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Mr. Massimo Pacetti

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● (1155)

[*English*]

The Chair (Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.)): Bonjour and good morning, everybody.

Let's just begin. I'd still like to try to keep to the schedule of one o'clock. Since we have fewer members, we can probably get through this.

Mr. Ménard, thank you for coming.

[*Translation*]

Thank you for accepting our invitation.

You will have a maximum of ten minutes to make your presentation. Committee members will then ask you some questions.

Go ahead, Mr. Ménard.

[*English*]

Mr. Jean Claude Ménard (Chief Actuary, Office of the Superintendent of Financial Institutions Canada): Good morning, Mr. Chairman.

Good morning, honourable members of the committee.

Thank you for the opportunity to appear before you today to talk about the mandate and the activities of the Office of the Chief Actuary. Although the office is housed within the Office of the Superintendent of Financial Institutions, it operates independently with a unique role and mandate different from OSFI's.

Our primary role is to provide actuarial services to the federal and provincial governments who are Canada Pension Plan stakeholders. While I report to the Superintendent of Financial Institutions, I am solely responsible for the content and actuarial opinions reflected in the reports prepared by my office. The reporting and accountability framework for the Office of the Chief Actuary establishes this responsibility.

The federal government and the provinces, through the Canada Pension Plan, public sector pension arrangements, and other social programs, have made commitments to Canadians and are responsible for the funding of these commitments. Some are long term, and it is important that decision-makers, parliamentarians, and the public understand these commitments and the inherent risk they present. The Office of the Chief Actuary has a vital and independent role to play in this process. We provide appropriate checks and balances on the future cost of the different pension plans that fall under our responsibilities.

Our mandate is to conduct statutory actuarial evaluations of the CPP, old age security program, and pension and benefit plans covering the federal public service, the Canadian Forces, the RCMP, federally appointed judges, and members of Parliament. Since 2001, we have also performed an annual actuarial review of the Canada student loans program.

Whenever a bill is introduced before Parliament that has a significant impact on the financial status of a public pension plan falling under the statutory responsibilities of the chief actuary, the office must submit to the appropriate minister an actuarial report valuing this impact. I submit these reports as well as triennial statutory actuarial reports to the ministers of finance, social development, human resources and skills development, and to the President of the Treasury Board. The Office of the Chief Actuary also provides sound actuarial advice to these departments to assist them in the design, funding, and administration of these programs.

In the interest of fostering informed public commentary on the CPP, a policy was developed for public or third-party organizations outside of the executive arm of government to provide special information or actuarial work and services related to the CPP on a fee-for-service basis. This policy brings transparency to the existing practice since information provided to requesters is publicly available.

The Office of the Chief Actuary is funded by fees charged for actuarial services and in part by an annual parliamentary appropriation for services related to public sector pensions. We are forecasting planned spending in the main estimates of approximately $4.9 million for the 2005-06 period. This amount is composed of $755,000 coming through appropriations and $4.1 million from cost-recovered services.

[*Translation*]

For the second half of my presentation, which will focus on the Canada Pension Plan and its independent peer review process, I will address the committee in French.

The Office of the Chief Actuary is required by law to produce an actuarial report on the Canada Pension Plan every three years. The federal and provincial governments, as co-stewards of the CPP, have taken meaningful steps to strengthen the transparency and accountability of actuarial reporting on the CPP. In 1997, governments agreed to increase the frequency of actuarial reporting on the CPP from every five years to every three years. The CPP legislation was also changed to require federal and provincial ministers to review the Plan's finances every three years.

You were given the most recent CPP actuarial report that was tabled before Parliament in December 2004. This report is one item considered by federal and provincial finance ministers when reviewing and making recommendations on the CPP. In a past Federal-Provincial Review of the Canada Pension Plan, the ministers of Finance endorsed regular peer reviews of such reports and consultations by the Chief Actuary with experts on the assumptions to be used in actuarial reports.

The current environment for the retirement income system puts an additional onus on the Office of the Chief Actuary to be, and be seen to be, fully accountable and professionally independent. The Chief Actuary and all Fellows and Associates are members of the Canadian Institute of Actuaries (CIA) and are subject to the CIA Rules of Professional Conduct, which identify the professional rules and ethical standards with which a member must comply and thereby serve the public interest. The quality of the OCA work is of utmost importance. The OCA maintains its credibility by adhering strictly to professional actuarial standards. The statutory actuarial reports are prepared by OCA Fellows of the CIA and co-signed with the Chief Actuary to enhance the internal quality control process.

The most recent independent review of the statutory actuarial report on the CPP confirmed that the work of the Chief Actuary meets professional standards of actuarial practice and is of sound quality. The independent review also confirmed that the OCA has adequate resources and access to data and other information required to fulfill its mandate. To ensure the quality of future actuarial reports, the Chief Actuary continues to consult with experts in the fields of long-term demographic and economic projections in the preparation of actuarial reports.

