The Path to Retirement Security in Canada:
How Employers and Plan Administrators Can Help

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Introduction

What Is Retirement Security?

While the meaning of a secure retirement varies by individual, it can generally be viewed as having the ability to fund one’s retirement lifestyle goals and paying bills without worrying about running out of money during one’s lifetime.

In recent years, a combination of powerful financial and demographic forces has made retirement income security a topic of enormous concern in many parts of the world. Research reports and news headlines shout warnings of the greatest retirement crisis in history as policy makers, employers and households brace for what they fear is ahead.

The baby boom following World War II, improvements in health care that have increased life expectancy, persistent low interest rates and retirement savings decimated by the financial meltdown of 2008 have contributed to the anxiety for future retirees. Many argue we need a broad range of actions to avoid a crisis. Others say Canadians may be better off than they think and any notion of a crisis is more perception than reality.

The purpose of this paper is to examine the factors that have led to concerns regarding retirement security, assess the extent to which there is a problem facing future Canadian retirees and explore the implications for Canadian workers, employers and plan administrators (Sections I through III). Understanding these elements is essential to developing efficient and rational retirement income security programs. The other aim of this report is to enlighten employers and plan administrators regarding the critical role they can play in helping workers achieve a secure retirement (Section IV).
I. Retirement Readiness

Perceptions

How do some of the stakeholders in retirement security—plan sponsors, plan administrators and workers—view the financial readiness of Canadian workers with respect to retirement? In 2014, the International Foundation of Employee Benefit Plans asked representatives of multi-employer pension plans and employers to assess the retirement preparedness of their average active worker at normal retirement age (Figure 1). Just 13% described these workers as “very” or “extremely” prepared. They considered almost half (49%) “somewhat” prepared.¹

How do workers feel regarding their personal preparation for retirement? When AEGON asked workers (excluding those who were self-employed) how confident they were that they would be able to fully retire with a lifestyle they considered comfortable, only 21% reported they were either “very confident” or “extremely confident.” Slightly more than one in three (35%) reported they were “not at all confident” or “not very confident” (Figure 2).²

Reality

Statistics Canada employs a computer model to gauge the retirement readiness of households. Essentially, the model calculates a net replacement ratio that compares disposable income after retirement with preretirement. See Figure 3, which breaks down the projected replacement rates for households by income quintiles. In the analysis, a replacement rate of 75% is considered low but tolerable. The ideal rate is above 95%. For an explanation of why most Canadians do not have to replace 100% of their income, see Exhibit 1.

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Exhibit 1 | Retirement Savings and Income: How Much Is Enough?

Do retirees need 100% of their preretirement income during retirement? While there are always exceptions, the answer for most people is “no.” Keep in mind that work-related expenses such as commuting to work are eliminated when people retire. For most, mortgages, the cost of raising/educating children and saving for retirement are also behind them. Taxes are often lower with senior tax breaks such as the age 65 tax credit and the pension income credit. Furthermore, when seniors make retail purchases, there is a proliferation of senior discounts that provide savings not available when they were younger. On average, health-related expenditures will be the only component of spending that rises after age 65—These costs offset only part of the declines in spending.3

In addition, how much money people earn and spend is not consistent through retirement. When contemplating retirement, it is important to recognize there are different phases.

- **Phase I.** This is the most active phase of retirement. Assuming they have no serious health issues, this is the time retirees often elect to spend money on travel, hobbies or other forms of entertainment. They may also do more food preparation and other work around their home on their own, which cuts costs. During this phase, some elect to participate in part-time employment to boost their other sources of income.

- **Phase II.** Diminishing physical and/or mental capacities move people into this second phase of retirement. The death of a spouse or close friends can also precipitate the transition. During this phase, retirees tend to travel less and cut back on other strenuous activities. They may no longer be able to drive a car. In general, their spending declines and employment is less likely.

- **Phase III.** When a person’s physical/mental impairments are such that the individual needs home or nursing care, he or she has entered the third phase of retirement. The level of spending in this phase depends in large part on whether a person desires private nursing assistance or an upscale nursing home beyond what is provided via government programs.

The decline in consumption as the average person ages has been confirmed by a 1992 study of German households in an environment similar to Canada in terms of (1) per capita income and (2) a social safety net that includes public health spending.4 More recent data using Statistics Canada’s *Survey of Household Spending* shows the same pattern.5

Statistics Canada considers 95% to 115% an ideal net replacement ratio, while 75% to 95% is low but tolerable.6 In contrast, a C.D. Howe Institute report suggests most persons can retire comfortably on less than 70%.7 Instead of accepting any one of these assumptions, individuals are well-advised to take the time to consider how they envision spending their retirement years and the implications for their retirement spending. A person’s risk tolerance will also influence the ratio chosen, with some choosing a higher ratio so they can feel more secure they will have sufficient funds for both their needs and wants when they retire.
Contrary to what some may anticipate, the vast majority of households in Canada’s lowest income quintile (Q1) will be much better off in retirement than they were in their working years. For this group, the problem may be one of over-saving. Grasping how this could be possible requires an understanding of the four pillars that support Canada’s retirement system (Exhibit 2).

The small percentage of those in Q1 with readiness scores under 75% are persons with spotty employment records and new Canadians who have not lived in the country long enough to receive the full Old Age Security (OAS) and Guaranteed Income Supplement (GIS) benefits that comprise Pillar I. Generally, any efforts to increase the savings of households in this low-income quintile would do more harm than good. Not only does saving reduce their disposable income during their working years, the additional retirement income generated would reduce their GIS entitlement.

The story is entirely different for those in Q4, with 30% of households having low replacement ratios (under 75%). Caution must be given, however, as to how many are at risk in this group:

- The computer model does not take into account all Pillar IV assets. Only half of the equity of one’s home is included. Other financial assets outside tax-assisted retirement vehicles, equity in a business and real estate are fully excluded. Downsizing a home, collecting rent on investment property or selling a business and investing the proceeds are all opportunities for supplementing retirement income. While Pillar IV assets are skewed toward Q5 households, it is likely Q4 households also have substantial Pillar IV assets that could be used to supplement other retirement resources.
- It is assumed balances in capital accumulation plans (CAPs) will be converted into a stream of retirement income that is fully inflation-protected. Such protection is expensive, and there is some research that indicates it may be unnecessary since retirement income needs decline with age. Note that the fifth quintile—the top 20% of households, with an average income of $204,000—was excluded in Figure 3. Those doing the analysis assumed persons in Q5 have the means to achieve retirement income security without government initiatives. High-income workers are much more likely to have pension coverage than those with lower income. Furthermore, as stated previously, this group is more likely to have personal retirement savings (Pillar IV assets).
Canada’s retirement system is often described as three or four pillars. How these pillars are defined varies. For the purposes of this report, four pillars will be referenced.

I—Old Age Security (OAS).
Sometimes referred to as Social Security, this federal program is funded from general tax revenues. It provides protection from abject poverty by guaranteeing a floor of income support below which most Canadians will not fall. The federal government’s Guaranteed Income Supplement (GIS) and various provincial government programs top up incomes—providing additional support. OAS and GIS are flat, income-tested benefits paid to individuals 65 years and older who meet a long-term residency requirement. GIS benefits are cut 25 cents for every dollar of non-OAS income. Both OAS and GIS—as well as some provincial guaranteed income supplements—are adjusted quarterly to reflect changes in the Consumer Price Index as protection against inflation.

II—The Canada/Québec Pension Plans (CPP/QPP).
Mandatory government programs, the CPP/QPP are employment-based and financed entirely by employee and employer (including the self-employed) contributions over a person’s working life. The maximum benefit under CPP/QPP is 25% of career average earnings up to the average industrial wage ($53,600 in 2015). Unlike OAS and GIS, the CPP/QPP is not income tested. Originally established as an occupational pension arrangement, the CPP/QPP provides various disability and spousal survivor benefits. Spouses receive 60% of their partner’s benefit if they do not receive other CPP/QPP benefits. Given the initial intent of CPP/QPP was to help people without a workplace plan, many pension plans integrate their benefit formulae and target income replacement payouts with CPP/QPP benefits. To keep pace with inflation, benefits from these plans are indexed to the Consumer Price Index and adjusted annually.

III—Workplace pension plans.
The components of this pillar include tax-advantaged plans regulated by the federal government that are offered to employees as part of the terms and conditions of employment. Such plans are available in the workplace only where an employer has chosen to establish a plan or where a union with bargaining rights has persuaded an employer to establish or participate in a plan through collective bargaining. Other labels for this group of plans include occupational pension plans and employment pension plans.

Plans in this group that permit members to make investment decisions among two or more options offered within the plan are referred to as capital accumulation plans (CAPs) and are subject to the Guidelines for Capital Accumulation Plans released by the Joint Forum of Financial Market Regulators. While CAPSA Guidelines do not have the force of law, these guidelines may be used as a benchmark by the courts and/or regulators to assess whether a plan administrator has fulfilled its fiduciary obligations.

- Registered Pension Plans (RPPs) are defined benefit (DB), defined contribution (DC) or hybrid plans. The latter includes target benefit, cash balance and combination plans, etc. Employer contributions required for a DB plan are whatever is necessary to provide the benefits promised members. With DC plans, an employer must contribute a minimum of 1% of a worker’s income. For plans that are not a DB plan, the plan’s design determines whether an employee may contribute and whether an employee is required to contribute.

While employed by the employer sponsoring their RPP, members cannot withdraw required contributions—funds must remain in the RPP until the member’s termination of employment, death or retirement. Members may, however, withdraw amounts accumulated through voluntary contributions. At termination of employment, a member is entitled to his or her own contributions and plan sponsor vested contributions unless the assets are locked in. Members also have the option to transfer accumulated amounts to another RPP or a locked-in Registered Retirement Savings Plan (RRSP). Generally, funds in a locked-in plan cannot be withdrawn, but there are some exceptions such as small entitlements or a member with a shortened life expectancy. Members can also apply to the minimum standards regulator to withdraw funds on hardship grounds.
Exhibit 2 | The Canadian Retirement System (continued)

- **Registered Retirement Savings Plans (RRSPs)** are defined contribution plans that may be set up for an individual or a group of individuals who do not have an RPP. Set up at a financial institution such as a bank, credit union, trust company, mutual fund company, insurance company, investment dealer or brokerage firm, the plan may be a regular RRSP or a self-directed one. Those that are self-directed may hold a broader range of investment vehicles (e.g., individual stocks) and allow employees to manage personally the assets in their own accounts. Plan rules determine whether the RRSP is voluntary or compulsory for members.

Employee contributions to a Group RRSP are made on a pretax basis and can be deducted from taxable income, subject to Income Tax Act (ITA) limits. Money in these accounts accumulates tax free until withdrawn when it is treated as income for tax purposes. Beyond the tax advantages, a key benefit of a Group RRSP is that the employer regularly deducts an employee’s payroll contribution and deposits the funds into the employee’s personal accounts—creating an automatic savings option for the employee.

Technically, only employees are permitted to contribute to these plans, but some employers increase employee pay, then deduct it and remit it to the employee’s RRSP account. A downside for the employer in doing the latter is that even though the extra pay is tax-deductible, the pay increase leads to higher employee earnings and, therefore, higher payroll taxes (e.g., CPP/QPP contributions, employment insurance premiums and workers’ compensation premiums). In some jurisdictions, it also results in higher health insurance premiums. RRPs are not subject to minimum pension laws—only tax laws.

Although contributions are not locked in, an employer may place limits on withdrawals from an RRSP as long as an employee remains employed. Employers cannot, however, restrict employee access once the worker retires or the worker’s employment is terminated.

- **Deferred Profit-Sharing Plans (DPSPs)** allow employers to set aside a portion of company profits for the benefit of employees. Contributions can be suspended in unprofitable years. Like RRSPs, they provide an alternative to RPPs and can be set up for an individual or group of individuals. Only employers may contribute to a DPSP, and the funds put in an account must be paid out of profits (which includes retained earnings from prior years). To avoid an increase in payroll tax, employers often treat a DPSP as a Group RRSP. Like RRSPs, minimum standards do not apply, but tax laws do, with the same rules concerning taxation of returns on funds and employee access to funds.

- **Pooled Registered Pension Plans (PRPPs)—introduced by the federal government in 2012—are a defined contribution savings option available to the self-employed and employees of federal companies that do not offer occupational pension programs. Some provinces have introduced similar rules for provincial undertakings. Employees are automatically enrolled in PRPPs. The attraction of these plans to employers is that they are involved only to the extent they select a PRPP provider and make payroll deductions. Employers have no legal liability and almost no responsibility for managing the plans beyond making the payroll deductions. Interest and other returns accumulated on the funds in a plan are also not taxed, but withdrawals are subject to income tax.

Employer and employee contributions to all of the above non-DB plans are combined and tax-deductible to the extent total contributions do not exceed 18% of earned incomes up to about $125,000 per annum.

- **Tax-Free Savings Accounts (TFSA)** are a relatively new option that may be set up by an individual or for a group of employees. In contrast to the previous workplace options, TFSA are used for after-tax contributions. Funds in these accounts accumulate tax-free, and no tax must be paid when withdrawals are made. TFSA have a separate contribution limit, which is indexed annually.

Technically, as with RRSPs, only employees can contribute to a TFSA, and the ITA sets limits on the amount—The annual limit is indexed to inflation. However, employers can skirt this rule if they are willing to accept the financial downsides of doing so.

Low-income persons have found TFSA a smart choice because funds can be used for purchases such as a home or cars as well as retirement. Any funds withdrawn from a TFSA can be recontributed in a future year, whereas RRSP withdrawals cannot. Finally, earnings from a TFSA don’t affect income-tested government benefits such as OAS and GIS.
Taking all of these factors into consideration, Statistics Canada estimates slightly more than 20% of Q3 and Q4 households have “dangerously low” net replacement rates. Overall, 10% of Q1 through Q4 households are “seriously at risk.”

In recent months, conflicting viewpoints have appeared as to whether middle-income Canadians are at risk with respect to their retirement savings.

A recent report by the C.D. Howe Institute questions the Statistics Canada conclusion that middle-class workers are saving too little for retirement. The author of the report, Malcolm Hamilton, challenges two key assumptions in the Statistics Canada analysis. He claims:

1. The method used to calculate household savings in the analysis is a poor measure of retirement savings.
2. Few middle-income Canadians need to replace even 70% of their employment income to maintain their preretirement lifestyle.

At Canada’s 2015 Public Policy Forum on retirement security attended by leaders across the public, private, labour and academic sectors, there was agreement that a significant number of middle-income workers are not saving and are most at risk. Concern was also expressed that younger Canadians working in the public sector are also not saving enough. In the report published by this group, the proportion of Canadians at risk was 25% to 30%—a bit higher than in the previous study.

IV—Personal Savings.
RRSPs and TFSAs set up by individuals outside the workplace are part of this final pillar. Other assets in this category that can help ensure retirement security include equity in a home, a business or real estate. Some of these assets enjoy a tax-sheltered status, for example:

- RRSPs and TFSAs set up by individuals are given the same tax advantages as those available through an employer.
- Capital gains on stocks and real estate are taxed at half a person’s marginal tax rate. The capital gain on a principal residence is not taxable. Moreover, there is a lifetime capital gains exemption indexed for inflation ($813,600 in 2015).
- While investors must pay their full marginal tax rate on stock dividends—and 125% of dividends are taxable—national and provincial tax credits offset this liability and yield a significantly lower tax rate.
II. Reasons for Eroding Confidence

The lack of confidence that Canadians express with respect to retirement income security may be attributable to a confluence of factors. For some, there has been erosion in the pillars representing government and workplace plans. At the same time, households that must increase their personal savings to make up for these declines are not doing so. In fact, many have done the opposite—incurring more debt. Compounding these influences is a lack of understanding of how much is required for a secure retirement and the broad range of retirement income support mechanisms that are available to Canadians. While some factors are within the control of workers, others are not.

Demographics

When Canada’s modern retirement system was established in the 1950s, there were eight working-age adults for every senior citizen. Between 1970 and 2013, the ratio declined from 7.8 to 4.5. By the late 2050s, when most of those in Generation X and many of those in Generation Y are also expected to be out of the workforce, this ratio is predicted to fall to 2.3. A shrinking number of workers is supporting benefits for a growing pool of retirees—An increasing share of federal government spending will be devoted to public pensions and health care costs. The aging of Canada’s population can be attributed to dramatic shifts in two key factors: (1) birth rates and (2) life expectancy.

Changing Birth Rates

As World War II ended and economic conditions improved, North America experienced a 20-year bulge in population called the baby boom. In their heyday, boomers were an unprecedented economic force, pushing up rates of homeownership, consumer spending and employment. It’s no coincidence that the labour force participation rate in Canada hit a record high in the late 1980s when those born between 1946 and 1964 had all reached ages where they could enter the labor force. As those in the baby boom generation reached adulthood, women gained access to better methods of birth control and entered the workforce in greater numbers. Furthermore, people started to marry at a later age and wait longer to have children. The result among boomers was a drop in the birth rate that created the "baby bust," or Generation X. Born around the period spanning 1966 to 1985, Generation X was greeted by high unemployment and discouraging income levels. They had no incentive to increase the birth rate per family. There was, however, a baby boom "echo"—an increase in babies born to the large number of boomer children that followed in the 1980s through the early 2000s.

Just as the “echo boomer,” referred to as Generation Y or Millennials, are entering their prime working years, baby boomers are retiring. In 2011, the first of the baby boomers reached age 65—the traditional retirement age. The large number of persons who will retire in the relatively short period that follows will be unprecedented before flattening out by about 2030. Not long after, another peak will occur as the oldest of Generation Y begin entering retirement years. Canada’s population balance is going to continue shifting over the next several decades.

Longer Lifespans

During the previous century, life expectancy rose dramatically amongst the world’s wealthiest populations, from around 50 to over 75 years. This trend is expected to continue during the 21st century—although at a slower pace. Canadian men who reached age 65 by 2013 are expected to have an average of 20.9 additional years—a life expectancy of about 85.9 years. Women who reached the same age that year can expect another 23.3 years on average, or a life expectancy of about 88.3 years.
**Economic Events and Trends**

As if demographics weren’t problem enough, market shocks and broad economic trends have heightened retirement income concerns. The 2008 financial crisis in combination with the Great Recession provides an example of how market downturns can affect retirement security.

