

# C/QPP costs and private pensions

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**M**uch recent discussion has centred on prospects for growth in the share of Canada's workforce covered by employer-sponsored registered pension plans (RPPs). One issue that has not attracted much attention is the possible impact of the rising costs of the Canada and Quebec Pension Plan (C/QPP) on RPPs. Increased contributions, implemented in recent years to maintain the financial stability of the C/QPP, may hamper efforts to expand the private pension system. While participation in the C/QPP is mandatory for virtually all workers aged 18 and older, RPPs are largely provided at the employers' discretion. [\(1\)](#) Consequently, C/QPP coverage is almost universal, but fewer than four out of ten workers are covered by RPPs. Will the higher contributions legislated for the C/QPP deter the establishment of new RPPs or even cause the termination of some of those now in existence?

## C/QPP contributions

The Canada and Quebec Pension Plan is funded through contributions required from workers and their employers. A percentage of workers' "contributory earnings" is withheld for the C/QPP, and this amount is matched by their employers. (Self-employed individuals must contribute both the employee and employer portions.) Contributory earnings are those between a minimum amount (the basic exemption) and a maximum amount (the year's maximum pensionable earnings or YMPE). The YMPE is increased annually to bring it to the approximate level of average wages and salaries as determined by Statistics Canada's Survey of Employment, Payrolls and Hours. At the same time, the basic exemption, which is 10% of the YMPE, also rises. [\(2\)](#)

Implementation of the C/QPP in 1966 required matching contributions of 1.8% of contributory earnings from workers and employers, for a combined rate of 3.6%. While authorities recognized that this rate would eventually prove inadequate, it remained at this level for 21 years. [\(3\)](#)

## Rising rates

In 1985, to meet the demands of increasing benefit payments, an agreement was reached between the federal and provincial governments to gradually raise the CPP contribution rate, starting in January 1987. The rate schedule is reviewed every five years. The most recent review, in January 1991 resulted in a schedule that runs to the year 2016. If this schedule is not altered, by 2016 the combined employee/employer rate will be 10.1%, up from the 1993 level of 5% ([Table 1](#)). <sup>(4)</sup>



## Table 1 C/QPP combined employee/employer contribution rates\*.

Source: *Finance Canada*

\* *Implemented in 1987 and currently projected to 2016.*

## Integration with the C/QPP

Introduction of the C/QPP in 1966 meant that workers were able to accumulate a basic level of retirement savings, but at some cost to themselves and their employers. As a result, many employers re-evaluated their RPPs. A few RPPs were actually terminated, but many others were changed. <sup>(5)</sup> The most common approach was to integrate RPP contribution and/or benefit rates with those of the new public program (see [Data source and definitions](#)). By 1970, three out of every four RPP participants were in integrated plans.

To shield employees who were contributing to RPPs from additional C/QPP premiums, their contribution rates were integrated with the C/QPP rate. The usual method of integration was to "offset" RPP contributions by the amount paid to the C/QPP. While this approach sheltered employees from the C/QPP contribution requirement, it delivered less to their RPPs. <sup>(6)</sup>

In 1970, 77% of RPP contributors had an offset contribution formula. Fifteen years later, in 1985, the proportion had declined only slightly, to 71% ([Chart A](#)). By 1990, however, only 26% of contributors had an offset formula while 51% had a step-rate formula. <sup>(7)</sup>



## Chart A Offset integration has decreased dramatically in recent years.

Source: *Pension Plans in Canada database*

## More money flowing to the C/QPP

This movement away from contribution offsets was a direct response to the C/QPP contribution increases. Offsetting RPP contributions was not a problem as long as the C/QPP rate was held at 1.8%. But as this rate increased after 1986, the proportion of employee contributions allocated to RPPs decreased. For example, members whose RPP contribution rate was 6% less C/QPP contributions, and whose earnings did not exceed the YMPE, would have contributed 4.2% of their earnings <sup>(8)</sup> to their RPPs in 1986 (6.0% less the 1.8% C/QPP rate) but just 3.8% in 1990 (6.0% less 2.2%). Moreover, with each succeeding year, the portion of their earnings allocated to the RPP would further decline.

This reduction in employee contributions would result in either lower RPP benefits or increased employer contributions. Since most RPP members are in defined benefit plans (see [Data source and definitions](#)), a large number of employers would have to make up the difference.