The information required by statute, which is presented in the CPP actuarial reports, requires making several assumptions regarding future demographic and economic trends. The projections included in those reports cover a long period of time, namely 75 years, and the assumptions are determined by putting more emphasis on historical trends than on short-term trends. These assumptions reflect our best judgment and are referred to as "best-estimate" assumptions.

I hope that I have succeeded in providing you with a greater understanding of the actuarial reporting process. I wish to thank you for the opportunity to appear before this Committee and I will be pleased to answer any questions that you might have.

[*English*]

I will be pleased to answer any questions you might have.

Thank you.

● (1200)

Mr. Charles Hubbard (Miramichi, Lib.): Mr. Chairman, I have a point to make before we continue.

I see that neither the Conservative nor the Bloc members are here today. Can we proceed without representatives from those two parties?

The Chair: From what I understand, yes, we can. We can proceed. We're not voting on anything. I'd like to hear what Mr. Ménard has to say.

We'll go to Mr. Bell, and then we'll go to Ms. Wasylycia-Leis.

Mr. Don Bell (North Vancouver, Lib.): Welcome to you.

I have a couple of issues. On your Canada Pension Plan report as at December 2003—which I guess is the current one, is it? We don't have the one for 2004. Is that because you only do it every three years?

Mr. Jean Claude Ménard: The process is that we do the report every three years. We have one year to complete the report and to send the report to the minister. In that case it was before December 31, 2004. So it was sent to the minister in November and tabled after that by the minister.

Mr. Don Bell: On page 66 you have some references to the participation, the active population. I was curious about the gap that I noticed between the male participation and the female has narrowed. It was almost 32% in 1976; it's 12% by 2003. I gather this gap should continue to narrow, should it?

Mr. Jean Claude Ménard: Yes, it will continue to narrow. It has narrowed by a big number in the past 30 years, and we think it will still continue to narrow, but I would say to a smaller extent than in the past.

Mr. Don Bell: That's just strictly the demographics. In terms of demographics, I guess I mean the participation in the workforce by females.

Mr. Jean Claude Ménard: Yes. When we do the projections for the labour participation rates for females in particular, we look at that on a cohort basis. It's clear the females aged between 25 and 34, for example, are now more present in the labour force than was the case, let's say, 20 or 30 years ago. It is with that kind of information that we are projecting an increase for the younger cohorts in the future. In that case, our projection for the labour participation rates for females is quite reasonable for the long term.

● (1205)

Mr. Don Bell: The other, related question I had is on table 61—that's on page 97—on the proportion of contributors married or in a common-law relationship at death. It's interesting, actuarially, that the number of males who are in some kind of a relationship at age 90 is 47% versus 5% for females, and at 80 it's 67% to 25%. I was just curious. The percentage isn't always higher; it varies at the early ages. Is there any comment you want to make on that other than to say those are just the facts?

Mr. Jean Claude Ménard: Yes, it's particularly for later ages, let's say past 70, because the females live longer. It happens that at age 90, for example, most of the females are survivors, because their former spouse has passed away. That's the main reason for the big difference.

Mr. Don Bell: And they just haven't gotten back into a relationship, where the males are still alive, so their spouses are still alive?

Mr. Jean Claude Ménard: Yes.

Mr. Don Bell: The other question I had was about the Canada student loans, which you do as well. Maybe I'm missing it, but I didn't particularly see a report on that. My curiosity on that is, is there any trend that's happening there? The whole issue of post-secondary education is important. I gather you don't get involved in commenting—or do you—on the failure or bankruptcy rates. Do you just deal with the participation, or do you break out the details beyond that?

Mr. Jean Claude Ménard: In 2000 we moved to a new regime. Before 2000 the loans were administered by the banks, and since 2000 they've been administered by the government and the money has come directly from the government. The office has been involved in this program since 2001, and the mandate is to project the portfolio of loans for the future. Right now we have a population of around 330,000 students who are eligible and who receive student loans. In recent years we have had a portfolio of loans issued of about $1.5 billion, and the total portfolio right now is about $10 billion.

I would say that when our office started the work, we didn't have a lot of information on the new program. Now it is five years later and we have a good sense of the number of students eligible and the future trends for this population.

Mr. Don Bell: Now, is the default rate around 30%?

Mr. Jean Claude Ménard: The default rate you referred to, the 30%, is probably the gross rate. Our provision for the public accounts is around 12%, the net default rate. The student is first in default, and after that there's a recovery of the loans. At the end of day, let's say, it could be 10% or 15%—

● (1210)

Mr. Don Bell: It might go from 30% to start off with down to 12%. They actually make arrangements to collect the other percentage, so the net default rate is around 12%.

Mr. Jean Claude Ménard: Yes.

Mr. Don Bell: And has that grown? From what you can see, is that increasing or decreasing or stable?