**Decline in Investment Returns**

When the 2008 global financial crisis hit, central banks around the world cut interest rates to record lows to stop the economic free fall—punishing those who had bonds and other fixed income investments paying interest. Falling interest rates also increased the cost of annuities and adversely affected the valuation of defined benefit liabilities.

Those who had investments in equities were socked even harder. Between the second quarter of 2008 and the first quarter of 2009, the Toronto Stock Exchange (TSX) composite index fell 51%. Over the same period, home prices fell by 5.9%. It is estimated these and other asset price changes reduced the average wealth of Canadian families by 10.7% and average retirement assets by 14.3%. The same analysis suggests defined contribution (DC) plans probably lost 27.0% of their value and registered retirement assets dropped 26.3%.\(^{18}\)

Despite the recovery of stock prices, investment returns overall have not recovered. It is anticipated future returns will be lower in both *nominal* (before inflation) and *real* (after inflation) terms. Total investment returns are predicted to average 5.5% to 6% over the next quarter century—compared with the 8.2% delivered by the median Canadian pension fund manager since 1960.\(^{19}\) At present, low rates of inflation reduce the impact of this gap, but there is no guarantee this will continue.

Investor confidence is compounding the lower investment returns in individual retirement accounts. Shaken by the stock market volatility that occurred during the Great Recession, many individual investors shifted from stocks to fixed income products with lower, safer returns. This adversity to risk continues—More than half (53%) of employees in AEGON’s 2013 global survey agreed that as a result of the financial crisis, they “will take fewer risks when it comes to saving for retirement.”\(^{20}\)

While there is nothing wrong with a conservative approach to investing—and investors are often well-advised to reduce equity exposure as they approach retirement—abandoning equities can seriously shrink the amount and duration of a worker’s retirement income. Despite the higher investment risk, stocks provide yield in the long term that can help offset the risk of inflation.

**Rising Health Care Costs**

From 1975 to 2010, Canada’s expenditures on health care rose from 7% to nearly 12% of GDP.\(^{21}\) Given Canada’s current tax structure, little room exists for increased taxation to cover future increases. If costs continue to rise, there is the possibility there will be more cost shifting from government to individuals for some health products and services (e.g., provincial prescription drug plans, living assistance care and nursing home care). While this will probably have minimal effect on low-income persons, those with the ability to pay may have to pay more—especially for services not traditionally covered by the public health care system. While not all of these services are specifically for the elderly, the use of these services is primarily among the elderly as their health declines with age.

**Shifting Family Responsibilities**

Longer lifespans coupled with a weak economy have changed the game plan for many preretirees and retirees. In a BMO Nesbitt Burns survey of Canadians aged 45 to 64, almost one-third reported they were currently caring for a parent or older relative. More than half (55%) were caring for their children, aging relatives or both. Almost one in two say they fear caring for others will impact their ability to meet key financial goals, including saving for retirement.\(^{22}\)
Eroding Retirement Income Benefits From Government

Near the end of the 20th century, as baby boomers moved closer to retirement, government officials began to look at how people living longer and having fewer children would affect the financial sustainability of Old Age Security (OAS), the Canadian Pension Plan (CPP) and the Québec Pension Plan (QPP). Given public opposition to higher taxes and concern regarding the growing costs of these programs, it didn't take long to realize a challenge was looming as to the capacity of these programs to deliver the retirement benefits promised. In 1996, the federal government began to implement a strategy for CPP that was proposed by Québec:

- A separate reserve fund was created to support future benefit payments.
- Various benefit cuts were made.
- Over a six-year period, the CPP contribution rate was raised from 5.85% to 9.9% of contributory earnings (contributions to the QPP rose to 10.35%).
- The base level of income exempted from contributions was frozen—Previously, the base level of income had been inflation-adjusted.

### Table I | Canada’s Government Retirement Programs 2015

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<tr>
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</table>

Source: Canada Revenue Agency/Régie des rentes du Québec.
Adjustments are being made to the benefits paid when a worker retires before or after the age of 65. Prior to 2012, CPP retirement benefits were reduced by 6% per year (0.5% per month) for each year below 65 (to age 60) that a contributor applied for a pension. Between 2012 and 2016, this reduction increases gradually to 7.2% per year (0.6% per month). Benefits are being increased by 8.4% per year (0.7% per month) for each year above age 65 (to age 70) that a contributor delays applying for a pension. This change does not apply to contributors who began receiving a CPP retirement pension before December 31, 2010 and remain out of the workforce.

Individuals can start their CPP at any age after age 60, but they are required to contribute to CPP and earn a post-retirement benefit if they continue to work and are under the ages of 65. Employers are also required to contribute. Between age 65 and 70, workers have the option to waive contributions to CPP; if they continue to contribute, their employer must also contribute. Table I offers additional details of Canada’s retirement income security programs as they now stand and what changes remain.

Between January 1, 2014 and 2016, the monthly benefit reduction for retirement prior to age 65 increases to 0.6% per month. Conversely, those who begin receipt of QPP benefits after their 65th birthday have their payment increased by 0.7%. This adjustment has been in effect since 2013.

### Limited Access to Workplace Pension Plans

For middle- and upper-income workers, Pillar III—workplace pension plans—is essential to filling the void between the income they will receive from government (Pillars I and II) and what they will need to maintain their level of living in their postwork years. Today, less than 40% of Canadian employees have access to an employment pension plan. Such plans include defined benefit plans, defined contribution plans, hybrid plans and other composite or combination plans. Of the workforce as a whole (including the self-employed), only one in three is covered by a workplace pension plan. Among working-age Canadians irrespective of their work status, coverage is just 25%. In a 2014 Conference Board of Canada survey, 39% of persons currently employed reported they did not have a retirement savings plan or pension plan through their current employer. While coverage is relatively common if a worker is employed by government, this is not the case for those in the private and the not-for-profit sectors.
Shift Away From Workplace Defined Benefit Plans

By the mid-20th century, defined benefit (DB) plans became the dominant model among workplace pension plans. Sponsors of DB plans guarantee members a predetermined benefit typically based on an employee’s service and/or pay for the employee’s lifetime and, unless the member and spouse waive the option, the lifetime of the employee’s spouse. In recent years, these workplace plans have been giving way to defined contribution (DC) plans and other approaches to retirement benefits that transfer greater financial risk and responsibility from employers to plan members.

While DB plans continue to be available, DC plans, target benefit plans (TBPs) and other options are now playing an increased role in the retirement security of Canadian workers. Of those workers who had a registered retirement plan (RRP) at the end of 2013, 71% were enrolled in a DB plan, while DC plans accounted for 17%. The remainder were hybrid or composite plans. For additional information concerning target benefit plans, see Exhibit 3 on page 17.

Looking at the DB coverage for private versus public sector employees with an RPP, striking differences are revealed. In 2011, of those in the public sector with an RPP, 94% were in a DB plan—a 5% decline from the 99% coverage in 1974. During the same period, the proportion of workers in the private sector with DB coverage through an RPP dropped by more than a third, from 88% to 52%. Hence, a substantial portion of the shift away from DB plans in the workplace can be attributed to a decline in DB coverage among private sector workers.

In its 2014 employer survey, the Conference Board of Canada asked those who provide RPPs as well as other pension schemes what type(s) they provide (Table II). Among public sector employers, DB plans are most common (89%), followed by supplemental employee retirement plans (47%) and DC plans (38%). In the private sector, 74% of employers offered Group RRSPs, and 54% had DC plans, with DB plans coming in third with 45%. One-third (33%) of private sector plans offered a supplemental employee retirement plan.

With DC plans, an employee receives a lump sum of money at retirement that varies with factors such as the contributions made on behalf of the employee, the number of years contributions are made and investment earnings (or losses). When compared with DB plans, there are essentially four fundamental ways that DC plans generally differ—These same characteristics are also common among RRSPs and other capital accumulation plans.

1. Employers contribute less than they do to a DB plan.
2. Employees have greater responsibility for planning and managing their retirement resources.
3. Investment, inflation and longevity risk are transferred to employees.
4. Higher management fees and lower risk strategies when there are self-directed individual accounts reduce the return on plan investments.

The bottom line in this shift from DB to DC plans is greater risk and responsibility placed on the shoulders of workers combined with lower investment returns.

More Cost Sharing With Workers

Among employers offering a retirement plan to their employees, the majority (97%) contribute to the plan. However, the amount they contribute varies with the plan. The average contribution for those providing a DB plan is 10.5% of pensionable earnings, compared with 5.9% for DC plans and 4.6% for Group RRSP plans. Employee contributions must fill the gap.

Increased Employee Responsibility for Account Management

While DB plans promise a guaranteed retirement income for life, DC plan members are faced with choices that can significantly affect their retirement security. Workers with DC plans must figure out how much they must save and, if the plan is self-directed, how they will invest these savings to achieve a comfortable retirement. Upon retirement, members must choose between making lifetime withdrawals following the minimums/maximums established by government or purchasing an annuity paying a set monthly amount for life. The menu of decumulation choices they have to choose from is often influenced by the account types they used to save for their retirement.
When making these decisions, individuals must try to forecast their lifetime earnings, their health before and after retirement, how long they will be retired, expenses during retirement, investment returns, inflation, etc. The younger the worker, the further he or she must look into the future and the more difficult it is to make such predictions. Even the best financial planner finds predicting these factors a challenge.

Planning becomes even more complicated when an individual has multiple retirement benefit plans. In addition to government pension plans, a retiree may have plans from current as well as previous employers as well as personal savings. There may be a combination of DB and DC plans. Those who are married may be eligible for some of the benefits for which their spouse is eligible. Furthermore, some combinations of plans result in benefit reductions (offsets) from other plans. For example, RRSP payments reduce benefits otherwise payable under OAS and GIS.

### Table II | Workplace Pension Plan Prevalence

<table>
<thead>
<tr>
<th>Plan Type</th>
<th>Private Sector (%)</th>
<th>Public Sector (%)</th>
<th>All Employers (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defined benefit (DB) plan</td>
<td>45</td>
<td>89</td>
<td>56</td>
</tr>
<tr>
<td>Group Registered Retirement Savings Plan (RRSP)</td>
<td>74</td>
<td>29</td>
<td>63</td>
</tr>
<tr>
<td>Defined contribution (DC) plan</td>
<td>54</td>
<td>38</td>
<td>50</td>
</tr>
<tr>
<td>Supplemental employee retirement plan (SERP)</td>
<td>33</td>
<td>47</td>
<td>36</td>
</tr>
<tr>
<td>Tax-Free Savings Account (TFSA)</td>
<td>18</td>
<td>9</td>
<td>16</td>
</tr>
<tr>
<td>Deferred Profit-Sharing Plan (DPSP)</td>
<td>16</td>
<td>0</td>
<td>12</td>
</tr>
<tr>
<td>Hybrid pension plan</td>
<td>12</td>
<td>0</td>
<td>9</td>
</tr>
<tr>
<td>Employee profit-sharing plan</td>
<td>10</td>
<td>0</td>
<td>8</td>
</tr>
<tr>
<td>Savings plan</td>
<td>4</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Target benefit plan (TBP)</td>
<td>2</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>Share purchase plan</td>
<td>2</td>
<td>0</td>
<td>1</td>
</tr>
</tbody>
</table>

Risk Transfers

The shift from DB to DC plans with individual investment accounts also transfers risks from employers to employees. To understand the implications, consider the following examples:

- **Investment return risk** is the chance the return on an investment will be less than expected. Since 1987, there have been four major market downturns. It is not unreasonable to expect more downturns in the future. If a DB plan experiences a return less than anticipated, a change in investment strategies or a market recovery usually corrects the plan’s funding shortage. In a worst-case scenario, the employer and, possibly, plan members, must make additional contributions to the plan. Regardless, the retiree usually receives the income stream promised by the plan.

  In contrast, DC plan members absorb all of the investment risk and its consequences. If the assets chosen by a worker perform poorly, the money available during retirement will be less. One or two bad years—especially in the early years of retirement—can have a major impact on how long savings will last. The market downturn of 2008 provides an alarming example of what can happen for those on the verge of retirement. Many workers with DC plans had to postpone retirement, take on a postretirement job or resign themselves to living on less during their retirement.

  Even when workers purchase an annuity providing a guaranteed retirement income stream, they face investment risk. The price of an annuity goes up when interest rates go down, which means the cost of purchasing an annuity is elevated in periods with low interest rates. More money is required to generate the same retirement payments.

- **Inflation risk** is the possibility the rising cost of goods and services will erode the value of retiree benefits and savings. When a DB benefits formula is based on a worker’s most recent years of earnings, there is at least some built-in inflation protection because earnings over time tend to reflect inflation. Some DB plans go further and adjust payments after retirement to reflect price increases. DC members have no such protection.

- **Longevity risk** is the chance a retiree will outlive his or her retirement savings. Individuals do not know how long they will live or how long they will need to rely on their retirement savings. DB plans provide a guarantee that a retiree will receive an income for life. Given improvements in life expectancies, the money set aside for retirement may need to last a long time—potentially 20 to 30 years or more. Unless they buy an annuity, retirees with DC plans must try to estimate how long they (and possibly their spouse) will live, then manage their money so it will not run out before they die. They cannot use the mortality tables used by DB plans to reflect average or pooled life expectancies. Instead, risk-adverse DC plan members must assume they will live to the longest age possible.

- **Judgment risk** reflects the possibility a plan member makes an error or poor choice concerning his or her retirement resources. When it comes to figuring out how much to save for retirement, most DC members are on their own. Moreover, once they stop working, they must manage their personal nest eggs so they have enough money to last their remaining years. In contrast to DB plan administrators, DC members rarely have a cadre of professionals (e.g., lawyers, investment managers, benefit consultants) guiding them in making plan choices. Making the right choices can determine whether members are able to experience a stress-free retirement and, if they wish, pass assets to others as part of an estate.

  Add to this the possibility a retiree may reach a point when he or she is no longer able, mentally or physically, to manage his or her assets. Judgment risk is heightened by some investment advisors and scam artists who are focused on personal gain versus the best interests of the person they are advising.
Exhibit 3 | Target Benefit Plans

Four Canadian provinces (Alberta, British Columbia, Nova Scotia and Ontario) have recently enabled legislation providing a framework for target benefit plans (TBPs) in each of their jurisdictions. In addition, Québec has amended its pension law to allow TBPs. The specific definition of a TBP varies by jurisdiction. These pension programs are similar to DB plans in that there is a pooling of investments and longevity risk, but three other features of TBPs set them apart from DB plans.

1. TBP contribution rates for both employers and employees are fixed and clearly defined. The rates are based on the amount needed to accumulate sufficient funds (at an assumed interest rate) to pay a projected future benefit—the target benefit—to plan members upon retirement. Unlike with a DB plan, there is no automatic adjustment in employer contributions when a TBP has a funding shortfall.

2. If TBP assets are not sufficient to support the target benefit level and employers/employees are unwilling to contribute more to the plan, accrued benefits can be reduced. The obligation of the plan is only to pay whatever benefit can be provided given plan funding. Before reducing accrued benefits, however, there are a number of actions that may be taken:
   - Increase contributions
   - Decrease future benefits
   - Reduce ancillary benefits such as indexing and early retirement benefits.

   Of course, if there is a surplus, a plan can use some of the money to improve benefits. Plans may set out in advance how surpluses and shortfalls are eliminated.

3. Members are involved in the governance of the plan. Since members assume all (or almost all) of the risk of a TBP, it seems appropriate that they should be involved in plan governance.

While the potential for reductions in benefits introduces a degree of uncertainty for plan members, it is not near the level of uncertainty that exists with a DC arrangement, and it provides a steady stream of income like a DB plan.
Lower Investment Returns

Studies of investment returns consistently have found that returns earned by DB plans exceed those earned by individual DC accounts. DB plans have a larger pool of funds to invest, which means they are able to diversify investments among a multitude of asset classes, including some not available to individual investors. DB plans also have a longer investment time frame and can be fully diversified both before and after the retirement of a specific member. These factors yield a broader base upon which to spread risk and make it possible for DB plans to choose investment strategies with higher risk but also the potential for higher returns. Furthermore, DB plans are more likely to have professional money managers who are more knowledgeable in achieving investment goals and who avoid many common investment biases. As for the cost of using professional managers, the management fees associated with DB plans tend to be lower than those associated with DC plans, at least partly because of the volume of assets under management. TBPs are able to take advantage of the same economies of scale as DB plans.

A recent study confirms much of what has just been stated. Overall, DB plans delivered the same retirement savings as DC accounts at a 48% lower cost.

- DB pension longevity risk pooling generates a 10% cost savings.
- The DB balanced portfolio feature generates an 11% cost savings.
- The lower fees and higher returns of DB plans yield a 27% cost savings.

Inadequate Retirement Savings

As stated earlier in this report, government programs are succeeding in providing retirement security to low-income households. These programs do not, however, provide sufficient retirement income replacement for middle- and higher income households. A consensus appears to have developed that some middle-income households and young Canadian workers in the private sector are not saving sufficiently and are disproportionately at risk of having a declining level of living in their postwork years. For a look at why many workers aren’t saving more for retirement, see Exhibit 4.

Higher Mortgage and Consumer Debt

Using credit to make purchases—especially large purchases such as a home and education—can be an extremely valuable tool when used responsibly. However, debt accumulation can also hinder retirement security. Over the years and particularly in the last decade, Canadians have been accumulating debt twice as fast as their incomes have grown. Nearly half (42%) of those age 65 and younger identify paying down debt as a priority over saving for retirement. Much of this debt is driven by mortgages—43% of Canadian preretirees are carrying a mortgage.

What gets less attention is the amount of debt being carried into retirement. It used to be that retirement freedom meant more than not having to go to work; it also meant no mortgage and other debt payments. For many, this is no longer the case, as almost one in five persons expect to carry their mortgage into retirement. According to a 2013 Harris/Decima poll, 59% of Canadian retirees are carrying debt. Among this group, 19% said the amount of their debt had increased in the previous year, while another 36% said their debt level during the same period had stayed the same—indicating more than half (55%) of all retired Canadians were unable to pay down their debt in the 12 months prior.
Exhibit 4 | Why Workers Aren’t Saving More

For some low-income Canadians, saving for retirement is challenging if not impossible. In fact, saving is probably not a good idea. When they retire, any money they have managed to save will result in reduced OAS and GIS benefits. Nevertheless, what about those persons who should be setting aside some funds for their retirement? They say they know they need to save for retirement, but they don’t. Why aren’t they saving?

