year after the CPP and QPP were introduced;
- The increase in liability is consistent with the average integration level;
- The per cent increase in the liability and the current service cost for the affected categories of members is similar for both plans, which is expected given the similarities in plan provisions; and,
- Following an independent analysis of average age of contributors, their average age upon retirement, and their projected pension with and without integration at age 65, the results of these tests are similar to the cost increases determined by OSFI.

In conclusion and based on the findings listed above, Mercer affirms that the increases in liabilities and current service costs presented by OSFI are reasonable. They noted however, that given the changes in economic conditions since the last statutory valuations, a sensitivity analysis of the cost estimates to the main assumptions would be useful.

ANNEX A

- OSFI RCMP REPORT (DECEMBER 2011)
- OSFI CF REPORT (NOVEMBER 2011)

Office of the Chief Actuary
Office of the Superintendent of Financial Institutions

Bureau de l'Actuaire en chef
Bureau du surintendant des institutions financières

20 December 2011

Mr. Peter Murphy
Senior Policy Analyst
National Compensation Policy Centre
Royal Canadian Mounted Police
73 Leikin
Ottawa, Ontario
K1A 0R2

Dear Mr. Murphy:

Subject: Royal Canadian Mounted Police Ministerial Query – Bill C-215 (Removing the CPP integration provision from the RCMP pension plan)

This letter discusses the actuarial methodology used to estimate the cost of removing the integration provision from the *Royal Canadian Mounted Police Superannuation Act* (RCMPSA) and presents its results.

Main Findings

If the RCMP pension plan was amended to remove the integration provision, the current service cost of the plan would increase by 2.1% of pensionable payroll, from 20.6% to 22.7% for the plan year 2013 and the accrued liability as at 31 March 2012 would increase by $2.0 billion, from $17.2 to $19.2 billion.

Valuation Basis

This estimate is based on the statutory valuation data as at 31 March 2008, which is the most recent published statutory actuarial report on the Royal Canadian Mounted Police pension plan. The economic and demographic assumptions used are also those from the actuarial report as at 31 March 2008.

The population data as at 31 March 2008 were projected to 31 March 2012. As at 31 March 2008, there were 21,212 contributors and the average pensionable earnings were $78,434. The number of retirement pensioners was 11,485 with an average annual pension of $38,809, and the number of disability pensioners was 1,505 with an average annual pension of $29,454. Under the current provisions of the plan, pensions are reduced by on average 19% at time of integration.

The Canada Pension Plan coordination factor for this pension plan is 0.625% per year of service.

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Canada

Valuation Methodology

For valuation purposes, the projected accrued benefit actuarial cost method was used to determine the current service cost and actuarial liability.

The actuarial liability with respect to contributors corresponds to the value, discounted in accordance with the actuarial assumptions, of all future payable benefits accrued as at the valuation date in respect of all accrued service at that date. For pensioners and survivors, the actuarial liability corresponds to the value, discounted in accordance with the actuarial assumptions, of future payable benefits.

The current service cost computed in respect of a given year is the sum of the value, discounted in accordance with the actuarial assumptions, of all future payable benefits considered to accrue in respect of that year's service. The current service cost under the RCMPSA is borne by the members and the government: the members contribute according to a pre-established schedule; the government contributes the difference between the current service cost and the required contributions by members.

Actuarial liabilities and current service costs were calculated using individual member data according to the existing provisions of the plan and under the assumption that the integration provision would be removed. Under that scenario of the integration provisions being removed, it was assumed that pension benefits would not be reduced upon attainment of age 65 or when a member becomes disabled and is entitled to a disability benefit from the CPP plan. Further, for pensioners in payment as at 1 April 2012, the integration reduction, if any, would be removed. This estimate does not take into account reductions that occurred before the valuation date.