Mr. Jean Claude Ménard: It is increasing a bit. We mentioned in the previous report, the third report, that we didn't have enough information to see to what extent it would increase. We mentioned in the last report, the third report, that this provision could be revisited with more accurate or more recent numbers, and we are not sure. The fourth report is in preparation; it should be completed in the following month, and in that report it's possible we'll see the net default rate has increased, but we don't know exactly.

As I said, we have a lot of information for the past five years, basically the period when the loans were issued, and we don't have as much information on the experience with the default.

Mr. Don Bell: Do you have any sense of why that default rate is increasing?

Mr. Jean Claude Ménard: Not at all. Our role is mainly to look at the information, to look at the trends, and to reflect the trends in our evaluation.

Mr. Don Bell: And your most current report, then, will be ready in about a month, you were saying?

Mr. Jean Claude Ménard: Yes.

Mr. Don Bell: And the last report is available through the web?

Mr. Jean Claude Ménard: Yes, and in that case, unlike with other reports we do, it's not a statutory obligation. However, it's more frequent than on a triennial basis; it's on an annual basis. We produced one last year; we will produce another one in June.

Mr. Don Bell: And those kinds of studies are paid for by the federal government as the client for that information as opposed to the provincial governments. You basically provide them with information on CPP—or what are the provinces interested in?

Mr. Jean Claude Ménard: The provinces that are in the Canada student loan—

Mr. Don Bell: No, in the CPP.

Mr. Jean Claude Ménard: All the provinces are covered for CPP except Quebec, which has its own pension plan, the Quebec Pension Plan.

Mr. Don Bell: Thank you.

The Chair: Thank you, Mr. Bell. We'll come back.

I have Ms. Wasylycia-Leis, and then Ms. Minna.

Ms. Judy Wasylycia-Leis (Winnipeg North, NDP): Thank you, Mr. Chairperson, and thank you, Mr. Ménard, for your presence today.

I wish we had a fuller house, but circumstances are beyond our control to ensure that.

I did want to comment on your 21st actuarial report last December, which was very positive about the future of CPP, and then of course the independent actuarial review backed that up. For that reason alone I wish the Conservatives were here, who are always the naysayers on the ability of CPP to survive the present circumstances.

But let me just focus in on that for a moment. I see that on page 11 of the 21st report you say CPP will be able to withstand any unforeseen economic or demographic fluctuations. That's good news. I'm just wondering if you can elaborate a bit on that as to how you arrived at that conclusion.

Mr. Jean Claude Ménard: As you know, the legislated contribution rate is fixed at 9.9%; that has been the case since 2001, and it is projected to be the same rate forever. Our responsibility is to calculate what we call the steady state contribution rate, that is, the minimal rate that is sufficient to sustain the current plan provisions without further increases. In our report we say the steady state now stands at 9.8%, so there is a question as to whether it should be 9.8%, which we consider the minimal rate, or the 9.9%. This is basically why, given that kind of result, we think the plan is able to meet its obligations even if there are unexpected economic or demographic fluctuations.

The other thing I want to mention is that because we have moved into a situation where CPP is now and will be a partially funded plan, it means the assets are generating and will generate investment earnings in the future to help the contributors and at the same time pay the benefits for the beneficiaries. Because there's a large pool of assets, I think we are in a very good position to sustain the plan through any unforeseen events.

● (1215)

Ms. Judy Wasylycia-Leis: What does it mean when you say that over the projection period, which I believe is 75 years, there will be more cash inflows than outflows?

Mr. Jean Claude Ménard: If we go back in history, I would say to 1992, we see we were in a situation where there were more benefits paid than contributions received. This situation continued until 2000 or around then. Since 2000 we have been in a situation where contributions year after year are higher than benefits paid. That means excess cashflows. According to this report, we expect this situation will continue until 2022, which means there's a 17-year period when you have positive cashflows that could be invested through the CPP Investment Board and contribute towards increasing the assets of the plan.

The idea of the amendments put in place in 1998 was to bring the assets to a level equal to, let's say, five times the benefits paid or 25% of the liabilities at the time most baby boomers will be going into retirement. There was a need to build a reserve or higher assets to take care of the retirement needs of the baby boomers.

Ms. Judy Wasylycia-Leis: Thank you for that, and thank you for helping us, giving us the tools by which we can restore some confidence of Canadians in our CPP system. You can't open a newspaper today without seeing some article suggesting we're on the verge of collapse and on the verge of losing everything.

Mr. Jean Claude Ménard: I think it's going in the right direction in the sense that for the last two years, for example, the CPP Investment Board has got good investment results, and we are continuing in the direction we were expected to go in 1998.

Ms. Judy Wasylycia-Leis: I have three more questions that are more on structure and organization within government. I just wonder, as the chief CPP actuary for the country, do you see yourself as responsible to the finance department and the government or to Parliament?