What Workers Say

No statistics have been found that examine specifically why middle-income Canadian workers are not saving enough to achieve a secure retirement, but there are statistics from Canadians in general that provide some insight. Among Canadians who are not fully retired, 67% say money to invest is an obstacle to saving for retirement. As for younger persons, they face financial challenges that older generations did not worry about. When TD Canada asked those of the baby boom generation and Generation Y what they considered barriers to their ability to save in their 20s, these responses were given:

- Paying for education costs (44% of Gen Y versus 18% of boomers)
- Salaries too low to cover living expenses (39% of Gen Y versus 30% of boomers)
- Debts from credit cards, loans and lines of credit (38% of Gen Y versus 26% of boomers)
- The temptation to shop beyond their means (36% of Gen Y versus 16% of boomers).

What Behavioural Economists Say

A 2010 ING survey of plan members in the United States suggests the reasons people do not save more is more complex than the lack of money claimed. A stunning 87% of plan members who were not contributing the maximum to their employer-sponsored plan admitted they could afford to increase their annual contribution by 1% of their salary. In fact, 59% confessed they could boost their contributions by 3%, and 32% felt they could afford an extra 5%. What explains this contradiction? In recent years, behavioural economists have been trying to find an answer. They are learning the reason people don’t save for retirement is about more than whether they can afford to do so—People’s emotions are involved. The findings of behavioural economists suggest many workers may have some financial flexibility but are not using it. Two human behaviours are in play.

1. Future discounting. People have a tendency to focus on the short term versus the long term. Given a choice, they are more likely to buy something for today or set aside money for a vacation in a few months rather than save for retirement. The short-term purchases are more tangible—It is easier to envision the benefits of the immediate purchase over something decades away. The more time a person has until he or she retires, the less influence retirement has on decisions today.

2. Inertia and procrastination. Stop and think about it—People who delay enrolling in their retirement plan are making a choice. They are choosing to do nothing. Failing to do something (inertia) and putting off doing it (procrastination) impede even when people know it would be in their best interest to do something. Not only do people fail to enrol in their retirement plan, they don’t take the time to assess how much they will need to achieve a secure retirement. Inertia and procrastination are also the reasons many people fail to increase the amount they are saving and to rebalance the assets in their investment portfolios. Lack of knowledge combined with the complexity of the retirement planning process are viewed as the roots of these behaviours. Many individuals perceive the process of participating in a retirement plan—especially a DC plan—as tedious, time-consuming, confusing and overwhelming.
Leakage

During difficult times, workers sometimes turn to their retirement funds to pay pressing short-term expenses. While money cannot be withdrawn from workplace DB and DC plans unless there is a severe financial hardship or shortened life expectancy, other types of retirement vehicles (e.g., RRSPs) do allow funds to be withdrawn.

In a Scotiabank poll, about one-third of RRSP holders (36%) reported they took money out of their RRSP account in 2012, up from 23% in 2005. Moreover, the average amount withdrawn in 2012 was $24,531—more than double the $10,716 cashed out in 2005.41

According to the same poll (Table III), buying a first home is the primary reason people withdraw funds from an RRSP (40%); another 4% withdrew the money for educational expenses. Withdrawals for these purposes are not necessarily a bad idea—unless borrowers fail to pay back the money borrowed within the period set by the Homebuyers’ Plan and Lifelong Learning Plan. Money not paid back under these programs and withdrawals from RRSPs for other purposes result in taxable income and a reduction in the amount these borrowers can contribute to RRSPs in the future. The No. 2 reason people withdraw these funds is to pay down debt (16%). Of special concern is leakage when individuals make withdrawals for unnecessary expenses such as paying for a vacation (6%).42

Table III | Reasons People Withdraw RRSP Funds

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buy a first home</td>
<td>40%</td>
</tr>
<tr>
<td>Pay down debt</td>
<td>16%</td>
</tr>
<tr>
<td>Convert to RRIF</td>
<td>15%</td>
</tr>
<tr>
<td>Cover day-to-day expenses</td>
<td>14%</td>
</tr>
<tr>
<td>Home renovations</td>
<td>8%</td>
</tr>
<tr>
<td>Vacations</td>
<td>6%</td>
</tr>
<tr>
<td>Education</td>
<td>4%</td>
</tr>
<tr>
<td>Medical</td>
<td>3%</td>
</tr>
</tbody>
</table>


In a Scotiabank poll, about one-third of RRSP holders (36%) reported they took money out of their RRSP account in 2012, up from 23% in 2005.
Worker Failure to Plan

An essential element in preparing for retirement is simply having a plan. In fact, research indicates persons who have planned for their retirement have greater confidence they will be able to retire when they want to do so.43 For more details on how planning affects savings, see Exhibit 5. Even those who have thought just a little about retirement hold substantially more wealth than those who haven’t thought at all about life after work.44

Given the effort and uncertainty involved, it is not surprising that few workers have enthusiastically embraced the retirement planning process. In AEGON’s 2014 global survey of employees (excluding the self-employed), not quite two-thirds (61%) of Canadian workers reported they had some type of plan (Figure 4).45 An even lower proportion (41%) of individuals responding to a 2014 Conference Board of Canada survey said they had a plan. Just one-third (35.5%) of the respondents in this second survey reported they know how much income they would need in retirement.46

Exhibit 5 | The Retirement Planning Premium

People who take the time to develop a financial plan for their future retirement experience a “planning premium”—more savings. An HSBC study found that 41% of Canadians who say they have a financial plan report they increased their savings. Of those who used a professional advisor for planning, 57% saved more. The proportion saving more increased to 64% among those who consulted with a financial planner and prepared a written plan. The planning premium is slightly weaker among those nearing retirement—persons who were 55 to 64 years old.47 In a study of U.S. workers, it was found that those who plan saved more at almost all income levels.48

Figure 4 | Workers With a Retirement Plan*

Retirement and life in general are full of uncertainties. Failing to plan for the unexpected can blindside retirees during what are supposed to be their golden years. The Society of Actuaries asked individuals in the United States whether they had considered how they would respond to a number of major life changes that might occur in retirement such as losing a spouse or no longer being able to do certain activities (Table IV). Few had made plans for how they would respond in these scenarios. Only 23% of married preretirees had considered and made plans for the death of their spouse or partner. Even after retirement, the proportion that had planned for such a scenario was relatively small at 31%. The percentages planning for declines in the ability to do routine physical and mental activities were no better and, frequently, less common.49

<table>
<thead>
<tr>
<th>Table IV</th>
<th>Planned for Changes in Retirement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Considered, and Made Plans</td>
</tr>
<tr>
<td>You lost your spouse/partner</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>23%</td>
</tr>
<tr>
<td>Retirees</td>
<td>31%</td>
</tr>
<tr>
<td>You were physically no longer able to work</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>15%</td>
</tr>
<tr>
<td>Retirees</td>
<td>29%</td>
</tr>
<tr>
<td>You were less able to move around</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>10%</td>
</tr>
<tr>
<td>Retirees</td>
<td>24%</td>
</tr>
<tr>
<td>You were less able to manage your money</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>15%</td>
</tr>
<tr>
<td>Retirees</td>
<td>31%</td>
</tr>
<tr>
<td>You were less able to do household chores</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>10%</td>
</tr>
<tr>
<td>Retirees</td>
<td>23%</td>
</tr>
<tr>
<td>You were mentally no longer able to work</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>9%</td>
</tr>
<tr>
<td>Retirees</td>
<td>20%</td>
</tr>
<tr>
<td>You were no longer able to drive</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>9%</td>
</tr>
<tr>
<td>Retirees</td>
<td>19%</td>
</tr>
<tr>
<td>You were less able to provide caregiving</td>
<td></td>
</tr>
<tr>
<td>Preretirees</td>
<td>9%</td>
</tr>
<tr>
<td>Retirees</td>
<td>18%</td>
</tr>
</tbody>
</table>


Unrealistic Expectations

One reason individuals do not have contingency plans for their retirement is very likely unrealistic expectations regarding their working lives and retirement. Physical and mental decline are inevitable consequences of aging, yet many individuals do not believe things will happen to them. In a survey of U.S. preretirees and retirees, sizable percentages of both groups say they will never become:

- Less able to manage their money (38% and 54%)
- Mentally unable to work (34% and 46%)
- Unable to drive (19% and 33%)
- Less able to provide caregiving (15% and 30%)
- Less able to do household chores (18% and 28%).

In addition, 23% of married preretirees and 32% of married retirees report they will never lose their spouse.50
Retirement and Work After Retirement May Not Be as Planned

The age a person plans to stop working is a critical factor in retirement planning. The longer a person remains in the workforce, the more savings he or she will be able to accumulate. Delaying retirement a few years can significantly affect retirement income from government and DB plans. Regrettably, retirement timing is not always within a worker’s control.

When Canadian workers were asked when they expected to retire (Table V), 41% said they didn’t plan to do so until age 65 or older. A very small proportion (2%) said they were never planning to retire.51

For those who plan to retire, many say they will not be taking the “cliff edge” approach of stopping work altogether. In a CIBC online poll, slightly more than half (53%) of workers in their 50s said they plan to keep working after they retire in their 60s.

A 2014 survey of retirees suggests workers may be overly optimistic regarding how long they will work. Almost three-fifths (58%) report they retired earlier than planned. Of these early retirees, 43% retired because of their own ill health, 17% cited a job loss/unemployment and 12% identified family responsibilities such as becoming a caregiver as a cause.53

Underestimating the Number of Retirement Years

For middle-income persons who will need savings to close the gap between government benefits and, perhaps, a workplace plan to achieve a secure retirement, predicting the number of years they will need a retirement income is as important as deciding when they will retire. How long a person lives after retirement can add significantly to a retiree’s resource needs, but many individuals underestimate their longevity.

A common error is to use one’s average life expectancy at birth and to give little attention to the substantial probability one might live longer. People don’t realize that as they get older, their life expectancy increases. For both genders, life expectancy is at least 20 years longer at age 65 than at birth.54

In one study of U.S. preretirees, 46% thought they would not live as long as the average person their age and gender. Interestingly, even those who reported knowing (or having known) a family member who lived over 90 years expected to not live as long as this oldest living family member.55 There is also evidence that a sizable number of preretirees and retirees don’t know how long they can expect to live.56

Table V | Expected Retirement Age

<table>
<thead>
<tr>
<th>Retirement Age</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under age 65</td>
<td>53%</td>
</tr>
<tr>
<td>Younger than 55</td>
<td>4%</td>
</tr>
<tr>
<td>55 to 59</td>
<td>21%</td>
</tr>
<tr>
<td>60 to 61</td>
<td>16%</td>
</tr>
<tr>
<td>62 to 64</td>
<td>12%</td>
</tr>
<tr>
<td>65</td>
<td>24%</td>
</tr>
<tr>
<td>Over age 65</td>
<td>17%</td>
</tr>
<tr>
<td>66 to 69</td>
<td>10%</td>
</tr>
<tr>
<td>70+</td>
<td>5%</td>
</tr>
<tr>
<td>Never retire</td>
<td>2%</td>
</tr>
<tr>
<td>Don’t know</td>
<td>6%</td>
</tr>
</tbody>
</table>

Failing to Consider Inflation

Once someone starts receiving CPP, QPP, OAS and GIS cheques, the recipient benefit amounts automatically increase with changes in the Consumer Price Index to keep pace with inflation. It may be a surprise to some, however, that this does not ensure a steady income replacement rate after retirement. Since 1960, wage inflation has surpassed price inflation by 1% annually on average. Consider OAS benefits. Assuming this trend continues with average wages continuing to surpass prices by 1% for the next 25 years, the OAS benefit will fall from about 12.5% of the national average wage to about 10%.57

As for most private pensions and annuities, payments from these sources are not adjusted for inflation or are only partly adjusted. With no adjustment, inflation of just 3% annually could reduce by half the real value of benefits in 23 years.

A majority of current retirees (69%) say lifestyle adjustments are how they will cope with inflation.58 This may not be as easy as they think as they move into the second and third phases of retirement. The services they need later in retirement may not be as easy to adjust, and there will probably be fewer lifestyle options to change.

Underestimating the Cost of Health Care and Long-Term Care

It is estimated at least 40% of Canadians over age 65 will need some form of long-term health care services.59 A major benefit for Canadian retirees is the publicly funded health care systems that include some subsidies for long-term health care services. However, individuals who wish to supplement or replace public sources with private care will find the cost varies widely depending on the type of care, the type of room and how much government funding is available in the province providing care; for example:

- The hourly rate for homemaking, personal care or nursing care ranges from $10 to $200.
- A stay in a long-term care facility can cost from $1,000 to over $3,000 per month.
- Private facilities range from $2,500 to more than $7,000 per month per person.60

Setting Unsustainable Rates of Withdrawals

Upon retirement, individuals face the daunting task of managing their money so that it provides for their remaining years. A sustainable withdrawal rate—one that offers retirees a high probability of making their savings last for life—has been the subject of considerable analysis and debate. Traditionally, analysts suggested a 4% or 4.5% withdrawal of retirement savings per year. A more conservative approach encouraged workers to target a 3% or 3.5% withdrawal rate.61 Recently, a balanced portfolio of stocks and bonds has achieved an average rate of 2.2% after inflation—less than half the historical rate. If this holds true, a safe starting point for drawdowns will be less—perhaps 3%.62

Financial Illiteracy

For many Canadians, achieving retirement security requires a grasp of concepts such as inflation and the time value of money along with the basic principles of investing. Also essential are abilities such as making mathematical calculations and managing several forms of risk. Unfortunately, studies reveal few individuals have this knowledge. In AEGON’s 2014 survey, only a little more than one-fourth (28%) of Canadian respondents said they were “very able” to understand financial matters related to retirement planning.63

Of course, financial literacy encompasses a wide array of subjects that goes far beyond financial planning, investment management and retirement benefits. Other topics include debt management, home mortgages, taxes and insurance. Any and all of these can affect a person’s ability to save and achieve a secure retirement.
Among Canadians nearing retirement (aged 55-64), four in five (80%) say they plan to use CPP/QPP and OAS as sources of retirement income, yet 69% did not know what the maximum monthly payouts would be.

**Retirement Benefits**

**Private Workplace Benefits.** When the Conference Board of Canada asked employers whether they felt their employees had a good understanding of their workplace retirement savings and pension plans, only half (51%) felt this was true.64 Employee self-assessments substantiate employer sentiment with more than half (55%) saying they do not know the monthly benefit they can expect from their workplace pension.65 Women, younger workers and those in lower income brackets are significantly more likely to say they understand few or no aspects of their workplace plans.66

Among those with DC plans and other self-directed capital accumulation plans (CAPs), knowledge of an employer retirement plan is especially important. In a 2014 survey of CAP members, however, just 38% reported they had an “excellent” or “very good” understanding of their employee retirement plan—40% claimed a somewhat good understanding. A minority of members also claimed an “excellent” or “very good” understanding of specific aspects such as risk tolerance (40%), their plan statements (37%), asset allocation (31%) and the amount needed to contribute to their plan to retire with the amount of money needed (30%).67

CAP members with a DC plan or group RRSP also say they lack an understanding of the payout options for these plans when they retire. Only 27% said their understanding was “excellent” or “very good.” The same proportion (27%) said they had a “somewhat poor” or “very poor” understanding and 7% had “no” understanding. The remaining 38% said they didn’t know what would happen to their savings when they retire.68

**Public Benefits.** Among Canadians nearing retirement (aged 55-64), four in five (80%) say they plan to use CPP/QPP and OAS as sources of retirement income, yet 69% did not know what the maximum monthly payouts would be.69 As with private plans, women, younger persons and those with less income are less likely to know what their future payments will be. Education also seems to be a factor—Persons with lower levels of education reported less knowledge concerning their benefits.70

**General Personal Finance**

Unfortunately, financial literacy of individuals in a broader sense is no better than the literacy associated with retirement. In June 2009, the government of Canada created the Task Force on Financial Literacy to assess the nation’s financial literacy and make recommendations on a national strategy to strengthen financial literacy in Canada. Among the facts disclosed by the Task Force’s 2011 report:

- 82% of Canadians were having difficulty making ends meet.
- 66% had trouble keeping track of their money.
- 61% found planning ahead a challenge.
- 39% struggle to stay informed.71

When individuals are asked to assess their financial literacy, men tend to rate themselves higher than women. Not surprisingly, age and education also play a role. Younger persons rate themselves more poorly than those who are older. Those with higher levels of education are more likely to give themselves relatively positive grades. This said, even 12% of those with a master’s degree and above said their financial literacy was “poor” or “below average.”72

Persons who have the knowledge and skills to manage their personal financial resources in general are more likely to have thought about retirement. They are more likely to use formal planning tools (e.g., attend a retirement seminar, use a calculator/worksheet and consult a financial planner).73 Furthermore, financially literate persons are more likely to invest in stocks and other complex assets that provide a higher return in the long term and set aside more for their future retirement.74
III. Implications of the Retirement Challenges Ahead

With the many factors just noted—some that can be controlled and others that cannot—there is no question there are challenges ahead for Canada and its future retirees. How much any one household will be affected will depend primarily on the resources available to them via the four pillars described at the beginning of this report. Some retirees will have sufficient resources to pay their bills and experience a stress-free life after work. But there is no doubt—unless changes are made—an increasing number of retirees are going to struggle financially. This lack of retirement preparedness promises to have substantial negative consequences for workers and their employers.