Under this methodology, the cost of a plan amendment is measured by the increase in the current service cost (i.e. future annual contributions required to finance future benefit accruals) and the increase in actuarial liabilities as at the valuation date (where a new actuarial deficit may be amortized over a period not exceeding 15 years).

Detailed Valuation Results

1) **Current Service Cost**
   The total current service cost of the plan would increase by 2.1% of pensionable payroll (from 20.6% to 22.7% for plan year 2013 under the amended plan. The following table shows the current service cost for plan year 2013.

Current Service Cost for Plan Year 2013		
	In Percentage of Pensionable	In $ Million
Existing Plan	20.6%	442
New Plan (No CPP	22.7%	487
Increase	2.1%	45

2) Accrued Liability as at 31 March 2012

The following table shows the increase in liability of the plan as at 31 March 2012.

Actuarial Liability as at 31 March 2012
($ Billion)

	Contributors	Pensioners and Survivors	Combined
Existing Plan	*6.6*	*10.6*	*17.2*
New Plan (No CPP integration)	*7.2*	*12.0*	*19.2*
Increase	*.6*	*1.4*	*2.0*

If the increase in the actuarial liability of $2.0 billion were to be amortized in 15 equal annual instalments beginning on 31 March 2013, each instalment including interest would be $214 million.

Actuarial Opinion

This actuarial valuation has been prepared in accordance with accepted actuarial practice. The methodology, data and assumptions used for costing purposes are described in detail in the Actuarial Report on the Pension Plan for the Royal Canadian Mounted Police as at 31 March 2008.

Should you have any questions, please do not hesitate to contact me.

Yours truly,

Michel Rapin

Michel Rapin, F.C.I.A.
Actuary
Office of the Chief Actuary

cc: Jean-Claude Ménard (OCA)

Office of the Chief Actuary
Bureau de l'Actuaire en chef

Office of the Superintendent of Financial Institutions
Bureau du surintendant des institutions financières

10 November 2011

Mr. William Wellsbury
A/DPSP
Canadian Forces
Ottawa, Ontario

Dear Mr. Wellsbury:

Subject: OSFI Canadian Forces Superannuation Ministerial Query – Bill C-215 (Removing the CPP integration provision from the CFSA pension plan)

This letter discusses the actuarial methodology used to estimate the cost of removing the integration provision from the Canadian Forces Superannuation Act (CFSA) and presents its results.

Main Findings

If the CFSA pension plan was amended to remove the integration provision, the current service cost of the plan would increase by 2.0% of pensionable payroll, from 23.1% to 25.1% for the plan year 2013 and the accrued liability as at 31 March 2012 would increase by $6.6 billion, from $58.0 to $64.6 billion.

Valuation Basis

This estimate is based on the statutory valuation data as at 31 March 2010, which is the most recent published statutory actuarial report on the Canadian Forces pension plan. The economic and demographic assumptions used are also those from the actuarial report as at 31 March 2010.

The population data as at 31 March 2010 were projected to 31 March 2012. As at 31 March 2010, there were 71,862 contributors and the average pensionable earnings were $62,300. The number of retirement pensioners was 73,431 with an average annual pension of $25,942, and the number of disability pensioners was 14,261 with an average annual pension of $22,228. Under the current provisions of the plan, pensions are reduced by on average 19% at time of integration.

The Canada Pension Plan coordination factor for this pension plan is 0.625% per year of service.

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Valuation Methodology

For valuation purposes, the projected accrued benefit actuarial cost method was used to determine the current service cost and actuarial liability.

The actuarial liability with respect to contributors corresponds to the value, discounted in accordance with the actuarial assumptions, of all future payable benefits accrued as at the valuation date in respect of all accrued service at that date. For pensioners and survivors, the actuarial liability corresponds to the value, discounted in accordance with the actuarial assumptions, of future payable benefits.

The current service cost computed in respect of a given year is the sum of the value, discounted in accordance with the actuarial assumptions, of all future payable benefits considered to accrue in respect of that year's service. The current service cost under the CFSA is borne by the members and the government: the members contribute according to a pre-established schedule, the government contributes the difference between the current service cost and the required contributions by members.