Mr. Jean Claude Ménard: I would say I am responsible to Canadians first, in the sense that, as I said before, I am fully independent in the opinions provided in the actual report, and—how can I say this—we had discussions with clients, with different government departments, meaning it could have been Social Development or the Department of Finance....

Let me go back a bit to the way we produce an actual report. The first thing is we have to set the assumptions. So first of all we look at all the information we have on hand. After that, we organize the seminars to get information, to get advice, from other experts on demographic and economic trends. We organize interdisciplinary seminars, and in these seminars we invite mainly demographers, economists, investment analysts, but not necessarily actuaries because we have, I would say, a lot in our shop, so we need the advice of other experts.

Once that is done, we set our assumptions. After that, we discuss these assumptions with some specific departments, with the people who we think are also experts in that domain. For example, on demographic assumptions, we have to set assumptions on fertility, on migration, on mortality, and we think the experts are within Statistics Canada, so we exchange ideas and we disclose the assumptions we had in mind at that time. In some cases they are in agreement with us. In other cases they are in disagreement with us, but at the end of the day it is my decision to set the assumptions. That's for the demographic side.

For the economic side, there's a group at the Department of Finance that is responsible for the projection of labour participation rates. So we have our own set of assumptions. We compare our set of assumptions with their assumptions and we discuss. In some cases we agree. In other cases we disagree. For example, going back to the question of Mr. Bell, we think in 2030 there will be more women participating in the workforce than this group believes. So there could have been differences during the discussion.

Finally, we also have discussions with the investment manager of the CPP Investment Board and we discuss with them the investment assumptions. Once this is all completed, we produce an actual report and we send the report to the Minister of Finance. Again, when it's done, it's not only, I would say, my word or the word of my office. This is why it is so important that we decided to go to peer reviews to have other actuaries look at our report and give their views. Of course, peer reviews are extremely important for us. They help to improve the processes, to improve the setting of assumptions, the methodology, and all these things.

So going back to your question, I think our role, our statutory obligation, is to give the best information we have on the current financial status of the plan and the projected financial status of the plan, and as such this report is tabled before Parliament.

● (1220)

Ms. Judy Wasylycia-Leis: You have a role, clearly, to provide technical advice to the government in terms of CPP expenditures. Do you see it as part of your role, or do you think it would be useful to add to your role the question of assessment of the income needs of Canadians?

Mr. Jean Claude Ménard: I would be pleased to accept any mandate the government gave us in that sense.

For example, we are responsible for the old age security and the guaranteed income supplement. The guaranteed income supplement is paid to the older people with the lowest income. We have a good assessment of the current income of these people, and we make projections for old age security and the guaranteed income supplement.

Regarding the retirement needs of Canadians, I think in Canada we have one of the best systems in the world, for three reasons.

The first one is that we have been very successful in fighting poverty amongst seniors—and I would say, more than that, at a reasonable cost for Canadians. There are many countries that are looking at our system to see how we were able to reduce poverty amongst seniors and at the same time do it at a reasonable cost. That's the first thing.

The second reason we have a good system is because we have a fair mix of public and private pension plans. For example, if you are a worker with earnings of $10,000 to $20,000 a year for your entire career, you will basically get your retirement income from public pension plans, from CPP or QPP, old age security, and GIS. If on the contrary you have earnings around the average—I would say around the yearly maximum pensionable earnings of $40,000 a year—you will get a replacement rate of 40% of your previous income from public pension plans. Of course, this is not enough, so you need private means. You need either an RRSP or an employer pension plan. Of course, at the end of the spectrum, if you have earnings, let's say, twice the average earnings, you definitely need private sources.

This is why I say there's a very good balance between public and private pension plans.

● (1225)

Ms. Judy Wasylycia-Leis: My last question, for now at least, is rather hypothetical. We've been debating at this committee the idea of establishing an independent parliamentary office for fiscal forecasting. I'm just wondering what you think of the idea of an office that would do that forecasting but would also include a long-range actuarial component, including your office.

Mr. Jean Claude Ménard: I don't have any particular opinion on the creation of an independent office. I would say my main purpose or main objective is to make sure—

[*Translation*]

The Chair: Mr. Ménard, you are not obligated to answer.

[*English*]

You can just give your opinion if you'd like, but you're not obligated to answer.

Mr. Jean Claude Ménard: Okay.

As long as the independence of the chief actuary is not at stake, the office of the chief actuary could reside in the current organization or in another reporting structure. I don't have any particular opinion on this.

The Chair: Thank you, Ms. Wasylycia-Leis.

Ms. Minna.

Hon. Maria Minna (Beaches—East York, Lib.): Thank you, Mr. Chairman.

First of all, I'm glad to hear your reinforcement as to the soundness of the plan. As my colleagues just said, there's a constant discussion out there as to whether it is in fact sound.