Workers
Some workers who move into retirement with insufficient funds to provide the life they envision will be able to cut their living expenses and, perhaps grudgingly, accept that the final years of their life will not be all that they had hoped. There may be children or other family members who will step in and provide assistance in the form of housing, money and so forth. It is predicted many will attempt to close the gap between their retirement income and expenses by working longer. A three-year rise in retirement age increases income replacement ratios by about 10%.75

Older Canadians have already increased their labour force participation and are postponing retirement. In 2013, one in four persons between 65 and 69 years was still in the workplace. This is a marked reversal from a decades-long decline from 15.6% in 1976 to 11.8% in 2000. Even people over age 70 are working at record numbers, with their participation nearly doubling from 3.5% in 2000 to 6.7% in 2013. This increase in labour force participation is expected to continue.76

While some workers view working longer as a positive, this will not be true for everyone. Some who are working will be disappointed they have neither the time nor money to enjoy their later years as they had hoped. Of course, another difficulty is that not all who want to work may be able to do so due to poor health, a lack of job opportunities or other factors. Retirement for persons who cannot find work may be filled with financial challenges, mental stress and an unwelcome dependence on others. For workers doing manual labour, personal health and safety may become an issue.

Employers and Plan Administrators
Beyond concern for the financial well-being of retirees, are there other reasons employers and plan administrators should be concerned about the retirement security of workers? Yes—Those workers who delay retirement affect the ability of employers to hire and retain younger workers with new skills. Delayed retirement also affects benefit costs and an employer’s bottom line.

- **Limited opportunities for younger workers.** Employers often depend on the retirement of older workers to allow the hiring, development and upward movement of younger workers. When older workers delay retirement, the ability to bring in and develop new talent is stymied. Furthermore, some promising younger employees are lost when they decide to move on to greener pastures with another employer that has opportunities for growth and advancement.

- **Less productivity.** There are a number of reasons for waning productivity as workers age (e.g., poor physical health, a decline in cognitive abilities, failure to keep up with rapid technological changes). The extent to which productivity decreases depends on the individual and the type of work they do.77 There are circumstances where education and experience make up for some or the entire decline in certain abilities. Nonetheless, the probability of a decline in physical and mental abilities rises as workers age. Workers who have no choice but to continue working are more likely to be less engaged and perform poorly. Additionally, younger workers unable to move up the career ladder may be less motivated to optimize their own productivity.

- **Higher compensation and compensation-related benefit costs.** Older workers have higher salaries and wages that lead to higher costs for payroll and compensation-related benefits such as retirement plan contributions. At some point, pay continues moving upward while productivity declines. The value of a worker’s production may even be less than pay—especially when the cost of benefits is factored in.
• **Increased health care costs.** In general, older workers have more health issues than younger workers. Older persons are more likely to have chronic diseases (e.g., cancer, heart disease and diabetes). While primary medical care (i.e., doctor's visits, hospitalization) is available through provincial health insurance programs, many employers provide extended health and dental insurance—including the coverage of prescription medications. As the workforce ages, the health issues of older workers will have an increasing financial impact on the cost of these benefits provided by employers.

• **Longer and costlier workers’ compensation claims.** Older workers have fewer accidents in the workplace, but their injuries are often more severe. Older workers also take longer to recover from their injuries. More severe injuries and longer recovery mean higher cost workers’ compensation claims and the potential for higher workers’ compensation insurance fees charged to those employing these workers.

• **Higher absenteeism.** According to a Conference Board of Canada report, workers aged 55-64 took an average of 13.2 days of sick leave, compared with an average of 5.9 days for workers aged 20-24 and an overall average of 9.3 days.

While some workers view working longer as a positive, this will not be true for everyone. Some who are working will be disappointed they have neither the time nor money to enjoy their later years as they had hoped. Of course, another difficulty is that not all who want to work may be able to do so due to poor health, a lack of job opportunities or other factors.
IV. Strategies to Promote Retirement Security

With so many factors contributing to retirement uncertainty for workers, it should not come as a surprise that fixing it requires a multipronged approach. The performance of financial markets and other macroeconomic events cannot be controlled, but there may be occasions when government programs and policies can be modified to address problems. Plan administrators and employers also have a stake in workers achieving a secure retirement and are increasingly giving attention to what they can do to help. In fact, Canada’s Task Force on Financial Literacy specifically urges “employers and labour organizations to make a concerted effort to help address the financial literacy of their employees and members as part of their overall well-being.” The good news for those offering workplace benefit plans is that many steps can make a difference for workers and their families at minimal cost.

Many households will receive retirement benefits from multiple sources. There is a need to help workers understand the diverse benefits and how to maximize their value. As workplace retirement benefit programs increasingly shift from DB to DC plans, RRSPs and so forth, another critical element will be member engagement and education—driving increased retirement planning and, when appropriate, promoting greater savings by workers. Employers and plan administrators are a natural source of products, information, education and other support to help individuals understand the various retirement benefits available, establish personal retirement plans, reach savings objectives and make the transition into retirement.

Goals

As evidenced by the diversity of workers and existing retirement benefit programs, there is no one-size-fits-all solution for employers and plan administrators that want to take a more active role promoting the retirement security of workers. There is a variety of actions that can help achieve one or more of these five interrelated goals:

1. Help workers determine their retirement needs and where they stand.
2. Get workers enrolled and saving for retirement.
3. Help workers make prudent investment choices.
4. Help workers stay on track to meet their retirement objectives.
5. Assist those near retirement to make the transition.

Of course, the ultimate goal of any effort to promote retirement security should be to set workers up for success. The actions chosen by an employer/plan administrator depend on what actions are already in place, the needs and desires of workers and a variety of other factors that may be unique to the workplace where the effort is going to be made. Some advice on how to better understand workers is provided on page 57 in the section titled “Know the Audience.”

There is no specific order in which the strategies for achieving these goals must be deployed. For example, employers with a workplace plan that permits voluntary employee contributions often choose to automatically enroll new workers at the time they are hired to get these workers on the path to saving for retirement as soon as possible. Later, they provide information and tools that will help each worker determine personal savings needs. This may seem backwards, but the impact of autoenrolment is so great that its early implementation may be a wise choice. In selecting strategies to pursue, also keep in mind these two keys to helping workers:

1. **Human behaviour.** People are not as rational as many believe. The promotion of retirement security is not always what appears to be most rational or logical. Many of the suggestions that follow are based on the insight of behavioural economists on motivating behavioural change. Fundamental throughout each step is making action on the part of workers as simple as possible.
2. **Worker abilities and desires.**
Shlomo Benartzi, a professor of behavioural science and chief behavioural economist for the Allianz Global Investors Center for Behavioral Finance, has proposed DC plan members fall into three categories. See Figure 5. Conservatively, 90% of workers are *delegators*—They have neither the knowledge nor the desire to be actively involved in managing their retirement savings and would prefer professionals do it for them. For those in this group who need to set aside more for retirement, automatic investment in a one-stop, professionally managed, well-diversified investment portfolio may be the optimal approach. Another 9% of DC plan members—the *fine-tuners*—want to be involved with the management of their savings, but not deeply involved. A menu of five to nine core funds from which they can choose that includes a target-date fund is a nice fit for this group. The remaining 1% are *customizers* with extensive knowledge of investing. Persons in this group want to be extensively involved in the management of their retirement investments and prefer a much broader menu of investment options from which to choose, including specialty funds.82
Getting Started

A good place to begin for an organization that wants to improve the retirement security of workers is an assessment of (1) what programs are already in place and (2) how well these initiatives are working. The Appendix provides a checklist of key strategies described in this paper that employers and plan administrators have used successfully to promote the retirement security of workers. As for how well current programs are working, Exhibit 6 suggests metrics used to gauge success.

Goal 1: Help Workers Determine Their Retirement Needs and Where They Stand

Winning athletes and successful businesspersons envision what they want to accomplish and then identify what they need to do to achieve their vision. The same approach can help individuals prepare for retirement. An increasing number of employers, plan administrators and vendors are providing workshops, planning tools and other resources to help plan members determine how much income they will need at retirement to achieve their retirement goals and whether they are on track for success.

Encourage Workers to Picture Their Retirement

Plan administrators should encourage workers to envision their future retirement—where they want to live, what they want to do, etc. Most people know they “should” save for retirement, but they find themselves doing something else instead. Behavioural economists refer to this problem as the future discounting obstacle. Young persons, especially, view retirement as something far in their future. Having their own personal retirement picture helps them avoid temptations to spend today that might derail their retirement. As workers get closer to retirement, the picture of their retirement years will be developed more fully—providing a foundation for determining how much it will cost to make their retirement dreams a reality.

Though they may not realize it, creating a picture of their retirement helps workers consider what is most important to them. Desires to be self-sufficient, stay active, care for loved ones, learn new things, spend more time on personal interests—All of these wants reflect a person’s core values and beliefs. They are intrinsic motivators that spur workers to make sure they have saved what they will need when they retire. While plan administrators can (and should) use extrinsic motivators such as contribution matches and competitions to jump-start employee savings behaviours, studies over many years have found that when extrinsic rewards stop, people usually return to the way they acted before the program began. It is intrinsic motivators that have the more lasting impact.

Get Life Partners Involved

For workers with spouses/life partners, the input of both individuals is essential to successful retirement planning. Having partners involved in the process not only introduces the partners to the choices available, it can increase the likelihood couples will have a joint retirement plan and work together to achieve a secure retirement. Plan administrators should encourage partners to become informed and actively involved throughout the retirement planning process.
Exhibit 6 | Measuring the Success of a Retirement Security Initiative

Gauging the success of efforts to promote the retirement security of workers varies with the type of retirement plan(s) offered. DB plan administrators have a fiduciary responsibility to monitor certain factors to ensure members receive the benefits they have been promised:

- **Contribution level**—whether current plan contributions are sufficient to pay future obligations
- **Investment performance**—whether the return on fund assets is reasonable while minimizing risk
- **Management fees**—the reasonableness of investment management fees given the investment return and services provided
- **Liquidity**—the ability of the plan to meet anticipated cash flow needs.

While not necessarily required by law, DC plan administrators should be concerned with:

- **Investment performance**—the return on investment options provided members
- **Plan fees**—how much members pay for their investment choices
- **Participation rates**—the proportion of eligible employees who need to save that are actually contributing to the plan
- **Member deferral rates**—how much workers who need to save are setting aside for retirement through their plan
- **Savings to employer match**—the proportion of members who defer sufficient funds to capture the full employer matching contribution (if there is a match)
- **Asset allocation**—whether plan members with self-directed plans have a diversified retirement portfolio. For example, a plan administrator might investigate how many members are invested in at least three different asset classes or an asset allocation fund (e.g., a lifestyle or target-date fund).

While all of the items identified so far are important, the true benchmark is whether each worker will have an adequate income at retirement. Metrics used for this purpose are:

- **Projected retirement income replacement**—the percentage of worker income just prior to retirement that will be replaced during retirement. Companies with significant numbers of relatively low-income earners will want to integrate workplace contributions and benefits with OAS, GIS and CPP/QPP to produce more appropriate net replacement ratios across the entire income spectrum.
- **Projected monthly retirement income**—the amount a retiree can expect to receive or draw out of retirement savings each month for the rest of his or her life.

Plan administrators are encouraged to dive down into plan data to examine differences among various demographics (e.g., age, income level, race, gender). Benchmarking data with others in the same industry can also be extremely valuable. Vendors can be quite helpful in providing this data and, sometimes, specific recommendations to improve outcomes.

Plan administrators also should seek feedback from workers. It is helpful to examine:

- **Worker ability and desire to be actively involved in planning and saving for retirement.** It is important at the outset to recognize the substantial differences that exist among workers with respect to their financial literacy, interest in managing their retirement savings, etc.
- **Worker use of information, education, advice and other tools offered**—What kind of support do workers consider most valuable, and which delivery methods are most effective?
- **Worker satisfaction**—How do workers perceive their retirement benefits and the various efforts to promote their retirement security?

See “Know the Audience” on page 57 for questions and strategies to gather this and other worker information including their skills and knowledge pertaining to retirement planning and their desires for help preparing for retirement.
Be aware that not everyone is able to come up with positive scenarios for retirement. When several thousand people were asked (1) what they feared most about retirement and (2) what their best-case scenario was for their retirement, two out of five admitted they were unable to see anything positive about retirement. What is positive about getting old?

Benartzi, the behavioural economist who discovered this obstacle, suggests giving workers a few minutes to suppose they have sufficient funds for retirement and will be able to live comfortably without worrying about paying bills or health expenses. Follow up by asking each person to write down everything that comes to mind in terms of both their tangible lifestyle and how they feel about this scenario.

As soon as individuals who need to save more complete one of these exercises, Benartzi also suggests, direct the workers to check a box indicating they wish to increase their savings rate. Alternatively, there might be four boxes offering rate increases of 3%, 2% and 1%, with the fourth box blank for another rate of their choice.

**Deliver Basic Retirement Information**

Research noted previously in this report indicates many Canadians simply do not understand the benefit programs and savings/investment vehicles available to them through government, their workplace and elsewhere that provide the pillars to achieving a secure retirement—let alone how these pillars can best be used to achieve a comfortable life in their later years. When it comes to saving and investing for their future, employees often look to their employers and plan administrators for guidance and direction.

A 2014 survey of CAP sponsors suggests employers agree to at least some extent. Almost all CAP sponsors (95%) said they have a responsibility to provide employees with tools and resources to help them make sound decisions regarding their employer retirement plan. Exhibit 7 suggests topics employers and plan administrators will want to consider addressing via an education program or other communication strategy.

For those employers that might fear providing workers with information regarding investment choices, consider these findings from the 2014 CAP member survey:

- Two-thirds (66%) of members said they trust their employer’s default investment will provide them with adequate funds for their retirement.
- Nearly the same proportion (63%) believes that if they don’t make their own investment choices, employers have the responsibility to ensure their contributions are invested properly.
- More than half (54%) said their employer is responsible for ensuring the investment choices they (the plan members) make are the “best choices for them.”
- Another significant percentage, 42%, believes their employer has the ultimate responsibility to ensure they will retire with enough funds to live with an acceptable standard of living.

It appears that providing employees with the basics of their retirement plan and investing may be more than just a “nice” thing to do; it may be essential to reducing employer risk down the road should employees experience a gap between what they expected and what they actually accumulated. Sponsors face three risks: (1) legal risk that employees will sue an employer, (2) business risk when people can’t retire when they had planned and (3) reputational risk to the organization.

Retirement education and planning tools, by themselves, will not address the retirement challenges faced, but they will provide workers with the information they need to better plan for their future and make choices that best fit their circumstances.
Offer Retirement Planning Tools

Section 3 of the *Guidelines for Capital Accumulation Plans* says CAP sponsors should provide decision-making tools such as:

- Calculators and projection tools
- Investor profile questionnaires
- Asset allocation models.

Calculators and projection tools can help members determine whether they need to save, how much they need to save, contribution levels and future balances. They also help workers determine whether they are on target for a secure retirement. Some calculators go a step further and consider the risk tolerance of the user. Assessments are also available to help individuals determine their comfort with different levels of risk.

Figure 6 provides a sample of model portfolios that illustrate different asset allocations based on the risk tolerance and investment objectives of plan members. As a member nears retirement, those with self-directed investments will typically move from a relatively aggressive portfolio to a mix of assets that is more conservative.

### Exhibit 7 | Basic Retirement Information

At a minimum, it seems appropriate for employers and plan administrators to provide information concerning:

- Government retirement programs (Pillars I and II) and the benefits they provide
- Eligibility requirements for workplace retirement plans (Pillar III) and how benefits from these plans are determined
- If there is an employer match, how much a worker must save to get a full match
- The advantages of participating in a workplace retirement plan (e.g., professional management, lower fees, payroll deduction, employer match, more savings/income at retirement)
- The consequences for members who do not make decisions regarding their voluntary workplace plan (e.g., automatic enrolment, automatic escalation, default investment in a choice with conservative returns)
- Common savings and investment vehicles available outside the workplace that comprise Pillar IV
- What tools are available to help workers determine whether they need to save for retirement and how much they need to save
- How Pillars II, III and IV can lead to reductions in OAS and GIS benefits. For example, low-income Canadians who save using an RRSP will reduce their GIS.

For those who will be setting aside funds for retirement:

- How saving early and compound interest can boost their savings
- The pros and cons of various savings options (e.g., TFSAs vs. RRSPs) including the tax consequences.

When workers have a choice among different investments for a DC plan or other CAP plan, there is additional information that should be provided to members. Note that many of these same items are suggested in Section 3.2 of the *Guidelines for Capital Accumulation Plans* published by the Canadian Association of Pension Supervisory Authorities (CAPSA).

- Glossaries explaining basic investment terms (e.g., stocks, bonds, money market accounts, fixed income, active vs. passive management, risk and return)
- Information on how investment funds work
- Information on the investment options members can choose from (e.g., equities, bonds)—including the risks and potential return of each
- How to diversify and rebalance an investment portfolio
- Alternatives available to members such as target-date funds that do not require them to manage their personal investments—and how these alternatives work.
- Investment performance reports.
Besides helping with decision making, calculators and projection tools have also been found to help motivate those who need to save more. A study of U.S. workers found that those who had calculated how much they must save to meet their retirement needs had higher savings goals than workers who had not done a calculation.\textsuperscript{91} When U.S. workers used an online calculator to determine their retirement savings targets, the likelihood they will save enough for a sufficient retirement income also increased. The magnitude of the savings increase ranged from 9\% to 18\% depending on the respondent’s gender, marital status and income. In general, the lower the income of the worker, the higher the impact of using the calculator.\textsuperscript{92} Individuals who merely guessed their retirement savings target tended to underestimate their savings needs—reducing their chance of a sufficient income by as much as 9\%.\textsuperscript{93}

The best retirement planning calculators allow workers to factor in assets and income from multiple sources; for example, benefits due a spouse, assets from past employers, personal savings and expected government payments. Some of the newest calculators are able to access savings accounts from other sources and automatically enter the information needed to make calculations. Users should have the ability to link investment returns to specific investments. In other words, the return on a money market account should not be projected to be the same as a stock fund.

If a member’s desired retirement age or income does not work given current savings and investment choices, a good calculator suggests adjustments to help bring the user closer to achieving his or her goals. Some calculators have a sliding scale that allows the user to see how their monthly retirement income will change if they save more money, adjust the asset mix in their retirement portfolio or delay retirement.
When selecting a calculator, be mindful of the assumptions used. Assumptions for return on investment, inflation rates, tax rates and health care costs can cause results to vary widely. Retirement projections should show a range of possible results, reflecting both the upside potential and downside of risks. The advantage of this approach is that users can see the ups and downs that may occur with different investment choices they make and the risks they face.