Actuarial liabilities and current service costs were calculated using individual member data according to the existing provisions of the plan and under the assumption that the integration provision would be removed. Under that scenario of the integration provisions being removed, it was assumed that pension benefits would not be reduced upon attainment of age 65 or when a member becomes disabled and is entitled to a disability benefit from the CPP plan. Further, for pensioners in payment as at 1 April 2012, the integration reduction, if any, would be removed. This estimate does not take into account reductions that occurred before the valuation date.

Under this methodology, the cost of a plan amendment is measured by the increase in the current service cost (i.e. future annual contributions required to finance future benefit accruals) and the increase in actuarial liabilities as at the valuation date (where a new actuarial deficit may be amortized over a period not exceeding 15 years).

Detailed Valuation Results

1) **Current Service Cost**
   The total current service cost of the plan would increase by 2.0% of pensionable payroll (from 23.1% to 25.1% for plan year 2013) under the amended plan. The following table shows the current service cost for plan year 2013.

Current Service Cost for Plan Year 2013		
	In Percentage of Pensionable	In $ Million
Existing Plan	23.1%	1,066
New Plan (No CPP integration)	25.1%	1,159
Increase	2.0%	93

2) Accrued Liability as at 31 March 2012

The following table shows the increase in liability of the plan as at 31 March 2012.

Actuarial Liability as at 31 March 2012
($ Billion)

	Contributors	Pensioners and Survivors	Combined
Existing Plan	***19.5***	***38.5***	***58.0***
New Plan (No CPP integration)	***21.0***	***43.6***	***64.6***
Increase	***1.5***	***5.1***	***6.6***

If the increase in the actuarial liability of $6.6 billion were to be amortized in 15 equal annual instalments beginning on 31 March 2013, each instalment including interest would be $656 million.

Actuarial Opinion

This actuarial valuation has been prepared in accordance with accepted actuarial practice. The methodology, data and assumptions used for costing purposes are described in detail in the Actuarial Report on the Pension Plan for the Canadian Forces as at 31 March 2010.

Should you have any questions, please do not hesitate to contact me.

Yours truly,

Michel Rapin

M. Rapin, F.C.I.A.
Actuary
Office of the Chief Actuary

cc: J-C. Ménard (OCA)

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ANNEX B

MERCER REVIEW OF OSFI COSTINGS

MERCER

CONSULTING. OUTSOURCING. INVESTMENTS.

Review of the Cost Estimates of Removing the Integration Provision of the CFSA and the RCMPSA, as Proposed Under Bill C-215

For The Office of Parliamentary Budget Officer

February 17, 2012

MARSH & McLENNAN COMPANIES

CONTENTS

1

Our mandate

The House of Commons Finance Committee has requested that the Office of the Parliamentary Budget Officer ("OPBO") provide an independent cost estimate of Bill C-215, an Act to amend the Canadian Forces Superannuation Act (''CFSA'') and the Royal Canadian Mounted Police Superannuation Act (''RCMPSA'') to eliminate the integration of annuities with the Canada Pension Plan ("CPP") benefits, therefore increasing the amount of pension payable after age 65.

Mercer has been engaged by the OPBO to review the reasonableness of the cost estimates of the proposed changes that were prepared by the Office of the Superintendent of Financial Institutions (''OSFI''). As part of his mandate, Mercer has been requested to complete the following tasks in respect of the above noted cost estimates:

- review the approach used by OSFI regarding the plan change, the membership data and the assumptions used for the purpose of the estimate;
- disclose our understanding of the approach and comment on its appropriateness;
- review the process used by OSFI to validate the cost estimate and comment on such process;
- confirm that the order of magnitude of the estimate is reasonable;
- identify any omissions and potential refinements and/or improvements regarding the cost estimate; and
- prepare a report summarizing our review and findings.