A lot of young people were convinced some years ago, before we did the restructuring, that they were not going to inherit anything; there was to be no pension. Some of them still think that way. Maybe communication is something that....

That's one question, actually. Do you do any communication out to the community at large to help people understand not only how it works but also the soundness of the plan and how that is steady for them? There is still a lot of misunderstanding as to how it works and to what extent they will have it when they retire.

Mr. Jean Claude Ménard: I agree. For any Canadian their retirement sources will be various...I would say there will be money coming from old age security, from CPP or QPP, from the employer pension plan, and from their own private sources. There's not only one basket or only one source of income, so it makes it, I would say, something more challenging in terms of communications. I personally think we should try to repeat, explain, and be more clear in the messages.

For example, there's the peer review panel. There was one question asked of them: does the actuarial report fairly communicate the results to Canadians and to members of Parliament? In my view, it is of extreme importance to make sure the report is clear and Canadians understand the financial status, for example, of the CPP but of the other pension plans as well, like old age security. They said in their review report that our report communicates the results well.

Hon. Maria Minna: Thank you.

I wanted to ask you at this point, how does the soundness of the Canada Pension Plan compare with that of other pension schemes in other countries? Favourably or less so? Do we do comparisons in terms of stability and so on? To what extent does the Canada Pension Plan also have a positive impact on competitiveness and productivity in the labour market?

● (1230)

Mr. Jean Claude Ménard: The CPP is in very good shape, that's for sure, but we have to remind ourselves that the CPP is a basic retirement pension plan. Depending on your level of income before retirement...you won't be rich with the CPP. It's a reasonable plan that provides—which is extremely important—all Canadians with a basic amount. In terms of competitiveness, I would say the project cost is very reasonable compared to that of other countries.

I missed your first question.

Hon. Maria Minna: My question was on whether the pension compared favourably with similar pensions in other countries. How does it compare?

Mr. Jean Claude Ménard: Every time we do that kind of comparison, the first aspect we look at is the aging of the population. If we compare ourselves with continental Europe, for example, we find Canada will age the same as the others, of course, but we expect Canada will still be much younger than many countries in continental Europe.

On the other spectrum, there are a couple of countries—and I would say the United States, for example—where we expect it will be the youngest country among the industrialized countries in 2050. The main reason for that with this country is their fertility rate, which now stands at 2.1, compared to Canada's at 1.5.

The reason for Canada's not aging at the same pace as European countries is that we continue to have a good flow of immigrants, who rejuvenate the country. We are a country with one of the highest percentages of immigrants in the population. If I look at the aging component, I see we are in a good position, so I would say the sustainability of our retirement income will face less pressure than in other countries.

Hon. Maria Minna: So immigration is a positive in this context. It's keeping us younger in the long term.

Mr. Jean Claude Ménard: Yes.

Hon. Maria Minna: I'm surprised about the Americans. I thought their birth rate would be about the same as ours.

Mr. Jean Claude Ménard: Right now, no. This difference started, I would say.... We were at about the same place 15 years ago in 1990, but since the last 10 years, the gap between the U.S. and Canada is different. I remember back 15 or 20 years ago when we looked at how to set the prediction of the fertility rate and we looked at the U.S. history and we said, okay, well, they are at that place, so we should be at the same place in the long term. In the past 10 years, it's not the case, and this is why we have an assumption. They have an assumption in their actuarial reports of 2 or 2.1 for the fertility rate and our assumption is 1.6. So it's a bit lower than their assumption.

Hon. Maria Minna: Do we know what it is in the demographic changes that are causing the difference between the two? Is it a higher immigration rate or just a change in attitude?

Mr. Jean Claude Ménard: I'm not an expert in the drivers of the fertility rate. However, we look at the fertility rates by age group. The fertility rate of the 15- to 19-year-old women—I have a daughter of 17 and still I don't consider her as a woman, more as a girl—in the U.S. is three times our fertility rate for the same age group for the 15- to 19-year-old group. The 20- to 24-year-old age group is about twice, so they have a fertility rate that is about twice our level. So you have in these two groups the main numerical explanation between the two countries.

● (1235)

Hon. Maria Minna: Thank you very much.

The Chair: Thank you, Ms. Minna.

Mr. McKay.

Hon. John McKay (Scarborough—Guildwood, Lib.): Thank you.

That was a fascinating answer to Ms. Minna's question. I thought it was quite a parallel situation to the United States. What I don't understand is, how do you square that with the notion in the public realm that the American public pension system is in real trouble?

Mr. Jean Claude Ménard: In 1998 the government introduced, I would say, big amendments to the CPP. They decided, following extensive consultations with Canadians, to increase the contribution rate. They reduced the growth of future benefits and they created the Canada Pension Plan Investment Board. When you look at these kinds of amendments and you go back to 1983 for the United States, they basically did the same thing at that time. They increased contributions; they reduced the future growth of benefits by pushing the retirement age to 66 or 67—67 will be in 2025 in their case—and they were in the situation of having excess cashflows. They are still in a situation of excess cashflows. The main difference between them and us is that they continue to keep that amount—the excess cashflow—in the government books. They don't create an organization like the CPP Investment Board that invested in the markets.