With so many unpredictable factors associated with retirement planning, tools that provide Monte Carlo simulations are worth considering. Named after the city in Monaco where the primary attraction is casinos, these calculators predict the probability of a certain retirement outcome much like a gambler might consider the chance of winning. A Monte Carlo analysis involves multiple trial runs, called simulations, with random variables that affect retirement such as life expectancy, inflation, wage growth and investment returns. Users are provided the likelihood they will achieve their retirement goals.

Plan administrators providing access to calculators and other retirement planning tools must keep in mind that many workers will not be able to use these tools without substantial guidance. If users are expected to use a calculator, the instructions for data entry must be clear—especially when it comes to making assumptions regarding interest rates and investment return. If users are asked to select an income replacement rate for their retirement years, they need information as to what might increase or decrease the percentage needed. For example, having a home with a mortgage paid in full lowers how much income is needed. Individuals may need to be reminded they will no longer be setting aside a portion of their income for retirement. On the other hand, health costs typically increase the income needed. In some cases, a counselor may be required to take a user systematically through the process—helping locate data, entering it and, ultimately, interpreting the results.

Sponsors are probably aware that there are legal implications associated with making retirement planning calculators and similar tools available. On the other hand, there are also risks associated with providing no guidance whatsoever. As with most things, a reasonable amount of diligence of the kind just described will go a long way in mitigating such risk.

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**Provide Access to Financial Advisors**

As stated earlier in this report, workers often have limited knowledge regarding their future retirement benefits, investment management and so forth needed to establish and follow through with retirement planning. In addition, not every person has the time or motivation to plan for his or her retirement.

Default investment options, professionally managed accounts, benefits information and education programs help address these obstacles, but even they cannot provide all the guidance needed to achieve a secure retirement. Sometimes, there is simply no substitute for personalized and objective financial advice. Unfortunately, not all workers can afford or will seek advice on their own.

When employees were asked to rate the effectiveness of the approaches used by their employers, personalized communication was rated most highly. Respondents identified a financial advisor (77%) as the most effective approach, followed by online retirement modeling tools (71%) and company/administrator websites (70%). At the bottom of the list were educational materials mailed to their homes (57%).

Plan administrators providing access to and encouraging the use of financial help workers make smarter decisions that keep them moving in the right direction—toward a secure retirement. An Aon Hewitt study of DC plan members in the U.S. found that those who used one or more professional tools (e.g., professionally managed accounts, online advice, registered investment advisors) had a median annual return 3.32% higher (net fees) than those who didn't receive help. To grasp the impact of this difference, consider two people who invested $10,000 for 20 years: The person who received help would have a portfolio worth 79% more than that of the person who did not receive help—$58,700 versus $32,800.

Furthermore, Aon Hewitt found that 61% of those persons who had not received help had inappropriate risk levels for their portfolios. Almost two-thirds of these persons were taking on too much risk, leaving them vulnerable to market downturns—The remaining third were taking too little risk, potentially jeopardizing their ability to retire as desired.
A Schwab study of another group of DC plan participants in the United States found using independent professional advice changed worker behaviours with respect to self-directed plans:

- **Increased savings**—70% of members increased their retirement savings contribution rates.
- **More diversification**—Members invested in at least eight assets, compared with an average of 3.7 assets for those who chose to manage portfolios on their own.
- **Periodic rebalancing**—Those with a plan that annually rebalanced the assets in their portfolio had a higher annualized rate of return than those who never rebalanced their assets.
- **Increased likelihood of staying the course**—Members were more likely to stick with their investment objectives and be less reactive during a market downturn or high volatility.

While plan administrators are often optimally situated to make retirement planning information and advice available to workers, not all are willing or able to do so. Some are concerned they could be held liable if workers later claim the advice harmed their financial position. To avoid liability and increase member use of professional advice, financial advisors and planning tools should be comprehensive, personalized and provided by a certified third-party advisor who is not selling products or services. Delivery through an independent advisor removes the conflict-of-interest concerns of some plan administrators. Employees get the unbiased help they need, and administrators do not incur the legal liability associated with specific investment recommendations.

When looking for a third-party financial or retirement advisor, seek someone who:

- **Holds a credible designation.** The Certified Financial Planner (CFP) designation has become the gold standard for financial planning. Other credentials that provide evidence of knowledge on a wide range of financial planning topics include Chartered Financial Analyst (CFA), Certified Public Accountant–Personal Financial Specialist (CPA-PFS) and Chartered Financial Consultant (ChFC). Because these credentials focus on asset investment and accumulation, consider asking these advisors whether they have any special training or expertise on generating retirement income; for example, designation as a Certified Retirement Counselor (CRC), Retirement Management Analyst (RMA) or Retirement Income Certified Professional (RICP). The Certified Employee Benefit Specialist (CEBS) designation ensures an advisor knows the benefits industry and fiduciary limits when providing investment advice in the workplace.

- **Will sign a fiduciary acknowledgment.** Advisors should sign a document that specifies they are acting as a fiduciary and, accordingly, will not let any conflict of interest affect their duties to those being advised. Furthermore, they will exercise a professional standard of care and good faith in protecting or promoting the interests of those they advise. CFP professionals have to sign off on a code of ethics every year.

- **Generates revenues on a fee-only basis.** An advisor who earns money based on commissions versus a flat fee could have an incentive to steer investment choices in a particular direction. There are also advisors who charge a percentage of assets managed—These professionals may not recommend annuities and other solutions that reduce the assets under their management.

- **Has significant work experience.** Look for an advisor who has or is currently working with plan members. He or she will more likely know what works and what doesn’t with respect to workers who participate in retirement planning.

To encourage use of a financial advisor, some sponsors arrange for an advisor to come to the workplace. A sign-up sheet is posted with a list of scheduled times for meeting with the advisor. All the worker has to do is put his or her name on the sheet and show up for the meeting. Consider letting workers meet with the advisor during paid work hours.
Provide a Regular Retirement Income Statement

Members of DB plans receive annual statements clearly indicating the benefit they will receive from their plan upon retirement. Such is not the case with DC plans because the income received at retirement is not predetermined. At minimum each year, a DC plan administrator should provide plan members a clear, concise retirement income statement projecting a range of possible monthly income amounts the member might receive during retirement given various contribution rates, asset allocations and years to retirement. The income generated by CAPs is highly uncertain and volatile depending on the choice of investments, market forces and the decumulation choices made. Hence, it is especially important for CAP members to see and understand the uncertainty that exists.

Plan members can quickly and easily sum up the monthly income estimates from their various retirement plan(s) to get a figure that is much more meaningful than an account balance. Projections that reflect how increases in contributions positively influence benefits might also help motivate members to raise their savings levels.

Placing monthly income projections on the first page of a retirement account statement and the account balance/investment performance information closer to the end of the report makes it easy for the member to find the income projections. It also helps members focus on the long-term versus short-term performance of investments. Monthly income projections seem less dramatic than short-term performance figures, which can also help calm those members most likely to overreact and chase investment returns.

Goal 2: Get Workers Enrolled and Saving for Retirement

For those persons who want or need more retirement income than what is provided by government retirement benefit programs (i.e., OAS, GIS, CPP and QPP), a workplace retirement plan offers a convenient, tax-advantaged way to help workers get additional funds. How such a plan is designed can do much to increase worker participation and the amount saved. The enrolment process also provides a natural opportunity to help workers understand how three elements—starting to save early, contribution rates and portfolio asset allocation—are key to how much money they will have when they retire.

Offer a Workplace Retirement Plan

For employers whose workers would benefit from a workplace pension plan, the first step in helping employees achieve a secure retirement is to provide such a plan. Employers that do not want to establish and maintain a plan on their own can use a Group Registered Retirement Savings Plan (Group RRSP) and/or Group Tax-Free Savings Account (Group TFSA). For more information on RRSPs and TFSAs, see Exhibit 2 on pages 7-9.

Employers—particularly those that are small—might also want to consider participation in a multi-employer pension plan (MEPP). MEPPs permit the pooling of funds from a large number of workers that can yield better plan design, administrative efficiencies and access to more professional expertise. Traditionally, most MEPPs have been available to union members, but there is no reason professional associations and nonunionized groups could not establish such plans.

Reforms related to target benefit plans—particularly the extension of such plans to the single employer environment—are an opportunity to broaden the scope of this option. When compared with a DB plan, a TBP gives employers more certainty with respect to contributions and no withdrawal liability. Pooling funds gives employees the potential for higher returns. Reminder: Additional background concerning TBPs is available on page 17.
**Relax Plan Eligibility**
Reducing waiting periods for plan entry allows new hires to start saving for their retirement right away. Plan administrators with high worker turnover concerned about the hassle of dealing with the accounts of workers who don’t work out might have workers complete the retirement plan enrolment forms at the time of hiring but simply delay participation for a period, say six months or a year. Even though saving doesn’t start immediately, enrolling a worker within the first days of work counters the inertia and indecision that too often paralyze individuals from starting to save and helps produce regular, long-term savers.

**Use a Stretch Match**
Most employers match worker contributions to DC plans to encourage retirement savings. The availability of a match, the size of the match and the *match cap* (the maximum amount that the employer will match) can all positively affect DC plan participation and the amount workers save, but some of these design features are more effective than others.

With respect to participation, there is general agreement that the availability of a match positively affects participation—in the range of 3% to 10%. The effect of the match rate on how much workers contribute is less clear. While some studies have found that an increase in the match rate increases contributions, others have suggested the increase has no effect or even lowers contributions. While any increase is welcome, the impact of offering a match and the size of the match on participation has not been nearly as dramatic as the universal 15% to 25% member boost created by automatic enrolment discussed on the next page.

The match cap has little or no impact on plan participation, but its effect dwarfs the effects of the other factors with respect to the amount members save. Figure 7 shows how employee contribution rates changed when one company introduced an employer match with a cap of 4%. Before the match and match cap were introduced, member contribution rates clustered around 5%, 10% and 15%. Within six months after the introduction of the 4% cap, almost 30% of members shifted to a 4% contribution rate—lower than the rates they had chosen on their own.

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*Figure 7 | Contribution Rates Before and After a 4% Match Cap*

<table>
<thead>
<tr>
<th>Contribution Rate Before Match Initiated</th>
<th>Contribution Rate After Match Initiated</th>
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<tbody>
<tr>
<td>1%</td>
<td>5%</td>
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<tr>
<td>2%</td>
<td>10%</td>
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<tr>
<td>3%</td>
<td>15%</td>
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<tr>
<td>4%</td>
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<td>5%</td>
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<td>14%</td>
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<tr>
<td>15%</td>
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</tbody>
</table>

A no-cost way to boost member savings is to stretch the match to a higher rate. As an example, consider a default contribution level of 3%. Instead of offering a 100% match of up to 3% on an employee’s pay, an employer might stretch the match by offering a 50% match of up to 6%. Employees who save up to the cap would have total savings of 9% contributed to their plan.

**Use Automatic Enrolment and Automatic Escalation**

For those workers who should be saving but have little interest in taking their retirement future into their own hands and/or do not have the ability to do it well, automatic enrolment and escalation are key. With automatic enrolment, a plan administrator reframes the decision to contribute to a DC plan. Instead of asking workers to enrol in their workplace plan, the administrator determines what percentage of employee salaries or wages will be contributed to the plan and automatically enrols employees.

Individual employees must take action to opt out of enrolment, change the percentage contributed and adjust how it is invested. Essentially, the same human behaviours that result in a failure to enrol—inertia and procrastination—are exploited to promote enrolment. A 2014 Aon Hewitt study found the average participation rate across companies offering a DC plan with automatic enrolment in the United States was 85%, compared with a rate of 62% among companies without automatic enrolment.103

While automatic enrolment seems to be a natural strategy to use with new hires, it also can improve the retirement savings of those who previously chose to opt out of their retirement savings plan. Plan administrators are now conducting a one-time “backsweep” or ongoing sweeps to autoenrol all nonmembers. If workers don’t want to enrol immediately, they can be asked when they would like to enrol in the future. At the beginning of the new year? One year from now?

Because workers tend to stay with the defaults chosen by the plan administrator,104 the contribution rates and asset allocation in an autoenrolment program must be chosen very carefully. Low default contribution rates and investment in conservative assets can result in workers not achieving a secure retirement. The default investment option accompanying autoenrolment should be a professionally managed, well-diversified, single-option solution for members who cannot or do not want to make asset allocation and rebalancing decisions on their own. See Exhibit 8 for a brief explanation of two options.
Given so many workers report household expenses and debt are obstacles to saving, many plan sponsors may be concerned as to how workers will accomplish a contribution rate greater than 3%. A 2012 survey of DC plan members suggests this concern may be unwarranted. A surprising 83% of respondents said they could cut their household budget by at least 5% to save more for retirement—including 64% who said they could reduce their budget by 10% or more.\textsuperscript{105}

The experience at one U.S. company that introduced automatic enrolment suggests what workers are saying about increasing their contributions is true. When the company initially introduced automatic enrolment, the default contribution rate was 3%. A year later, the contribution rate for new hires was increased to 6%. Throughout this process, the employer had a dollar-for-dollar match for employee contributions up to 6%. Contrary to what anyone probably expected, the participation rate at 6% was essentially identical to when the default was 3%—about 95%.\textsuperscript{106} The experience at this company also reinforces the conclusions of other research that the match cap has more influence than either the availability of an employer match or the rate at which the employer matches employee contributions. For plan sponsors that still think 6% is too high, Shlomo Benartzi at the Allianz Global Investors Center for Behavioral Finance suggests 4% as the initial default rate.\textsuperscript{107}

Once workers are enrolled, automatic escalation is a means to increase the proportion of a worker's salary or wages saved over time. When escalation occurs at the same time as a pay increase, members are less likely to miss money they didn't receive previously. In the same 2012 survey of DC plan participants, 52% said they would be willing to increase their savings rate to as high as 10% if their employer automatically increased the rate by 1% per year.\textsuperscript{108}

Some employers have taken the step of requiring automatic enrolment and autoescalation as a term and condition of employment. It may be necessary to give appropriate notice to existing nonunionized employees before autoenrolment and autoescalation can be made mandatory. In the case of unionized employees, this has to be worked out through the collective bargaining agreement. Employers considering any form of automatic enrolment or escalation should seek legal advice before proceeding.

Simplify Decision Making

While automatic enrolment and automation of other parts of the retirement decision process have been proven to get results, not everyone is an admirer of this approach. Employers could actually harm versus help low-income workers by automatically enrolling them. From a broader perspective, when individuals do not actively participate in making choices, it is likely they don't know the options available to them and what is best in their personal circumstances. Moreover, while they may be a minority, some workers want to be actively involved in making decisions regarding their future retirement. For these reasons, some plan administrators prefer a process that combines retirement benefit education with simplifying enrolment.

During orientation, new workers complete important forms concerning their extended health benefits, direct deposit of their pay and taxes. Workers can be asked to fill out retirement plan enrolment forms at the same time and hand them in before they leave the orientation. Alternatively, they might be asked to respond within a certain amount of time—perhaps two weeks or a month. Communication prior to the deadline should remind new hires they must make a choice and that the date for a response is nearing. While a deadline is nonbinding, it may be enough to nudge some employees to action.
To get workers who need to save for retirement to focus on doing so and to provide them with guidance in their decision making, an employer or plan administrator might divide the enrolment decision process into several small steps—providing individuals with information and directions on what to do at each stage. For example, the process might have these stages:

- **Determine whether personal savings are necessary.** Provide basic information on government retirement benefits, including how income generated on personal savings can offset these benefits, so workers can decide whether personal savings are appropriate for them.

- **Encourage enrolment and saving.** Use a broad variety of media sources and communication strategies to motivate individuals to enrol and save for retirement.

- **Choose how much to save.** When asking workers how much they will save, give them tools such as worksheets or online calculators that will help them determine the savings amount that is right for them. Indicate the minimum and maximum amounts they are permitted by law to save based on their income, and explain how any sponsor match works. Emphasize that the match is free money.

- **Choose where to save.** If the plan provides investment options, the administrator has a broad range of legal duties that include helping plan members identify their personal risk tolerances and information on the pros and cons of the alternatives available (including the default option) so that members can align their goals and risk tolerances to the available options.

  A simple enrolment card with boxes to check reflecting each decision made by the worker can be effective. Another approach is a one-page sheet with step-by-step instructions that includes a time frame for how long each step will take. For persons for whom English is a second language, materials in other languages may be needed.

While automatic enrolment and automation of other parts of the retirement decision process have been proven to get results, not everyone is an admirer of this approach.

**Leverage Competition**

Some people are motivated by competition. Principal Financial Group—a provider of financial products such as retirement plans—conducts a national educational campaign challenging members of its plans to defer at least 10% of their annual salary for retirement. Those who accept the challenge are eligible to win a Fitbit Flex™ (or comparable activity tracker) to help monitor their physical fitness progress. Employers conduct similar competitions with gift cards, lunch parties and vacation days as common prizes. If 10% seems too high a target for some workers, the bar might be set lower—say, 5% of their compensation. Alternatively, consider giving each worker one chance at a prize for each percent deferred.
Goal 3: Help Workers Make Prudent Investment Decisions

How plan assets are invested is a critical determinant of long-term retirement savings growth. In addition to providing access to a financial advisor, what can plan administrators do to help optimize the risk and return on a worker’s retirement savings?

Offer a No-Option Defined Contribution Plan

When DC plans were first introduced, plan assets were invested in a single investment option—often a balanced pooled fund—selected by the plan administrator or trustees. Plan members had no say as to how their funds were invested. When a member left the plan, the member received his or contributions plus a share of the return on investments in the fund. There are multi-employer plans that continue this practice today. However, over the years, DC plan sponsors increasingly gave members the ability to choose among multiple investments—the approach that is now prevalent. Plan sponsors had good reasons for making the switch from no- to multi-option plans. However, there are also good reasons to consider the no-option approach. Table VI briefly summarizes the advantages of both.

Without choice, the administrator’s only fiduciary obligations are to manage the assets prudently and to comply with the relevant pension requirements such as periodic disclosure and regulatory filings. The Guidelines for Capital Accumulation Plans do not apply.

The administrator’s potential liability is similar to that of a DB plan. The fees/costs of managing a no-option plan are also likely to be less than those in a multi-option plan.