### Reduced future RPP coverage?

As the C/QPP contribution rates continue to rise, their impact on RPPs may be even greater in the future. Some employers, particularly small businesses, may not be able to afford RPPs. A large proportion of workers in small businesses earn less than the maximum C/QPP contributory earnings level (YMPE). <sup>(9)</sup> By 2016, such employers will be required to contribute more than 5% of possibly 90% of their payroll (total payroll less each worker's basic exemption) to the C/QPP. This requirement may preclude some of them from providing an RPP.

Similarly, many low-income workers who currently contribute to an RPP may have difficulty making contributions as a rising share of their earnings is withheld for the C/QPP. In 1990, one out of every three RPP contributors had a total income above that year's basic exemption (\$2,800) but below the YMPE (\$28,900). <sup>(10)</sup> Nearly all of them contributed to the C/QPP as well. Their average RPP contribution amounted to \$741, while that paid to the C/QPP was \$362, for a total of just over \$1,100 ([Table 2](#)). But, if the C/QPP contribution rate had been 5.05% (the rate projected for 2016), their average C/QPP contribution would have been \$831. This would have made additional RPP contributions more difficult. <sup>(11)</sup>



### Table 2 Employer-sponsored pension plan (RPP) contributors by C/QPP participation and income, 1990\*.

Source: *Revenu Canada, Taxation*

Terminating RPP membership because of C/QPP requirements has occurred before. Between 1965 and 1967, an undetermined number of employees who belonged to contributory RPPs and whose participation was not compulsory, discontinued their membership when the mandatory C/QPP came into effect. These departures were reflected in higher levels of cash withdrawals from RPPs in those years ([Weitz](#), 1992).

## More non-contributory plans?

Despite the inevitable increases in the C/QPP rates, a substantial proportion of RPPs with offset employee contribution rates have not been amended. In 1990, nearly 1,600 plans, covering 949,000 workers (26% of all RPP contributors), still had an offset contribution formula. [\(12\)](#) Moreover, nearly 1,400 of these plans, covering 182,000 workers, had offset contribution rates of 5% or less of members' earnings. If these plans are not amended and the 25-year CPP contribution schedule materializes, by 2016 these plans will, in effect, be non-contributory for members with earnings below the YMPE. Consequently, their employers will be required to pay all the costs.

## Summary

Annual increases in the C/QPP contribution rate began in 1987 and are expected to continue well into the next century. While these increases have already affected RPPs, their impact in the future may be even greater. Since growth in the C/QPP rate reduces the share of contributions flowing to RPPs with offset contribution formulas, the majority of these plans have been amended. Those that still have an offset formula may well be changed in the near future.

If the currently projected C/QPP rates materialize, some employers may be unwilling or unable to sponsor a supplementary plan for their workers. Also, some workers, particularly those whose earnings remain at or below the average wage and salary level, may have difficulty making additional contributions to an RPP.

These conjectures about the possible consequences of increased C/QPP contribution rates are based on the assumption that the future relative earnings and economic well-being of the workforce will change little from the current situation. Also, this analysis considers neither the advantages of C/QPP contributions as tax credits to workers nor the impact of increased contributions on their income tax payable.

The problems of increasing pension costs are not unique to Canada. Declining private pension coverage of the workforce, coupled with mushrooming expenditures on public pension programs, is evident in most member countries of the Organisation for Economic Co-operation and Development (OECD). Among the alternatives being considered by these countries are measures that would have private

pensions (both employer-sponsored and personal plans) serve the needs of individuals with higher incomes, leaving government plans as a safety net for the remainder of the population ([Duskin](#), 1992).

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## Data source and definitions

### The Pension Plans in Canada database

The information in this article is from the Pension Plans in Canada database maintained by the Labour Division of Statistics Canada. This database has been made possible through a co-operative arrangement with the federal and provincial agencies responsible for the supervision and regulation of employer-sponsored pension plans (RPPs) in their jurisdictions. The information is updated annually and covers a wide range of characteristics of all RPPs, including detailed classifications of the contribution and benefit formulas of each one. These classifications indicate whether the plan design takes C/QPP contributions and benefits into consideration and, if so, how the linkage is achieved.