If you look at contributions and benefits in the U.S. right now, compared to the CPP, they are in a similar situation, and indeed they are supposed to be in positive cashflows until 2018, which is close to us—2022 for us. Having said that, it's in T-bills or government bonds, so they claim that at that time they will face negative cashflows, and at some point in 2041-42 or something like that the trust fund will vanish. This is one of the reasons why President Bush has introduced the idea of individual accounts.

Hon. John McKay: I knew the Americans mixed their pension revenues right into the general revenues. In fact their statement of deficit in this current fiscal year would be much worse if the positive cashflow of pension revenues were eliminated from the statement. Effectively what that does is it forces the pensioners to buy U.S. Treasury bonds at very low rates. Is that a fair statement?

Mr. Jean Claude Ménard: I agree with the first part of your statement, that the current social security surpluses are embedded in the overall budget of the country. I'm not so sure about who is buying these bills.

The only thing I want to say here is that in Canada we created a lock box. Now I would say it's clear as to what is going in—the contributions and investment earnings—and what is going out, which are the benefits. It's also clear that the financial review of the plan is done every three years by the provinces and the federal government. That's the main difference between what we have achieved compared to the United States.

● (1240)

Hon. John McKay: As you know, one of the drivers for the change in the foreign content rule was the situation with the Canada Pension Plan, which had basically run out of pension-grade investments in this country. I'm assuming you have an opinion with respect to the quality of the investments of the Canada Pension Plan. If that foreign investment rule is removed, will there be any change, in your view, with respect to the appropriate investments of the Canada Pension Plan?

Mr. Jean Claude Ménard: This is an excellent question. This brings me to our assumptions on the asset mix of the Canada Pension Plan. For the period where there will be positive cashflows—so until 2020—we set the asset mix at 65% equities and 35% bonds. With equities, there is 65% variable income. In that category the assumption is 10% in real estate infrastructure, 30% in foreign equities, and 25% in Canadian equities.

So it's a portfolio in which the content is more towards variable income securities than fixed income securities. However we think that as the population gets older and as we move from a situation of positive cashflows to negative cashflows, it means that benefits will be higher than contributions received after 2022. We feel the portfolio should be less aggressive at 55% variable income and 45% fixed income.

In all the projection periods for the 75 years, our assumption on the foreign content was 30%. I'm not an expert in investments, but I know that diversification is extremely important. So if someone is saying the rule could impede diversification, it is probably a good move to go in that direction and to permit the CPP Investment Board to have more diversified assets. But for now, of course, the removal of this rule could lead us to review that assumption in the next actuarial report.

Hon. John McKay: You're comfortable with the change in the rule, providing that at some point the asset mix goes from 60%-40% down to 55%-45%.

Mr. Jean Claude Ménard: Yes.

Hon. John McKay: Interesting.

I have one final small question. You're asking for an appropriation of $755,000 from Parliament. I notice in your speech you're mostly cost recovery, and the question I have is, why is it you're not 100% cost recovery?

Mr. Jean Claude Ménard: Well, I would say history. When I arrived in my current position, I would say we received three times the current amount from appropriations at that time. We took some steps to move all the budget to a cost-recovery basis. The remaining appropriations are related mainly to the actuarial services for the pension plan of the judges and the members of Parliament, and also to some work on the life and disability insurance plans.

Of course, we entered into many MOUs, memoranda of understanding, with our clients, and it is our objective to try in the following years to move completely to a cost-recovery basis.

Hon. John McKay: Am I out of time?

The Chair: Yes.

Mr. Hubbard.

● (1245)

Mr. Charles Hubbard: Thank you, Mr. Chair.

I have just a couple of quick points. Mr. McKay did get into this business about investments. We've had quite a bit of volatility in the last few years in the markets.

Is there, in your opinion, vulnerability in terms of the future of the Canada Pension Plan on the basis of the investments the board is making? Is this a concern? Should we be watching?

Mr. Jean Claude Ménard: For the first time in this report we introduced a section on the volatility of the financial markets. We showed some scenarios on what could happen if there are two consecutive years with either positive—

The Chair: Mr. Ménard, it would be helpful for us to know what page that's on so we can follow.

Mr. Jean Claude Ménard: Sorry, Mr. Chairman. I'm referring to pages 44 and 45, financial markets volatility, in the main report.

Let's look at table 20. What we provided this time is to replicate what could be the impact on the financial status of the plan if in 2017 and 2018...and you could ask me why these years. We want to look at the impact, once we're at our target, on the assets when benefits paid will be close to the highest. And we provide some information as to what could be the change in assets if we have two years of minus 10% or two years of plus 15%. So you can see there's a volatility on the assets invested.