When choice is provided, the administrator acquires a host of legal duties including the responsibility to provide educational opportunities to members, communicate with members and monitor the performance of each investment option. Providing investment choice also places a duty on the administrator to identify, understand, negotiate and explain the fees/expenses of each option.

Deciding which of these two options is best for a particular plan depends on a number of factors such as member demographics, the investment sophistication of members and the willingness of individuals to take responsibility for their investments. A no-option plan tends to be appropriate when members are a relatively homogeneous group.

Offer Target-Date Funds

The investment industry’s solution to helping plan members maintain appropriate asset allocation is target-date funds (TDFs), also referred to as age-based funds and lifecycle funds. Target-date funds are hybrid mutual funds that invest in a mix of assets (e.g., stocks, bonds and cash) that put retirement savings on autopilot.

Members choose the fund with the date nearest when they plan to retire. The target year is identified in the name of the fund; for instance, a person who plans to retire in or near 2050 would pick a fund with 2050 in its name. The mix of assets in the fund is automatically rebalanced as the fund date approaches and typically becomes less risky so investors have more stable values and returns as they near the time when they will begin withdrawals.

Plan administrators choosing a TDF should be aware that great diversity exists in products on the market and their fees/expenses. It is essential to understand what the specific TDF’s glidepath (asset allocation over time) is designed to accomplish. Some products feature a glidepath that matures at the member’s projected retirement date, while others carry the investor well into retirement. TDFs also vary in risk, ranging from conservative to aggressive. Some funds are actively managed while others use index funds with a passive management approach.
<table>
<thead>
<tr>
<th>Plan Members</th>
<th>Multi-Option (a.k.a. Self-Directed)</th>
<th>No-Option</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Can be more engaged in their plan</td>
<td></td>
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<tr>
<td></td>
<td>Have the ability to direct their investments given they are the ones who bear the investment risk</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Can align their investment strategy so that it is appropriate given their individual risk tolerance, their investment horizon and any assets they hold elsewhere.</td>
<td></td>
</tr>
<tr>
<td>Plan Administrators</td>
<td>Select and monitor the plan provider</td>
<td>Experience lower investment management costs</td>
</tr>
<tr>
<td></td>
<td>Select the investment menu</td>
<td>Select and monitor the plan provider</td>
</tr>
<tr>
<td></td>
<td>Negotiate investment management costs</td>
<td>Must employ a reasonable investment strategy</td>
</tr>
<tr>
<td></td>
<td>Monitor investment options for members but do not have to make investment decisions</td>
<td>Negotiate investment management costs</td>
</tr>
<tr>
<td></td>
<td>Communicate investment options to members.</td>
<td>Have little responsibility for providing information and decision-making tools to members</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Can devote significantly fewer resources to educating members about investment options</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Are not subject to CAP Guidelines.</td>
</tr>
</tbody>
</table>
Limit the Number of Investment Choices

When DC plans provide a menu of investment options, the plan administrator must keep in mind that while some members may appreciate being able to select options that fit their personal circumstances, other members will likely be overwhelmed by the choices—especially if there are a lot of choices. The unintended consequences of a large number of choices are member inertia and procrastination—in other words, choice avoidance.

One study found that for every ten new investment options offered, plan enrolment drops between 1.5% and 2%. The same researchers found that among those workers who do enrol, increasing the number of funds offered might also cause members to shy away from equities; instead, members select simpler, easier-to-understand bonds and bond equivalents. For every ten funds offered in a plan’s menu, members reduced their exposure to equities by 3.28%.

A consensus of experts recently surveyed by the TIAA-CREF Institute suggests the appropriate number of funds in an investment menu should be between five and ten.

How the menu of options is structured is as important as the number of choices offered. When creating a list of investment choices for members, it might seem logical to list investments from least to most risk or alphabetically. It has been learned, however, that when people are provided a list of items, they tend to choose the first choice they are given. When lists are very long, another behaviour kicks in—choosing the last items because these are the items that stick in people’s minds.

Consider the implications when a list of investment choices is ordered from least to most risky. Members may choose an option that is too conservative for their needs. At the other extreme, a very long list might result in individuals selecting inappropriate aggressive investments. The top of the investment menu should be the funds that are most appropriate for the widest range of members—very likely a target-date plan.

For plan sponsors concerned that placing “appropriate” choices at the top of the investment menu may be considered investment advice, one must recognize that no list has a neutral design. It is impossible to avoid giving implicit advice given human behaviour. Ordering choices is actually guiding members so they don’t end up with an overly conservative or aggressive portfolio. An optimal investment menu for a DC plan might have a “basket of funds” such as a balanced fund or target-date fund at the top of the list that is appropriate for a majority of workers who prefer to delegate the management of their retirement portfolio. The remaining choices could be a small group of core funds that permit those who want to have some control over their investments to create a well-diversified portfolio.

Be aware there is also some evidence that the higher the number of lines for members to enter investment choices on the plan enrolment form, the higher the number of options selected. A sponsor may want to test whether changing the number of lines available affects the investment choices made by new enrollees.

Despite the advantages or rebalancing, it appears few members with self-directed DC plans do so.
**Promote Diversification**

While stocks get the most media attention, those saving for retirement via a self-directed DC plan shouldn’t ignore bonds and other fixed income investments. Diversification of assets doesn’t ensure a profit or guarantee plan members will not experience a loss, but it can reduce the volatility of an investment portfolio.

When choosing a menu of investment options to offer DC plan members, plan administrators must provide choices that include several asset classes (e.g., domestic and foreign stocks, bonds and short-term investments). Furthermore, DC plan members faced with making investment allocation choices must be educated on the need to diversify and how it is accomplished.

The financial industry offers a multitude of mutual funds that can help small investors achieve diversification—with index funds, balanced funds and TDFs among the most popular solutions. The vast majority of members choose a small number of funds (three or four) and then divide assets equally among the funds chosen. At the extreme, some members select all the funds offered and divide their contributions equally among all the choices.¹¹ Five Both approaches are misguided attempts to diversify, as some investment choices may be quite similar with respect to risk and return.

While TDFs can help members achieve diversification, many individuals are not using these funds as they are intended. An Aon Hewitt study of DC plan members found only 38% were using TDFs as a “one-stop” investment. Almost three out of four (74%) members with a TDF held less than half their assets in the fund. Members tended to misallocate the remainder of their portfolios, with 62% having an inappropriate risk level for their overall portfolio.¹¹ Five

Generally, plan administrators cannot hold company-issued securities in a DC plan; however, exceptions for publicly traded companies do exist. When company-issued securities are permitted, the administrator should disclose this and inform members of the risks associated with such investments—particularly the fact that if the company’s stock takes a beating, so will member retirement savings if members own a substantial amount of the stock.

**Discourage Chasing Returns**

When a particular investment is doing well, it is human nature to want to put more money into it. When something is doing poorly, investors are tempted to get out before they lose more. The problem with chasing returns is that “hot” investments don’t usually stay hot. In fact, they often crash and burn right after everyone starts buying them. As for investments that aren’t doing well, it is very possible they will make a comeback and the investors who sold them will miss their recovery.

Employers and plan administrators are encouraged to educate persons in self-directed CAPs on the importance of establishing and sticking with their investment plan with respect to asset allocation, level of risk and so forth. This includes warning members that past returns rarely are a good indicator of future returns. Moreover, people who try to “time” when they buy and sell assets tend to (1) end up with portfolios with more risk than is appropriate and (2) lose more money than they gain.

Experience shows few individuals take these common cautions to heart. Providing members with an example such as the painful consequences individual investors experienced in the 2008-2009 stock market crash may get plan members’ attention. When the market crashed, many members experienced devastating declines in the value of their retirement accounts. In an effort to stop the free fall, they sold the stocks in their portfolios. When the market recovered, they lost out again because they owned no stocks. Had they stuck with their original investment objectives and waited out the downturn, they would have more than recovered their initial losses.

A strategy to discourage efforts to time the market is to restrict the number of fund transfers a member can make within his or her portfolio during a month. Some DC plans allow members to make transfers on a daily basis. Permitting only two transfers per month, for example, would restrict this activity. Alternatively, some plans allow daily trading but thwart excessive trading by prohibiting round-trip transactions—fund purchases followed by a sell or exchange within 30 calendar days in the same fund and account.
Promote Rebalancing

While buying and selling portfolio assets to time the market is generally considered a terrible idea, buying and selling stocks, bonds, etc., to rebalance a portfolio’s asset mix is a central tenet to investing for retirement. Asset values rise, fall and grow at different rates. While the relative value of some assets in a portfolio booms, the values of others shrink. Over time, the result is a collection of assets out of sync with the mix initially established by a plan member. In addition, as persons age they should be moving into more conservative investments that have less risk than what was acceptable when they were younger. Rebalancing is how investors make sure the assets they have chosen for their portfolios maintain a level of risk within their comfort zone. Rebalancing at least once or twice a year also forces investors to take profits from investments that are doing very well and put money into other good investments that are not.

Despite the advantages of rebalancing, it appears few members with self-directed DC plans do so. During the years 2009 through 2013, Vanguard found just 29% of members made a trade; and only about one in ten members made a fund transfer in any one year.117

Encourage members who are managing the investments in their portfolio to establish a plan for rebalancing their portfolios once or twice a year. Members can choose an easy-to-remember date or dates when they are most likely to take any action required. Several of the investment firms that offer DC plans now offer automatic rebalancing. Look for a firm that offers this option and encourage members to take advantage of it.

Pay Attention to Investment Expenses and Other Costs

Administrative, investment and other expenses associated with a retirement account can have a sizable impact on retirement savings. For example, Chris Daykin, chairman, Pensions, Benefits and Social Security Section of the International Actuarial Association, estimates a charge of 1% a year on a fund would reduce the accumulated amount over 40 years by almost a quarter. A 2% charge would reduce the accumulated amount by almost 40%. For a charging structure of this type to give good value, Daykin says the charge needs to be quite small (e.g., 0.5% or less).118

No law requires plan administrators to select plan investment options with the lowest fees available, but plan administrators do have a responsibility to make sure the fees charged are reasonable in terms of the quantity and quality of services provided. In the United States, there have been a number of class action suits over the reasonableness of fees. While this issue has not yet arisen to the same extent in Canada, it would not be surprising to see more activity in this area. Plan administrators should negotiate with service providers to reduce the negative effect of fees on worker retirement savings. Benchmark fees with those charged to plans that are similar in size, number of members, employer industry, employer match and asset allocation. Once investment choices are made, monitor the fees regularly to ensure they remain competitive.
A good place to start an examination of fees is investment expenses. Low-cost index funds might be an appropriate alternative to more costly actively managed funds. Index funds are mutual funds composed of securities selected to mirror a designated market index (e.g., S&P/TSX Composite Index, Vanguard Canadian Aggregate Bond Index). Historically, passively managed index funds have outperformed the majority of actively managed mutual funds. Any fees that add little value in terms of investment return or service might be lowered or eliminated. Perhaps the plan is paying for features or services that members are not using.

Beware of the wide range of payments for different asset managers and investment vehicles; there are situations where a minority of workers is paying the majority of plan costs. Even members with the same account balances may be paying significantly different amounts for plan administration. Plan expenses should be distributed across the plan population in an equitable manner. Conducting a detailed analysis of plan fees helps an administrator determine whether certain workers are shouldering a larger percentage of fees than others are. Ideally, administrators can select a set of funds with no reimbursement for administration included and, instead, deduct the fees needed to cover administrative expenses equitably across all asset classes.

Plan administrators that have or are considering annuities as lifetime income generators should not overlook the special fees associated with these accounts. Members pay a fee referred to as a mortality and expense risk charge to compensate the insurance company for various risks it assumes under the annuity contract such as the life expectancy of the annuitant.

**Goal 4: Help Workers Stay on Track**

Life happens. Any number of events can result in an individual failing to implement steps in a retirement plan or going off track. Employers and plan administrators should review their total benefits package to consider where changes might be made that could reduce this leakage and have a significant impact on the ability of workers to achieve their retirement objectives. Expanding worker education regarding retirement plan features, assistance with plan rollovers and instruction on general money management may also have a positive impact.

**Assist With Rollovers**

When DB or DC plan members with vested benefits change jobs, they typically have choices that depend on the plan design. They may be able to:

1. **Take a lump sum if they are not vested and locked in.** For most employees, the worst option is to take the funds out as a lump sum and then spend it or invest it in a nonretirement savings account. With this decision, the member pays taxes on the funds and, sometimes, an early withdrawal penalty. The amount set aside for their retirement is reduced and the long-run opportunity for the money to compound tax-free is taken away. The ultimate consequence is that the amount the worker needs to save during the remainder of his or her working years increases.

2. **Leave savings in the former employer’s plan.** While this option may make sense for workers who have many years with the same employer, there are disadvantages for workers with small account balances and those who have changed jobs multiple times. Since most plans are priced on the average account balance, a collection of small accounts may result in higher management fees than if savings were all in one place. When there are many years until retirement, workers also run the risk of simply forgetting an account exists.
3. **Move to a new workplace plan.**
   The third option for terminating employees is to roll funds into a new employer’s retirement plan if permitted. Wide variations in plan rules and policies governing how rollovers are handled can make fund transfers complex and frustrating for employees.

4. **Transfer the funds to a tax-sheltered RRSP.** With this option, funds remain tax-sheltered. If the funds from the previous employer’s plan are locked in, they can be transferred to a locked-in RRSP or similar vehicle. *Locked in* means the funds cannot be withdrawn and must be used to purchase an annuity or transferred to a Life Income Fund.

Plan administrators can help employees use the third choice by designing their plans to accept transfers and by encouraging members to ask a subsequent employer if this is available. Keep in mind that plan administrators as well as current and former employees can benefit when help is provided with rollovers. Sponsors reduce the number of plan statements they must disseminate and the chance they are going to have difficulty keeping track of former employees.

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**Offer Other Benefits That Help Workers Manage Risk and Increase Savings**

It is easy to overlook the substantial impact that elements of a worker’s benefit package other than a retirement plan can have on the ability to save for a secure retirement. Such benefits typically support retirement planning in one of two ways: (1) helping workers cope with life’s surprises that can wreak havoc on an individual’s finances and (2) providing funds for other financial goals that often compete with achieving retirement goals.

- **Life insurance** or another type of death benefit is a relatively low-cost way to help a surviving spouse stay on track saving for retirement if a worker dies before retirement. Many workers are provided basic life insurance in the workplace at no or a limited cost. Workers may be given the option to purchase additional coverage for themselves and their spouses at group rates lower than what would be available if they tried to purchase protection on their own.

- **Disability protection** provides periodic payments to workers who are unable to perform the regular duties of their jobs or any occupation for which they are suited by virtue of their education, training and experience. These payments may be paid through a life, disability or workers’ compensation plan. Protection may also be provided as part of a retirement plan so that benefit accruals, qualifying service or contributions continue if a plan member is totally and permanently disabled prior to normal retirement age. When considering this option, be sure to investigate how disability coverage provided by CPP/QPP might offset this private coverage.

- **Medical, vision, dental and hearing benefits** help workers and their dependants deal with unpredictable but inevitable health expenses. Travel insurance that covers a person while in another country could spare individuals the significant expense that could result from a medical emergency.

- **Long-term care (LTC) insurance** is offered by some employers to supplement coverage provided by the public health system. While some employers pay for the benefit, others give employees the option of purchasing their own coverage through their employer. In the latter case, coverage may be offered not just for the employee but also the employee’s spouse, partner, parents and in-laws. A group policy also opens up opportunities for LTC coverage with a lower premium.
• **Emergency loan programs and hardship funds** can help workers in financial crises who have exhausted other means of obtaining financial assistance—avoiding withdrawals from an RRSP, DPSP or similar plan.

• **Employee assistance programs** increasingly offer services and resources to help workers deal with financial issues, in addition to personal and family issues. Assistance ranges from coaching to address concerns such as budgeting, loan repayment and debt consolidation to advice on financial planning and investment options.

• **Education assistance programs** partially or fully reimburse employees for education and training expenses. The development of a worker’s skills is the foundation for ongoing employment, career advancement and meeting retirement savings goals. Such a program can also help workers garner knowledge and skills that will enhance their chance of employment after retirement. Many young workers are burdened with substantial college or university debt. An employer might consider programs for debt retirement, such as employer assistance for education loan repayments. Some plan administrators also help fund the college education of a worker’s dependants. Every dollar given for education represents a dollar a worker can shift to a retirement savings account.

• **Registered Education Savings Plans (RESPs)** provide an easy, no-cost way for employers to help parents save for their children’s education through payroll deduction. An RESP allows after-tax contributions to be paid into a fund that grows tax-free. When it is withdrawn, it is taxed at the recipient’s tax rate. Since the recipient is normally a postsecondary student, there will be little if any tax. The government also supplements RESP contributions by matching 20% of the first $2,500 in eligible contributions made to the RESP—free money. Group RESP enrolment is completely optional for employees, and employers can work with a provider of their choice.

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**Make Personal Finance Information and Education Available**

Until recently, the focus when educating retirement plan members was limited to introducing plan features and how to enrol. Employers and plan administrators are starting to realize achieving retirement security cannot be isolated from other parts of a person’s financial life.

An increasing number of employers and plan administrators are embracing a more holistic approach to retirement security that includes personal finance education. Such efforts align with a 2010 recommendation by Canada’s Task Force on Financial Literacy encouraging employers to incorporate financial literacy training into workplace training programs and communications.119

Areas that often have the greatest impact on retirement savings and for which there is the greatest need for education include:

- Creating and managing a budget
- Managing credit/debt
- Saving and borrowing for the purchase of a home
- Saving for a child’s education
- Acquiring sufficient insurance coverage
- Saving and investing for retirement
- Reducing taxes.

Another potential role of financial education is to help individuals assess their abilities to make personal financial decisions including those related to retirement preparedness. To help members maximize the benefits from financial professionals, members can be provided:

- Recommendations on when to seek advice
- Characteristics of a good advisor
- Common questions they might ask an advisor.