As new plans are registered and existing plans amended, information is provided to Statistics Canada. Because the effective date for most amendments and new plans is January 1, annual figures reflect the number of active plans and their characteristics at the beginning of each year. There is, however, a time lag in the filing of documents by plan sponsors, the sanctioning and registering of applications by the pension authorities, and the reporting of data to Statistics Canada. Consequently, annual figures may not reflect very recent changes.

For further information, contact the Pensions Section of the Labour Division at (613) 951-4034.

**Integration:** Adjustments to contribution or benefit formulas of employer-sponsored registered pension plans (RPPs) that take into account the amounts paid into, or received from, the Canada and Quebec Pension Plan (C/QPP).

**Benefit step-rate:** A form of integrating an RPP benefit formula with the C/QPP to provide a lower level of benefits on earnings up to the year's maximum pensionable earnings (YMPE). For example, a formula of 2% of final earnings (average earnings in the last few years before retirement) for each year of service might be amended to 1.3% on earnings, up to the YMPE, and 2% on the balance of these earnings.

**Contribution offset:** A form of integrating employee, and sometimes, employer RPP contributions with the C/QPP, whereby the amount that has to be allocated to the RPP is reduced ("offset") by the C/QPP contributions; for example, 5% of earnings less the required C/QPP contributions.

**Contribution step-rate:** A form of integrating employee and employer contributions with the C/QPP, whereby the percentage of earnings allocated to the RPP is lower for earnings up to the YMPE. For example, employees may be required to contribute 3.2% of their earnings up to the YMPE and 5% on the balance of their earnings.

**Defined benefit plan:** An RPP that specifies the benefits that members will receive at retirement or termination from the plan, but does not define the employer's contributions. Instead, the employer's contributions are determined by calculating the costs of providing these benefits. More than 90% of RPP members belong to defined benefit plans.

**Defined contribution plan:** An RPP that specifies the employer's contributions. Members' benefits consist of accumulated contributions plus interest earned at the time of retirement or termination from the plan.

**RPP contributors:** Members of RPPs who are required to contribute. More than 70% of RPP members are in contributory plans; for the remaining 30% their employers alone contribute.

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## Notes

### *Note 1*

The C/QPP is a universal program, introduced in 1966 to provide minimum levels of retirement, disability and survivors' benefits for Canada's workforce. The CPP is administered by the federal government and covers workers outside Quebec, while the QPP is administered by the Quebec government for workers in that province. Most RPPs, whose roots can be traced back to the early 1800s, predate the C/QPP ([Weitz](#), 1992). Because of legislative restrictions, some workers cannot participate in RPPs, and many employers, particularly those with few employees, do not provide such plans. For details on RPP coverage rates by various employee and employer characteristics, see [Frenken and Maser](#) (1992).

### *Note 2*

Both the YMPE and the basic exemption are rounded down to the nearest \$100. Consequently, the 1993 basic exemption and YMPE are \$3,300 and \$33,400, respectively.

### *Note 3*

The C/QPP has always operated on a "pay-as-you-go" basis. Benefits were paid from current contributions, and the contribution rate was deliberately kept low, with the understanding that it would eventually have to be raised ([Minister of Supply and Services Canada](#), 1985). The increased costs are

primarily the result of dramatic growth in the number of beneficiaries.

**Note 4**

There is no comparable 25-year schedule for the QPP. However, the Quebec government conducts a similar review every five years and, so far, has implemented identical increases in the QPP contribution rate. Some observers have suggested that the rate projected to 2016 may be insufficient ([William M. Mercer Ltd.](#), 1992). In fact, the recently released actuarial report of the CPP indicates that the projected surplus in the fund, based on the current 25-year contribution schedule, will not be as large as previously anticipated ([Office of the Superintendent of Financial Institutions](#), 1993).

**Note 5**

Just 433 RPPs, covering fewer than 4,300 members (out of a total of 2.3 million), were discontinued as a result of the introduction of the C/QPP ([Statistics Canada](#), 1967).

**Note 6**

Integration of employee contributions was usually accompanied by integration of RPP benefits (usually benefit step-rate formulas), resulting in lower benefits.

**Note 7**

The remaining 22% had a combination of rates or rates that varied for different classes of members.

**Note 8**

It would be slightly higher than 4.2% since C/QPP contributions are not required on earnings below the basic exemption.