I would like to go to page 113. That is what could be the impact on the contribution rate. On table 72, between the two lines, we have the steady-state contribution rate that I referred to previously—9.8%—and our nominal equity returns assumption is plus 7.5%. So if we have two positive years of, let's say, plus 20%, the impact on the calculation of the contribution rate will be a reduction of the rate to 9.6%. On the other hand, if we have two consecutive years of minus 10% or even minus 15%, the contribution rate could be as high as 10.1%. However, it is important to look at the other column, that is, the probability of this happening. These probabilities were calculated with the past history of this last 65, last 75...in that case, last 65 years. To have two consecutive years of minus 15%, the probability is only 2%.

Of course, there are impacts in investing in the financial markets, and I would like to go back to the two extremes of how you could finance a pension plan. You could either go on a pay-as-you-go basis, like the old age security.... In that case, the demographic risk is the highest. What I mean by demographic risks are fertility rate, migration, to some extent, and mortality rate, if people are living longer, for example. The other spectrum is the fully funded plan. If you have a fully funded plan, it means the assets equal basically the liabilities, the promise for future benefits. In that case the highest risk is the investment risk. And for CPP the target is to have the assets equal 25% in the liability. So in my view it's a good mix of all the risks together, either demographic risk or investment risk.

Nevertheless, we decided this time for the first time to introduce these tables to show what could be the impact of extreme results on the financial status of the plan.

● (1250)

Mr. Charles Hubbard: Thank you.

I have one other small question, and maybe it's a little bit irrelevant here today, but I would hope somebody with your expertise in the area of pensions.... We have a conflict—I shouldn't say a conflict, but we have a major problem today between a group of correctional officers with our corrections institutes across Canada and with Treasury Board in terms of a new demand on pensions. That demand would mean that after 25 years of service they could retire with full pension benefits.

I asked the question in the House on that last week. I wonder, have they come to you to do an actuarial plan in terms of that problem between the union and Treasury Board? Would your organization look at that and give recommendations on whether or not there really are problems?

Mr. Jean Claude Ménard: That's a very good question, and a very good example, by the way.

Every time there are these kinds of proposals, we are asked to evaluate the cost of any proposal. It's true for the Correctional Service, and it's also true for all other categories of public servants who are covered through the public service pension plan. We have done some evaluation on the financial impact.

Mr. Charles Hubbard: Would a brief report on an evaluation be available, or is it subject to...?

Mr. Jean Claude Ménard: I would have to ask my client first.

Mr. Charles Hubbard: And your client would have been the union or it would have been the Correctional Service of Canada?

Mr. Jean Claude Ménard: I've provided the cost estimate to Treasury Board Secretariat.

Mr. Charles Hubbard: They've been three years, Mr. Chair, without a contract. This apparently is one of the main impediments. I guess we're hearing both sides.

Thank you, anyhow.

Mr. Jean Claude Ménard: You're welcome.

The Chair: Thank you, Mr. Hubbard.

I have a couple of quick questions.

Just quickly, Monsieur Ménard, who reviews the chief actuary? What is the relationship, again, in the Office of the Superintendent? In terms of your assumptions, I think we're pretty clear on the process. But in terms of the bureau administratively, is the Office of the Superintendent in charge? Just quickly, could you go over that again? How is the relationship?

Mr. Jean Claude Ménard: My direct boss is Nicholas Le Pan, the superintendent. On reviewing my work, it's basically done through the peer review process. For the CPP, there's an independent panel that was hired. I would say it's now the third time. For the public sector, the actual reports on the public sector pension plan, our work has been reviewed by the Auditor General, who hired actuarial consulting firms to do the review. This is basically how my work is reviewed.

The Chair: So the administration part falls under the Office of the Superintendent, which is then audited by the Auditor General?

Mr. Jean Claude Ménard: Yes.

The Chair: Okay. What is your relationship with the QPP? How is that tied in? Is there any relationship there, in terms of—

Mr. Jean Claude Ménard: Yes, indeed, I would say a very good relationship. As you know, the CPP and QPP—Quebec Pension Plan—are very similar plans. They provide the same retirement benefits and the same contributions—they are indexed in the same way—and they have the same obligation to do actuarial reports every three years. From time to time, I discuss with them mainly the assumptions and the results that are in both reports, CPP and QPP.

The Chair: Is it the same three-year period?

Mr. Jean Claude Ménard: Yes, it is the same three-year period.

The Chair: So will their report be very similar to yours in terms of the assumptions?

Mr. Jean Claude Ménard: There could be differences in assumptions, but they have to do the same assumptions. I would say fertility rate, mortality...sorry?

The Chair: They could be different, but you must know if the results are different. They must have published and you must have compared each other's notes.

Mr. Jean Claude Ménard: Yes, indeed.