A survey commissioned by FinFit found that with the help of a financial wellness program, 66% of employees said they were able to increase their monthly savings—31% increased their savings between $1 and $50, 25% by $51 to $200, 7% by $200 to $400 and 3% by more than $400.120
Goal 5: Assist Those Near Retirement to Make the Transition

Many aspects of retirement planning are not fully understood by preretirees—After all, most individuals make the decision to retire only once in a lifetime. When poor choices are made, they can’t always be corrected, and the consequences may affect people—as well as their life partners—for the rest of their lives. Making the right choices can also be the difference in whether individuals are able to pass some of their assets to others as part of an estate. There are specific actions that employers and plan administrators can take to help those near retirement understand the options available to them and make informed decisions.

Help Preretirees Assess Different Retirement Scenarios

Workers’ decisions on when and how to retire affect (1) when they stop saving for retirement, (2) the income they receive from both workplace and government benefit programs and (3) when and how they start drawing on their retirement savings. Plan administrators are encouraged to make a concerted effort to ensure those closest to retirement have a realistic, comprehensive plan that takes into consideration different life scenarios.

Exhibit 9 offers a preretiree checklist suggesting issues to address as part of this endeavor. A mix of programs and services may be required. Some employers provide preretirement seminars to workers about five to ten years before workers plan to retire. Given some workers begin to seriously think about retirement 20 years in advance, earlier efforts may also be appropriate. Print worksheets, online modeling tools and one-on-one meetings with a financial advisor are among the other tactics used depending on the characteristics, needs and preferences of the workers. Some plan members might feel comfortable making their own decisions by independently studying materials. Others may prefer working with a financial advisor who can help them make choices.

Exhibit 9 | Preretiree Checklist

Before an individual retires, employers and plan administrators should help workers:

• Determine their retirement expectations with respect to work, leisure, care for loved ones, etc.
• Identify the pros and cons of lump-sum distributions and decumulation options
• Analyze how much income it is reasonable to expect from their workplace retirement plan(s), government benefits and personal savings/investments
• For those who plan to work during retirement:
  – Assess what job opportunities will most likely be available to them
  – Identify the skills they will need to develop or update to be employable
  – Forecast the income they will be able to generate from this work.
  – Examine the tax and other implications employment may have on their retirement income (e.g., payments to CPP/QPP after 60 for a postretirement benefit).
• Consider how changing their retirement date, when they claim benefits and the amount of time they work during retirement might affect their income.
• Assess the risks associated with retirement—particularly longevity, investment and inflation risks. Identify what strategies can be used to manage these risks, including the pros and cons of each.
• Identify and assess the impact of any debt that will carry into or be incurred during retirement
• Develop a contingency plan if they find a cognitive or physical decline impacts their ability to handle their finances and other day-to-day activities
• Create an expense plan that takes into consideration the additional costs they may incur during retirement—especially health care and long-term care—and how expenses may fluctuate over time.
• If they have a spouse, life partner and/or dependants:
  – Examine what savings and benefits these other persons will contribute
  – Assess how income and expenses would change for survivors if any of these persons die
  – Identify any death benefits available to survivors.
Create Opportunities for Transitional Employment

For individuals who have insufficient funds set aside for retirement, working longer than the typical retirement age may be critical. Other people want to continue working on a part- or full-time basis just to stay active. To help these employees, consider modifying workplace practices and policies to permit a gradual transition into retirement. Organizations that have people near retirement with knowledge and skills that are in short supply may benefit from the policy changes as much or even more than the employee.

Whether phased retirement is a formal program or an informal arrangement, it might include any one or a combination of the following features.

- Retraining or updating worker skills
- Employees working on a reduced or modified basis as they approach retirement
- Work more suitable to older workers (e.g., less stressful or physically demanding)
- Permitting employees to collect some portion of their retirement benefits while continuing to work.
- The reemployment of those who have retired
- Employer-provided health care coverage.

Some employers will want to keep their own employees while others will be tapping employees who worked elsewhere.

Offer Retirement Income Options and Guidance

With the increasing use of DC and other self-directed retirement plans, there is a growing realization that more consideration must be given to *decumulation*—managing and spending these accounts after retirement. Like the accumulation of plan assets in many of these plans, decumulation requires plan members to make complex decisions involving the unknown—their future health, longevity, return on investments, inflation, etc. Some DB plan members face similar choices if their plans offer retirees a one-time lump-sum payout as an alternative to a monthly payment for life.

The federal and provincial governments have established several vehicles or *retirement income options (RIOs)* where funds from registered retirement accounts can be moved when a saver wants to start making withdrawals. RIos fall into two types: (1) retirement income accounts and (2) annuities. Exhibit 10 summarizes the circumstances when the various RIos can be used and some of the rules that apply to their use.

<table>
<thead>
<tr>
<th>Exhibit 10</th>
<th>Retirement Income Options</th>
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<td>The most common type of retirement income option (RIO) chosen by Canadians is a Registered Retirement Income Fund (RRIF)—probably because their source, Registered Retirement Savings Plans (RRSP)s, are very popular. Money in an RRSP must be converted to an RRIF or an annuity by the time the account holder reaches age 71. Like an RRSP, there is a variety of investments that can be held in an RRIF and the assets grow tax-free. While the Canada Revenue Agency (CRA) mandates account holders take a minimum amount each year, withdrawal can be as often as desired. Funds in an RRIF are taxed as income only when they are withdrawn.</td>
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<td>Individuals with certain other registered retirement accounts such as locked-in RRSPs are required to roll their assets into an annuity or a Life Income Fund (LIF) by the year they turn 71. LIFs have a minimum and maximum withdrawal schedule that is calculated differently from that of an RRIF, and the amounts change each year, but there is still some withdrawal flexibility. Any funds that remain at the time an account owner reaches the age of 80 must be used to purchase an annuity.</td>
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<td>Locked-in pension funds are placed in either a Locked-in Retirement Savings Plan (LRSP) or a Locked-In Retirement Account (LIRA). LRSPs and LIRAs are different from LIFs in that the maximum payments are based on the investment returns, not the account owner’s age or current interest rate. In addition, there is no requirement the owner purchase an annuity at age 80. What determines which one of these retirement income options must be used is the pension legislation governing the individual’s locked-in savings. The CRA establishes the minimum withdrawal each year while provincial rules determine the maximum that can be taken out.</td>
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<td>When an annuity is purchased with funds from a registered retirement account or retirement income fund, payments are taxable as income. Persons who wish to purchase an annuity with nonregistered funds can buy a prescribed annuity—only the interest, not the return of capital, is taxed with payments from these policies. Each payment includes the same amount of interest and capital to even out the amount subject to tax and provide some tax deferral.</td>
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For those who want to maintain control over some or all of their assets, a retirement income account is most appropriate. Within minimum/maximum limits established by government, retirees can decide how they will withdraw their funds. Common strategies to help ensure a person does not outlive their assets are to (1) limit withdrawals to investment earnings and (2) make systematic withdrawals at a predetermined rate.

With the second type of account, annuities, a policyholder has to do little more than wait for the regular payments to arrive. Buying an annuity from an insurance company, in effect, is a strategy to guarantee a stream of income payments as well as an RIO. Exhibit 11 provides more detail concerning a retiree's decumulation strategies.

No single strategy for decumulation is appropriate for all individuals. Each option has pros and cons—and the income a retiree receives significantly depends on the strategy chosen. It is not uncommon for a combination of strategies to be the best choice. Unfortunately, the number of choices is so complicated that too many individuals choose nothing.

Another concern is the expenses individuals incur with decumulation. It is estimated that 80% to 90% of Canadian retirement savings is turned into income at retail prices. Furthermore, the resulting retirement incomes are 20% to 30% less than what they could have been if institutional fees and fiduciary oversight had been applied. Plan administrators are in a strong position to negotiate better group pricing to deliver more income and/or protect the remaining wealth of members than individuals would be able to get on their own via the retail market.

Exhibit 11 | Decumulation Strategies

There are three basic approaches to turning all or part of a worker's accumulated assets into retirement income. Each method can be implemented using a variety of financial instruments and/or tactics.

1. **Investment earnings.** The retiree withdraws just the interest and dividends received on invested assets—the principal is left intact. Realized capital gains are typically reinvested but are available to spend if needed. This may be an appropriate strategy for those who want to leave funds to their heirs and feel they will have sufficient money set aside to generate the income they need without dipping into their account principal at some point during retirement. Individuals must have the knowledge and willingness to manage their investment portfolio or seek the assistance of professional management.

   A downside to this approach is that poor investment returns can force a retiree to dip into his or her principal if the return on investments is less than anticipated; there is no guaranteed income stream. As with the investment earnings approach, retirees are able to maintain some control over their funds.

2. **Level income.** Assets are invested with a fixed dollar amount (with or without adjustments for inflation) withdrawn over time. This strategy is often referred to as a 4% withdrawal program, but the percentage must be adjusted to factor in variables such as the retiree's age, anticipated market returns and investment volatility. A 4% withdrawal rate assumes a relatively aggressive investment portfolio that includes stocks. For retirees heavily invested in fixed income vehicles such as bonds and certificates of deposit (CDs) that provide a lower return, a rate of 2.5% or even lower might be more realistic.

   The downside to this approach is that poor investment returns and/or high longevity can cause the invested assets to be depleted during the retiree's lifetime. Again, there is no guaranteed income stream. As with the investment earnings approach, retirees are able to maintain some control over their funds.
3. **Annuity.** An individual transfers some of his or her savings (and longevity risk) to an insurance company that guarantees a lifetime income. A common strategy is for retirees to annuitize what they estimate they will need to supplement their income from government programs and defined benefit plans for basic living expenses. This leaves other assets available for large purchases and emergencies.

Annuities are the only one of these three options that can guarantee a retiree a monthly income payment for life. Available for purchase at or after retirement, annuities are available with a combination of features. Buyers can choose between an annuity providing income for life and one that pays for only a specific period.

- **Life annuity** — a fixed stream of income that is provided for the life of the policyholder.
- **Fixed term annuity** — also referred to as *term certain annuity*, this type of insurance policy provides a fixed stream of income for a preset period—perhaps 10 years, 20 years, etc. In some situations, there may be a stipulation that the term can’t extend past a certain age.

There are also annuities that have the potential for increased payments over time.

- **Inflation-adjusted income annuity** — a guaranteed stream of income for the life of the policyholder is provided with the payment amount tied to changes in a consumer price index. These annuities initially provide a lower monthly income amount than a fixed income annuity, but the amount has the potential to surpass that of a nonindexed annuity because of inflation.
- **Variable annuity** — an income for the life of the policyholder is provided that varies with the performance of the underlying investment portfolio managed by the insurer. If the assets in the portfolio perform well, there is the possibility of larger payments. An annuity of this type may come with a *guaranteed minimum withdrawal benefit (GMWB)* that promises a base amount of income regardless of how the underlying investments in the annuity have performed. There is a trade-off with a GMWB—The payment guaranteed is substantially less than the fixed amount provided by a life annuity.

Survivor benefits are available through additional policy provisions.

- **Joint life annuity.** This product provides an income as long as the policyholder and his or her spouse/partner are alive. After the death of either person, payments continue for the life of the other. Persons who use a registered pension or locked-in RRSP fund must purchase this option unless the spouse/partner is permitted to and does waive this requirement with a signed consent. Joint life annuities can also be used to continue payments for the life of a person other than a spouse or partner.

- **Guaranteed payment period.** Those considering the purchase of an annuity often worry they might die right after they purchase the policy—leaving nothing to their heirs. With this option, payments are promised to a beneficiary if the person or persons covered by the policy die before the end of a period identified in the policy.

- **Cash refund guarantee.** This policy feature provides a refund of any principal remaining from the original investment amount at the death of the policyholder to a spouse, partner or other beneficiary.

It is important to realize that the more guarantees and flexibility provided by an annuity, the higher the fees or the lower the retirement income. In addition, not all options may be available everywhere.
In an article for *Benefits Canada*, Jean-Daniel Côté asserts that the fear of increased fiduciary responsibility has kept most plan sponsors and administrators away from helping members with the decumulation phase of group retirement savings arrangements. He suggests an increasing number is starting to get involved due to:

- Increased longevity and the high fees that come with retail products that negatively impact members.
- A large number of employees retiring in the next five to ten years, largely on the savings in their DC plans.
- Unionized environments, in which delivering better retirement outcomes will increase union willingness to transition from a DB to DC plan.
- The new CAPSA Guideline No. 8 urging sponsors to consider the payout phase—encouraging them to assist "members in making informed decisions, which strikes a balance between protections from the risk inherent in various products, and achieving target replacement rates."122

Côté says helping members with decumulation can take many forms and does not necessarily increase fiduciary risk. He provides these examples in increasing order of complexity/involvement by the sponsor/administrator:

- **Ask the DC plan provider about the transition services it offers.** Most are gearing up to ensure they capture member assets at retirement by improving their offerings. Advice from a provider is often free, but providers must be asked hard questions given their advice will not necessarily be independent and may have fiduciary implications for a plan sponsor/administrator.

- **Bring in an independent expert.** This person can explain the pros and cons of options with no hidden agenda to sell products. While this approach is not free, the costs can sometimes be paid through a governance account (i.e., an investment management fee paid by members).

- **Review target-date solutions.** Make sure the funds offered go "through" retirement, not just "to" retirement.

- **Reduce member fees during retirement.** Retail fees are high and can severely reduce retirement income. Negotiate lower investment management fees with the DC plan provider. Some sponsors have also been able to negotiate reduced pricing on annuities.

- **Set up group options.** Keep retiree assets under one umbrella by establishing an RRIF/LIF to be part of the sponsor contract. This may result in lower fees for all DC members and may permit the addition of a different set of funds that are a better fit for retirees. The investment options designed for accumulators may not be the best choices for those looking to decumulate. The one downside of this approach is an increase in governance burden.

- **Pay a pension out of the DC plan.** Some jurisdictions allow LIF-like or variable-annuitylike benefits to be paid directly from a plan. Most who have embraced this option have been universities and others in the public sector due to the extra costs and the governance requirements.123

For plan administrators considering offering income-generating options, Exhibit 12 suggests questions for a plan administrator to ask when evaluating which options to offer.

By offering information and guidance regarding RIOs and decumulation, plan administrators increase the likelihood plan members will make decisions appropriate to their individual circumstances. Information that is particularly useful includes:

- What RIOs are available for different retirement savings accounts
- Strategies for decumulation
- The risk associated with various choices
- The amount of retirement income that is reasonable to expect under different scenarios.

In addition, education may be required to help workers overcome the perception of annuities as investments that require people to give up a lot today with an uncertain return. Framing annuities as buying insurance that guarantees lifetime payments versus investing can positively affect how many individuals are willing to purchase annuities.124

For those who plan to buy an annuity, it is essential purchasers understand they are relying on an insurance company to make payments for decades. Advise these workers that buying a policy from a large, well-established and well-capitalized company is wise. The company should also be a member of Assuris, the industry-sponsored guarantor, with a guarantee limit of up to $2,000 a month or 85%, whichever is larger.
Exhibit 12 | Choosing Retirement Income Options and Their Providers

When choosing lifetime income solutions to offer plan members, the process for the plan administrator is much the same as with any other fiduciary decision. A rigorous and documented process for evaluating and monitoring offerings must be established. The primary difference is the type of information reviewed. While factors to assess also vary with the type of RIO and its source, these are some common questions to ask:

- How much income is provided to retirees? How does this income compare with that from other sources?
- Who determines the amount provided as income?
- Can the income amount be affected by investment volatility or changes in interest rates before or during retirement?
- Is there a potential for an increase in income to counter the impact of inflation?
- Is the income guaranteed for life?
- Is there an option that guarantees income for at least a set period?
- Who controls the investment of assets used to provide the income?
- What has been the historical return on the investments providing the income relative to the risk?
- Can savings be accessed by the member after retirement income has started?
- Can any assets remaining at the death of the retiree be passed to survivors?
- What types of services are provided to workers, retirees and the plan administrator (e.g., administration, communication, education) by the financial institution providing the product? What is the quality of these services and are there any restrictions on their use?

- Are the fees, commissions and other costs of the product and associated services reasonable? How do they compare with those from other sources?
- What has been the financial institution’s experience with similar products?
- How long has the institution offering the product been in business?
- Overall, is this option appropriate for both the plan and the members served?
- When a professional will manage the assets and no income guarantees exist, there are special concerns.
  - What is the experience and credentials of the investment management team?
  - How stable is the management team?
- When the provider is an insurance company promising to provide an income to members for as many as 30, 40 or even more years, the financial soundness of the company is essential. A plan administrator must evaluate whether the company will be able to make all of these future payments.
  - What is the company’s level of capital, surplus and reserves?
  - How has the company been rated by the various insurance rating services over several years and economic cycles?
  - Is the company a member of Assuris, the nonprofit organization that provides protection on annuities up to $2,000 per month or 85%, whichever is larger?
  - When an annuity is needed that is greater than the Assuris protection limits, can the purchase be laddered with several insurers to ensure full coverage?
Offer Health Insurance Options and Guidance

Many employees do not know what health and dental coverage they will need in retirement, if any. They also do not know what individual products and services could help them meet their needs. Because their employer paid most, if not all, of their group benefits coverage, employees also have little knowledge of the cost of individual coverage when they retire. Employers and plan administrators can help individuals determine their future health needs and the costs of purchasing coverage. Most group insurers offer individual coverage for plan members who are retiring. Employers and plan administrators can direct preretirees to information regarding these and other products that might be appropriate when they retire.

Effective Communication: Another Key to Success

A thread that runs through all workplace strategies to promote retirement security is communication. How information and new initiatives are framed and delivered can make or break the most well-intentioned efforts. Effective communication is optimistic and action-oriented—inspiring people to plan and save for their retirement.

Fortunately, employers and plan administrators don’t have to go it alone in the communication process. Investment fund managers and third-party administrators often have education specialists and financial advisors on staff who can offer educational services for little or no charge. They may also have content that can be used as is or with minor modifications. Other potential sources of help include benefit and communication consultants, public relations and advertising people, audiovisual producers, editors, IT personnel, those who directly supervise/serve workers and even some plan members.

When developing communication tactics, begin with an analysis of the objectives to be accomplished. Establishing communication objectives that are clearly understood makes it easier for everyone involved in the implementation and increases the likelihood of success. Sample objectives might be to:

- Inform individuals how to enrol in their workplace retirement plan
- Encourage more participation and higher savings in the organization’s retirement plan
- Increase the number of individuals using a retirement program or service
- Involve spouses/life partners in the retirement information and decision process
- Raise the number of workers who achieve a secure retirement
- Meet legislated and regulatory disclosure requirements
- Develop increased worker appreciation for their retirement benefits.