This report provides a summary of our review and findings regarding the cost estimates as of March 31, 2012.

Please note that we have not attempted to replicate the valuation results of the most recent statutory valuations for each plan. In particular, we have not verified the validity of the membership data used in these valuations, which were also used for purposes of the estimates. Moreover, we do not provide an opinion on the reasonableness of the assumptions and methods used for these statutory valuations. Where the same assumptions and methods are used for purposes of the cost estimates, we comment on such use for the purpose of the cost estimates, but not on the reasonableness of these assumptions and methods for the purpose of the funding of the plans.

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Information analyzed

The basis of our review is the cost estimates presented in the following documents ("Documents Under Review"):

- A letter dated November 10, 2011 signed by Mr. Michel Rapin, Senior Actuary at OSFI, on the estimate of the cost of removing the integration provision for the CFSA as of March 31, 2012; and
- A letter dated December 20, 2011 signed by Mr. Michel Rapin, on the estimate of the cost of removing the integration provision for the RCMPSA as of March 31, 2012.

As part of our review, we have referred to the following additional information:

- A copy of Bill C-215;
- A copy of the most recent statutory valuation reports prepared by OSFI for both plans; the valuation date being March 31, 2010 for CFSA and March 31, 2008 for RCMPSA ("Statutory Valuation Reports");
- Further breakdowns of the results by categories of plan members for both plans (provided by OSFI);
- Information pertaining to average salary and age information for contributors as well as the average expected remaining service lifetime (provided by OSFI); and
- Lists of pension and integration amounts for retired and disabled members (with no personal identifier) for RCMPSA (provided by OSFI).

We have also met and discussed with OSFI as follows:

- A face-to-face meeting with Mr. Mario Mercier, an Actuary at OSFI, on January 31, 2012, to enquire about the process underlying the preparation of the cost estimates for the RCMPSA and to request further relevant information;
- A telephone conversation with Mr. Michel Rapin on February 1, 2012, to enquire about the process underlying the preparation of the cost estimates for the CFSA and to request further relevant information; and
- Various subsequent telephone conversations with Mr. Mercier to obtain clarification on the process and on the additional information received.

3

Review of cost estimate process

Our review of the process is mostly based on the Documents Under Review, and our meeting and conversations with OSFI actuaries. They confirmed that their work is governed by the Canadian Institute of Actuaries and the laws applicable to each plan, i.e. RCMPSA and CFSA.

The actual membership data used by OSFI was the data used in the most recent actuarial valuation for each plan, and it was therefore compiled as at March 31, 2008 for the RCMPSA and March 31, 2010 for the CFSA. For purposes of the cost estimates, we understand that the data was projected to March 31, 2012 for each plan with additional years of service, using assumptions pertaining to terminations, deaths and retirements, growth of population, new entrants and salary growth, consistent with assumptions noted in the Statutory Valuation Reports. In our opinion, this approach is appropriate for the purpose of the cost estimates.

We understand that OSFI prepared two valuations as of March 31, 2012 for each plan, based on the data projected to March 31, 2012: one valuation with the current plan provisions (i.e. including a provision of integration with the CPP) and one valuation with the proposed change (i.e. with no integration). We understand that the data pertaining to the reduction in pension which was or would be applied for healthy pensioners and disabled pensioners is already available in the membership data; therefore, to perform calculations with no integration, the actual reduction amounts, adjusted to reflect indexation between the date of pension commencement and April 1, 2012, were added back to the reduced pension amounts. This ensures that the appropriate increases in pensions were valued, given that the integration level of each pensioner depends on his/her year of attainment of age 65 (the integration level is graded down from 0.7% to 0.625% over five years). For the contributors, we understand that the table of integration factors was updated to indicate 0% integration instead of the current percentages applicable in the year of assumed retirement.