One of the biggest differences is in the investment assumptions. Our real rate of return on investments, on a long-term basis, in our report is 4.1%. They use 4.6%. So it's a bit higher than us.

In that case, you people—external experts—could say maybe one is either too aggressive or the other too prudent.

Another piece of information on that aspect is that the peer review panel looks at our report. They were in agreement with all the assumptions. They consider these assumptions reasonable. However, there were a couple of assumptions where they said, “Well, our own best assumptions would have been X”. For example, in the real rate of return on investments, they would have chosen 4.6%.

● (1255)

The Chair: Okay. On the relationship between yourself and the CPP board, is there any influence at all in terms of what investments should be made with the money?

Mr. Jean Claude Ménard: No, I'm not involved in the investments.

The Chair: What is the relationship? Is there any contact at all in terms of—

Mr. Jean Claude Ménard: There are a lot of contacts. Contacts are related to the setting of assumptions. We met with them last year to discuss the assumptions in this report and to discuss with them if our assumptions make sense.

The Chair: But you won't meet with them again for another three years.

Mr. Jean Claude Ménard: Indeed, we have a meeting next week with them to discuss the findings of the current peer review panel and to continue to work together, mainly to make sure we assess correctly the risk of investments versus the potential impact on the contribution rate.

The Chair: Okay. There's no real influence in terms of what should be invested and what should not be invested.

Mr. Jean Claude Ménard: Oh, no. I'm not an expert in that case.

The Chair: I have one final question. The final table is what I look at, appendix F on page 127, where in the year 2078 you're projecting that we'll have $4.3 billion in assets and our yearly expenditures will be $770 million a year. I'm just using the last table.

Mr. Jean Claude Ménard: Table 82?

The Chair: Yes, appendix F, table 82.

Mr. Jean Claude Ménard: Yes. Those are the results under the 9.8% steady-state contribution rate. Under the legislated contribution rate, you have to look at table 11 on page 32. So if the act remains the same, the contribution rate is 9.9%.

The Chair: Okay. Let's use table 11. If we look at table 11 and use the last line, in 2075, in an ideal world, we would have $14.8 billion in the CPP in terms of assets.

Mr. Jean Claude Ménard: Are you talking about the economic assets?

The Chair: Yes, I'm talking about the assets. My expenditures on a yearly basis, and again for the year 2075, would be $678 million. So that would be what? Even if we divide by seven, it would be six or seven times.

Mr. Jean Claude Ménard: Yes.

The Chair: At what point is enough, enough? A couple of years ago, or if we look at 2004, where the contributions were $28 million to $29 million, versus $76 million to $77 million, it's about three times. What do we look at? When do we say enough is enough? When do we stop contributing? When do we increase the contributions? What are we looking at in terms of...?

Mr. Jean Claude Ménard: I would say the target is roughly to get the assets equal to five times the expenditures. This is the kind of result we will get with the steady-state contribution rate of 9.8%.

There is maybe something we should be careful of. I have high confidence in the projections for the next 15 years, 20 years, 25 years. It's more hazardous to go to, let's say, the period 2050 to 2075. There are a lot of unknowns at that point.

I would say because the 9.9% is 0.1% higher than the 9.8% minimal rate, over time it continues to increase. As a rule of thumb, if a person wants the CPP on a fully funded status, the target is to get the assets to expenditure ratio to 20%.

● (1300)

The Chair: I guess that's my question, because it seemed like a couple of years ago we were panicking. All of a sudden we increase the rates, and now people seem to be panicking less. I wonder if we're justified in doing that.

Mr. Jean Claude Ménard: We are in a much better situation right now than six or seven years ago.

The Chair: Okay.

Hon. John McKay: Mr. Chair, I have a question.

If your goal is to have assets equal to five times what your expenditures are.... At 2075 your expenditures are $678 million. Is that right?

Mr. Jean Claude Ménard: Yes.

Hon. John McKay: Your assets are $4.8 billion.

Mr. Jean Claude Ménard: Yes.

Hon. John McKay: That's quite a bit more than five times.

Mr. Jean Claude Ménard: In 2075, yes.

The Chair: I just used 2075 because that's the last line, but as Mr. Ménard was saying, you probably have to look at it after a 20- or 25-year period.

Hon. John McKay: So in theory, then, you could decrease the contribution.

Mr. Jean Claude Ménard: Indeed, the ministers of Finance are looking at the plan every three years. So they will have, I would say, some occasions during that period to revisit the financing of the plan—the contributions, benefits, or anything else.

Hon. John McKay: Thank you.

The Chair: Mr. Ménard, thank you. It was an interesting session.

Mr. Jean Claude Ménard: Thank you very much.

The Chair: Sorry about being late, but this is the type of environment we live in. I'm not going to apologize for the rest of my colleagues, but I'm sorry about the situation.

The meeting is adjourned.

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