**Note 9**

Small businesses tend to pay lower wages than large firms ([Morissette](#), 1991).

**Note 10**

According to Revenue Canada taxation statistics, based on income from all sources, 34% of taxfilers who contributed to an RPP in 1990 had incomes in this range. Based on employment earnings only, this percentage increases to 40%.

**Note 11**

Even RPP contributors with income above the YMPE may have some difficulty managing the increased C/QPP contributions. In 1990, those with total income above the YMPE but below \$40,000 contributed, on average, just over \$2,000 to their RPP and the C/QPP combined. If the 5.05% C/QPP contribution rate had been in effect, this combined contribution would have been more than \$2,700.

Increased C/QPP contributions may have a similar impact on registered retirement savings plans (RRSPs). In 1990, nearly 1.5 million RRSP contributors (35% of the total) reported total incomes less

than the YMPE. More than 90% of them also contributed to the C/QPP. Their RRSP participation rate and contributions might have been much lower if the C/QPP rate projected for 2016 had been in effect, as their average C/QPP contribution would have been \$813, instead of \$354. Also, those with incomes above the YMPE but below \$40,000 that year, would have been obliged to contribute nearly \$1,300 to the C/QPP on average, rather than the \$562 reported on their tax returns.

### Note 12

Three-quarters of these members were public sector employees. For definitions of the public and private sectors, as they apply to these data, see [Frenken and Maser](#) (1992).

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## Source

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Table 1

**C/QPP combined employee/employer contribution rates\***

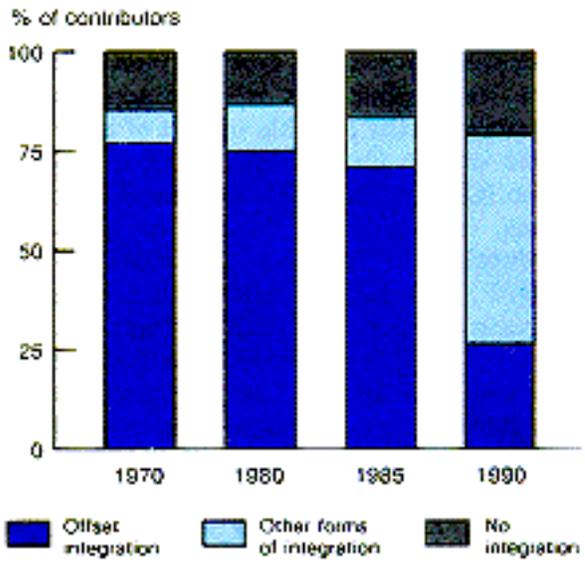
Year	%	Year	%
1987	3.80	2002	7.10
1988	4.00	2003	7.35
1989	4.20	2004	7.60
1990	4.40	2005	7.85
1991	4.60	2006	8.10
1992	4.80	2007	8.30
1993	5.00	2008	8.50
1994	5.20	2009	8.70
1995	5.40	2010	8.90
1996	5.60	2011	9.10
1997	5.85	2012	9.30
1998	6.10	2013	9.50
1999	6.35	2014	9.70
2000	6.60	2015	9.90
2001	6.85	2016	10.10

*Source: Finance Canada*

*\* Implemented since 1987 and currently projected to 2016.*

Chart A

**Offset integration has decreased dramatically in recent years.**



Source: Pension Plans in Canada database

Table 2

**Employer-sponsored pension plan (RPP) contributors by C/QPP participation and income, 1990\***

	RPP contributors		Average 1990 contributions	
			RPPs	C/QPP
	'000	%	\$	
<b>All contributors</b>	<b>3,696</b>	<b>100</b>	<b>1,607</b>	...
With C/QPP contributions	3,598	97	1,628	496
\$ 2,800 - 28,899**	1,203	33	741	362
\$28,900 - 39,999	1,032	28	1,456	557
\$40,000 - 59,999	1,020	28	2,275	569
\$60,000 and over	339	9	3,364	569
Without C/QPP contributions	98	3	843	...

*Source: Revenu Canada, Taxation*

*\* Includes income from all sources. A small number of RPP contributors had income less than \$2,800. They were not required to contribute to the C/QPP.*

*\*\* The 1990 basic exemption was \$2,800 and the YMPE \$28,900.*