The difference in liabilities and current service costs between those two valuations produced the cost estimates presented by OSFI.

OSFI confirmed that the March 31, 2012 valuations were based on the same valuation methods used in the statutory valuations as set out in the Statutory Valuation Reports. In particular, to determine the current service costs as a percentage of pensionable earnings, the total salary pensionable under the RCMPSA or CFSA, as applicable, and under the Special Retirement Arrangement Act was used, and a provision for administrative expenses was included.

OSFI also confirmed that the March 31, 2012 cost estimates were based on the assumptions set out in the Statutory Valuation Reports and applicable for years starting with plan year 2013. Given that the plan modification would increase retirement benefits, we enquired whether consideration was given to changing the retirement scale to reflect a potential anticipation in future retirement dates. OSFI mentioned that they felt that modifying such assumption at this point is unnecessary since retirement rates at young ages are already significant because of the plan's early retirement provisions. Without having more insight into patterns of retirement for these employees, we tend to agree with that.

We have confirmed with OSFI that there has been no significant event since the last statutory valuation, such as modifications to each of these plans' provisions, or significant changes in membership data (e.g. due to a workforce downsizing) or in salaries (such as negotiated salary increases which would be significantly different from the assumed increases).

With respect to OSFI's validation of the results of these cost estimates, they have confirmed that, to prepare the cost estimates, they have used the same programs that have been tested extensively for valuation purposes, that they compared the results with previous similar cost estimates that had been prepared, and that the results are consistent with the average percentage of pension reduction due to the integration provision. Their process seems appropriate. We would normally suggest that individual testing would take place in the course of preparing a cost estimate, but it seems as though in this case, additional testing was not necessary, in light of prior testing done on these programs and prior similar cost estimates.

4

Review of results

To verify the reasonability of the results pertaining to the increase in liabilities and current service costs, we have performed a series of validations, as summarized below:

- Based on the detailed breakdown of results, we have confirmed that the impact of the plan change is nil for contingency benefits for healthy pensioners and disabled pensioners, and for widows and children, which is as expected since current benefits for these groups are not integrated with CPP.
- Based on detailed information on pension reductions due to the integration provision for healthy pensioners and disabled pensioners of the RCMPSA, we have validated that the increase in liabilities for these groups is consistent with the information on the average level of integration.
- The increase in liability for the contributors is lower than the increase for the pensioners, given that the benefit improvement would take place on their future attainment of age 65, which is later than for pensioners and therefore represents a lower proportion of their total liability.
- For the contributors, we have confirmed that the percentage increase in the current service cost is consistent with the percentage increase in their liability.
- To validate the cost increase on the liability of the contributors for each plan, we have independently estimated the average impact using the average age of the contributors, their average age at retirement (based on the expected average remaining service lifetime) and their projected pension with and without an integration at age 65; the results of these tests are very close to the actual cost increase determined by OSFI.
- We have confirmed that the percentage increase in the liability and the current service cost for the affected categories of members is similar for both plans, which is expected given that plan provisions are very similar.

Based on the above, we affirm that the increases in liabilities and current service costs presented in the Documents Under Review are reasonable.

5

Our comments and findings

Interpretation of Bill C-215

OSFI explained that their mandate was to cost the impact of Bill C-215, assuming that the removal of the integration provision would apply as at March 31, 2012 to all service for all contributors, healthy pensioners, and disabled pensioners. OSFI assumed that the Bill C-215 would have no retroactive impact, i.e. the pensions in payment that have already been reduced by the integration would be increased as of April 1, 2012 to reverse this integration but no retroactive payments would be made to compensate for the lower pension payments made during the period since the date of the reduction and March 31, 2012.

Since Bill C-215 does not clarify the service (e.g. past vs. future), the category of members (e.g. contributors vs. pensioners), or the application date contemplated by the change, we recommend that the intent of such Bill be confirmed to ensure it is consistent with the assumptions described in the preceding paragraph before using the cost estimates.