Finally, don’t forget that every communication has legal implications either as part of a promise made in an employment contract or as a statement of fiduciary obligations. Communications should be reviewed by legal counsel for consistency with plan documents as well as regulatory compliance.
**Know the Audience**

Sponsors and administrators need to understand where workers are in terms of financial preparedness and needs so they can adapt their communication plans to address specific needs. Working with recordkeepers can yield data concerning plan participation and current retirement savings. Ideally, data in reports can be broken down by gender, age, income, education, language, ethnic background, etc., to identify specific groups for messages that motivate individuals to take the steps needed to achieve a secure retirement. Questions that might be asked are:

- Who is eligible but not enrolled in the retirement plan?
- Who is participating, and how much are they saving?
- Who is saving enough to get the full organization match?
- Who might be better off putting savings in a TFSA vs. RRSP?
- Who is invested in funds with lower expected rates of return?
- Who has a portfolio that is not diversified, and where are they putting their money?
- Who is at risk of not achieving a secure retirement?
- Who is probably within ten or 20 years of retirement?

Getting to know an audience also involves listening to workers. What do they already know? What misperceptions do they have? What do they want or need to know? How do they want to get information? Among the ways to learn about workers’ knowledge, attitudes and needs are:

1. Interviews
2. Focus groups
3. An advisory group
4. Questionnaires—administered by mail, e-mail or in person
5. Analysis of inquiries that come to the plan office
6. Tracking use of website content and other information/education efforts
7. Discussion and questions at meetings.

Workers have life experiences and knowledge that have the potential to enhance or thwart communication. Former experiences can make a message more meaningful. Conversely, a bias or experience can impede efforts to help members. Communication strategies and educational programs must acknowledge and build on the interests, knowledge and experiences of plan members.

**Target Messages**

To be effective, communications must consider worker differences. Once again, one-size-fits-all efforts rarely work. Specific groups of middle-income and young persons that should be saving might be targeted as follows:

- **Nonenrollees.** Persons who are eligible and would benefit from plan participation but are not yet enrolled should be given messages that promote enrolment in a plan appropriate to their specific income level. For workers in their 20s, the emphasis might be on the value of starting to save early for retirement. With older and higher paid workers, messages might emphasize pretax savings. Recent immigrants may need help understanding and trusting financial products and/or institutions.

- **Contributors with low savings rates.** Messages designed to boost savings should be aimed at those who are not saving enough for a secure retirement—especially those who are not contributing enough to take full advantage of a sponsor match.

- **Members whose assets are not diversified.** Persons who are inappropriately diversifying their funds should be educated on the benefits of diversification and the options available to them to diversify such as automatic rebalancing and the selection of a target-date fund. Young persons who have a large proportion of their assets in low-risk/low-return investments should be cautioned they are on a path that may result in insufficient retirement resources. Individuals near retirement with an extremely conservative or aggressive mix of assets in their retirement portfolio can be cautioned regarding inflation or investment risk, as appropriate.

- **Women.** Given women often live longer than men and spend more time as retirees, messages that point out they must factor in extra years when planning for retirement are appropriate. Other topics that may be appropriate are discussions regarding divorce, widowhood and caregiving—all issues that tend to financially affect women more than men.
Exploit Multiple Delivery Channels

In the past, communication regarding saving for retirement primarily took the form of print materials including an annual retirement plan statement. A group seminar might have been offered for those close to retirement. Communication routes have dramatically expanded in recent years, and plan administrators must take advantage of more of these channels to reach workers effectively. The availability of the Internet and mobile technology makes it possible to reach workers no matter where they are located all day and every day. Among the communication choices now available are:

- Quarterly or annual retirement plan statements
- Brochures, fliers and posters
- Newsletters and mail stuffers
- Posters
- E-mails
- Podcasts
- Blogs, text messages and other social networks
- Mobile apps
- Websites
- Staff meetings
- Webcasts and in-person workshops
- One-on-one meetings or phone calls with a professional advisor
- New employee orientations.

Employers report some modes of communication are more effective than others. When the Conference Board of Canada asked employees what they considered the most effective methods for communicating retirement savings and pension plan information, mandatory sessions topped the list (68%), followed by optional sessions (52%). At least 40% of respondents also identified one-on-one financial educational sessions, organization intranet/plan websites and employee orientation/staff meeting communications (in that order).126 Keep in mind that factors such as an employee’s age, education, culture, income, etc., can affect a person’s preferences for information delivery.

Anecdotal evidence suggests that online “retirement savings games,” where participants can move through different levels, compete with each other or share their accomplishments with others, may be an important solution in changing behaviours and stimulating participation and saving—particularly among younger workers. Sun Financial’s introduction of a new gaming product has been found to increase both the number of employees saving for retirement and the amount being saved.127

Tap Multiple Messengers

Plan administrators should consider cultivating employees who are “centers of influence” within their organization to encourage others to share why they think it is important to plan for retirement. Managers, union representatives and peers respected by fellow employees can help create a culture that makes planning for retirement the right thing to do.

A small number of individuals from a targeted group might be trained and given materials to reach out and educate others in the group. Not only may workers be more receptive to information from these influential persons, these persons can serve as role models demonstrating that those who plan and save can achieve a secure retirement.

Testimonials by trusted individuals are especially effective. Many people think statistics are the way to get people to change attitudes or behaviours, but testimonials almost always trump eye-popping numbers and logic. Personal stories are more likely to resonate with the recipients.

There is one caveat in adopting these tactics. Make sure messengers understand that their role is to tell their personal stories and direct people to other sources of information—not interpreting plan obligations, endorsing a product or providing investment advice. Such communication could have unwelcome legal implications for employers and plan administrators.

Tapping outsiders may also be helpful. Some employees think they already have heard what their plan administrator has to say. They may think a plan administrator or vendor has an agenda that is not in the best interest of workers. In these situations, an independent, unbiased third party that doesn’t sell products can increase employee confidence in a message and a retirement plan. Outsiders can also reduce an organization’s liability with respect to providing financial advice.
**Keep It Simple**

Oral communications are often easier for members to understand than written ones. There are occasions, however, when written information is the only realistic option; for example, the law requires a written format for benefit statements. To increase the likelihood persons targeted will (1) actually read/listen to what is presented and (2) comprehend it, it is essential information be presented in a way that can be understood by the typical member.

- Keep it short and focus on a few key points.
- Avoid jargon and legalese whenever possible.
- When technical terms must be used, include clear and simple explanations.
- Provide examples and real-life stories that support the main points.
- Insert simple graphics to make presentations more interesting.
- If English is the second language for a significant portion of the target population, communicate in their native language.

People have difficulty focusing on complex topics for more than seven to ten minutes. Keep this in mind for workshops, seminars, webcasts, etc. For longer programs, occasionally switching presentation tactics helps keep members engaged. Use multiple presenters, look at a video clip, break into small groups to discuss an important topic or have members complete a worksheet. All of these techniques help break up the program.

**Find the Right Time**

Benefit statements and other required notices give administrators regular opportunities to communicate with members. They can be used for anything from providing information on new plan features to reminding members to consider rebalancing assets. Nonetheless, this should not be the only communication between a plan administrator and members. Information is often set aside or forgotten when it is not provided at a point when a member needs it. The right time to provide information tends to be when individuals are faced with a decision. For example,

- **New hires.** When new employees are asked to enroll in their workplace retirement plan, plan administrators provide information on plan features, any employer match and the immediate tax implications of member choices. This is also a good time to encourage workers to seek advice to determine how much they should be saving, if anything. The process might be part of an employee orientation or a separate program dedicated to retirement security.

- **20- and 30-somethings.** Emphasize the importance of saving early, the value of compounding and continually increasing the amount saved.

- **40-somethings.** Four in ten retirees (42%) say they began to plan for retirement 20 years before they planned to retire. Almost three in ten more report they started planning ten to 19 years before retirement. Target these early planners and encourage them to assess their progress toward retirement. If they haven’t already done so, this is also a time to consider what they want to do in retirement, adjustments to savings levels, the asset mix in their portfolio, etc.

- **50-somethings.** As individuals begin to look at their future with greater depth and intensity, provide them with information and programs that can help them make the transition into a secure retirement.

Letting workers access information and educational programs at their convenience and/or when they decide they need to is also effective. Delivery methods that do this well include recorded educational programs, employee hotlines and websites.
For those who say they don’t have time to think about retirement or are intimidated by the process, tell them why it will take as little of their time as possible. Emphasize how simple the process can be and who is available to help them.

*Put Worker Concerns First*

Closely related to the timing of messages is focusing on the issues that most interest the target audience. Are they most concerned about paying for current day-to-day expenses? Managing their debt? Funding the education of their children? Emphasizing what is important to members will grab their attention and help motivate them to take action.

If some of their goals conflict with saving for a secure retirement, offer solutions that might make it possible for them to accomplish both—for example, suggest sources of debt counseling or alternative resources to help them plan for college funding. In some situations, it may be more effective to offer a program on personal finance (e.g., eight ways to stretch your paycheque) and weave in a message or two on saving for retirement.

For those who say they don’t have time to think about retirement or are intimidated by the process, tell them why it will take as little of their time as possible. Emphasize how simple the process can be and who is available to help them.

*Stress What Will Be Gained or Lost*

One of the chief tenets of behavioural economics is that people are loss averse. People are highly motivated to avoid what they consider a loss. In fact, losing hurts worse than winning feels good. To spur action, frame messages so workers will clearly understand how they might “gain” by taking action or “lose” if they don’t do something. For example:

1. Planning for retirement is how dreams become reality. (Gain frame)
2. Give your retirement savings a boost—five ways to increase your savings that will cost you nothing. (Gain frame)
3. Make your money work for you—Take advantage of compounding! (Gain frame)
4. Would you like a 5% pay increase? Take advantage of your retirement plan match. (Gain frame)
5. Just say NO! Stop missing out on your retirement plan match. (Loss frame)
6. Would you rather pay yourself or the government? Increase your retirement savings and cut your taxes. (Loss frame)
7. Get the government to contribute to your retirement savings. (Gain frame)

Messages 4 and 5 show how the same point can be made using either a gain or loss frame. Some people may be motivated by one type of frame and not the other, so consider using them in different messages. However, don’t try to use both in the same message.
Point Out What Others Are Doing

When making choices, people tend to do what they think most other people are doing. If they do what other people are doing, they believe there is less chance they will make a mistake. They are also influenced by what they think is expected or socially acceptable. Using these social norms can help drive people to take specific actions. Consider these two messages to induce employees to save for their retirement:

1. 80% of ABC employees contributed to their retirement plan last year.
2. Nine out of every ten new hires say “yes” to saving 15% of their pay for their retirement.

The more similar the people described in a message are to those being targeted (e.g., co-workers in the same building), the more likely people are to copy the behaviour desired.129

What happens if an organization doesn’t have positive statistics? Use a message that promotes the desired behaviour. Just as companies have forbidden employees from smoking in the workplace and using cell phones while driving, an organization can tell workers that saving for retirement is something that is valued. For example:

ABC Inc. is committed to supporting our employees on the road to a secure retirement. We will provide savings choices, information, education and other tools that will make it possible for our employees to achieve a life after employment that is gratifying and financially secure.

Contrary to what many believe, facts and figures on bad behaviours are rarely helpful. Consider this news headline:

Canadians Should Be Saving More: Do you want to eat cat food in your golden years?

Using such messages is an attempt to shock the audience into taking action, but it frequently has the opposite affect: “A lot of other people like me aren’t saving for retirement, so I don’t have to do anything either.” Another element of this headline is the effort to scare people—People who don’t save for retirement are going to eat cat food. Scare tactics should be used cautiously if at all.

Offer Incentives

Even after following all of the aforementioned advice, it may still be a challenge to get some workers to take advantage of the programs and materials offered to help them achieve a secure retirement. People have busy lives with competing priorities. Some simply may not care.

One successful program pays workers to attend a half-day event that includes breakfast and a raffle of practical items—T-shirts, jackets, fishing gear, winter gloves and work tools. By the end of the morning, workers sign up online for their retirement plan using laptop computers provided by their employer. Benefit counselors are available to help guide workers through the process.130

Another option is to divide workers into groups and sponsor a competition. The group with the most individuals attending a program or using a retirement planning tool might be recognized with a mention in a staff newsletter, gas cards, a half day of vacation and/or a free lunch. Better yet, ask workers to read a brochure, watch a webcast or attend a program and then take a quiz. The group with the highest average score is rewarded.

A mandatory program is another path to consider. Such a program has parallels with requiring people to get a driver’s license before they are allowed to drive on their own. A “financial license” might be required before workers make their pension choices. Requiring a “license” is an opportunity to introduce the features of a retirement benefit plan as well as other basic financial information that may help workers make their retirement choices.

When making choices, people tend to do what they think most other people are doing. If they do what other people are doing, they believe there is less chance they will make a mistake.
Conclusion

Shifting economic and demographic trends threaten to reduce the standard of living for millions of Canadians in their postwork years. While government programs in Canada are highly effective in supporting low-income households in retirement, these programs were not designed to provide full income replacement for middle- and upper-income persons.

Many are concerned that a significant number of middle-income workers and young Canadians in the private sector are not setting aside sufficient funds to fill the gap that will provide them with retirement income security. Many in this “at-risk” group lack access to—or are not participating fully in—workplace pension plans. Without changes in their savings behaviours, these persons may experience a declining level of living in their postwork years.

Employers and plan administrators can help these persons whose retirement needs may exceed their income. For some employers, the first step is offering a workplace retirement plan—at minimum, creating opportunities for “at-risk” workers to start saving through a payroll deduction plan. When a retirement plan is already in place, employers and plan administrators can partner to help employees (1) determine unmet retirement needs, (2) establish a plan for filling gaps identified and (3) provide support in following through with their plans.

Efforts promoting the retirement security of workers are more than a good thing to do for workers and their families; they can also benefit employers and plan administrators. Such programs can increase appreciation for benefits provided via a retirement plan and an employer’s total compensation package.
Appendix | Retirement Security Strategies Checklist

Check which strategies your organization is presently using to promote the retirement security of workers. Next, consider which ones you might adopt. Some strategies will be more appropriate than others depending on factors such as the benefits you currently provide workers, the characteristics of your organization and the wants and needs of workers.

Goal 1: Help Workers Determine Their Retirement Needs and Where They Stand
- Encourage members to picture their retirement
- Deliver basic retirement information
- Offer calculators and other retirement planning tools
- Provide access to an independent financial advisor at a reduced or no cost
- Provide a regular retirement income statement

Goal 2: Get Workers Enrolled and Saving for Retirement
- Offer a workplace retirement plan
- Reduce plan enrolment waiting periods
- Offer a stretch match for DC plans
- Use automatic enrolment for DC plans
- Use automatic escalation for DC plans
- Simplify DC plan enrolment decisions
- Conduct a program to introduce new workers to their retirement benefits and enrol them
- Leverage competition to motivate worker retirement savings and plan participation

Goal 3: Help Workers Make Prudent Investment Decisions
- Offer a no-option DC plan
- If DC plan members manage their own investments:
  - Offer a target-date and/or a balanced mutual fund that automatically diversifies and rebalances assets
  - Limit the number of investment choices to between five and ten options
  - Structure the menu of investment options to encourage appropriate choices
  - Educate members on the value of diversifying assets and how to do it
  - Discourage members from chasing investment returns
  - Educate members on the value of rebalancing assets in DC accounts and how it is done
  - Check/monitor plan investment expenses and other costs to ensure they are fair and reasonable

Goal 4: Help Workers Stay on Track
- Make it easy for workers to transfer retirement savings from other retirement plans
- Make it easy for terminating workers to transfer retirement savings/accrued benefits to a new employer or retirement benefit program
- Offer other workplace benefits that help workers manage risk and increase retirement savings
- Make personal finance information and education available

Goal 5: Assist Those Near Retirement to Make the Transition
- Help preretirees assess different retirement scenarios and risk management strategies
- Offer members retiree income options
- Check/monitor the fees, costs and risks associated with retirement income options
- Provide members with the information they will need to choose between various retirement income options and the providers of these products
- Create opportunities for transitional employment
- Offer supplemental health insurance and guidance on how to select an insurance plan
Endnotes


6. Ibid., pp. 2-5.


8. Supra note 4.


10. Supra note 5, pp. 2-5.

11. Supra note 7.


15. George Masnick of the Harvard Joint Center for Housing Studies labels those born from 1966 to 1985 as Gen X—in part because it is a tidy 20-year period.


19. Supra note 5, p. 5.


26. Supra note 23.


29. Ibid., p. 46.

30. For example:
   • Chris Flynn and Hubert Lum, DC Plans Underperformed DB Funds (Toronto: CEM Benchmarking Inc., 2006).
   • Towers Watson, Defined Benefit Plans Outperform Defined Contribution Plans Again: Should We Care? (July 2013).


36. Ibid.


41. Scotiabank poll as reported by Mark Goodfield, “Are RRSPs the Holy Grail of Retirement Savings or the Holey Grail?” The Blunt Bean Counter Blog (December 3, 2012).

42. Ibid.

43. Supra note 24, p. 19.


45. Supra note 2, p. 40.


48. Supra note 44.


50. Ibid., pp. 39-40.


53. Supra note 38, p. 45.


55. Supra note 49, p. 12.


63. Supra note 28, p. 52.

64. Supra note 24, p. 26.


68. Ibid., p. 13.


70. Supra note 24, pp. 24-25.


84. Supra note 82, p. 148.

85. Ibid., p. 150.

86. Ibid., pp. 159-160.

87. Supra note 67, p. 8.

88. Ibid., pp. 8-9.

89. Ibid., p. 8.

90. Ibid., p. 9.


93. Ibid., pp. 7-8.


96. Ibid., pp. 16-17.


100. Supra note 82, pp. 61-62.


106. Supra note 82, pp. 43-45.

107. Ibid., p. 118.

108. Supra note 105.


113. Supra note 82, p. 183.


119. Supra note 81, p. 8.


123. Ibid.


126. Supra note 28, pp. 24-25.