Economic assumptions

As previously mentioned, the economic assumptions used for purposes of the cost estimates are those used in the most recent statutory actuarial valuations. It is an acceptable practice to use the same assumptions as those used in the latest actuarial valuation for purposes of preparing a cost estimate.

However, economic conditions have changed considerably since March 31, 2008 and March 31, 2010, as applicable. If new economic assumptions were to be established as of March 31, 2012, it is most likely that assumptions would be revised. In particular, discount rates would likely be set at lower levels than those used for the latest statutory actuarial valuations to reflect lower long-term expectations, resulting in larger increases in liabilities and current service costs, compared to those determined by OSFI. Recognizing that a valuation represents one assessment of the financial position based on a set of assumptions and that other assumptions would yield different results, an analysis of the sensitivity of the cost estimates to the main economic assumptions would provide useful information.

Moreover, it is unclear to us what the actual cost of such plan amendment would be for the government, and if the actuarial basis used for the cost estimates is appropriate for that purpose.

Funding of additional benefits

It is unclear to us how the funding of additional benefits resulting from the amendment would be allocated between the Superannuation Account and the Pension Fund for both plans. OSFI has assumed that the increase in liabilities would be split between the Superannuation Account and the Pension Fund according to the service covered by each of these accounts. We do not know if there have been precedents for taking this approach. It is important to match the assumptions used for determining liabilities with the underlying expected return on assets backing such liabilities. Note that if the increase in liabilities were to be fully attributed to the Pension Fund, the impact of the plan change would be different. Based on assumptions used for the latest statutory valuations, the impact would be lower since the discount rate used to value the liabilities covered by the Pension Fund is higher.

Special Retirement Arrangements Act ("SRAA")

Our understanding is that the SRAA covers benefits in respect of earnings in excess of the maximum earnings that can be covered under the RCMPSA and CFSA ("Base Plans"), as applicable, in accordance with the Income Tax Act. A direct consequence of the removal of the integration provision is the reduction of the maximum level of pensionable earnings recognized under the Base Plans, and therefore a related increase in earnings covered under the SRAA. The funding of benefits covered under the SRAA is more expensive than funding similar benefits under the Base Plans, given that it is funded through a Retirement Compensation Arrangement (RCA), which does not benefit from the same tax sheltering of retirement income.

OSFI confirmed that, for the CFSA, the cost estimates only include the increase in liabilities and current service cost in the Base Plan. Therefore, the costs related to the plan change are potentially underestimated. Having said this, although it is impossible for us to evaluate the impact of the plan change on the SRAA, given the size of the current SRAA liabilities based on the Statutory Valuation Report, and the high level of the salary covered under the Base Plan (even after the impact of the contemplated change), it seems fair to assume that such impact would be immaterial for purposes of the cost estimates.

With respect to the RCMPSA, OSFI confirmed that the cost estimates include the increase in liabilities and current service cost for both the Base Plan and the SRAA. However, a portion of the impact on the SRAA liability seems to have been valued using the Base Plan assumptions. As mentioned above, the costs related to the plan change therefore seems to be slightly underestimated. Again, given the size of the current SRAA liabilities based on the Statutory Valuation Report, and the high level of the salary covered under the Base Plan (even after the impact of the contemplated change), it seems fair to assume that such impact would be immaterial for purposes of the cost estimates.

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Conclusion

Based on our review of the process, as described in Section 3 of this report, and of the results of the cost estimates related to Bill C-215 for the CFSA and the RCMPSA, we confirm that the process used by OSFI is appropriate and that the results presented in the Documents Under Review are reasonable, assuming that the intent of such Bill is consistent with OSFI's understanding, as noted on page 6 of this report.

We have a few comments and suggestions, as noted in Section 5.

We would like to thank OSFI's personnel for their cooperation during the execution of this mandate.

Respectfully submitted,

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Date	Date

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