

# Canada Pension Plan

**ANNUAL REPORT OF THE**  
Canada Pension Plan ○  
2003-2004



Government  
of Canada

Gouvernement  
du Canada

Canada 

# ANNUAL REPORT OF THE CANADA PENSION PLAN

**Fiscal Year 2003-2004**

ISPB 202-06-06E

Publication of the *2003-2004 Annual Report of the Canada Pension Plan* was delayed due to a number of organizational and governmental changes.

As of February 2006, the legal names of the minister and department responsible for the Canada Pension Plan (CPP) are the Minister of Human Resources and Skills Development and the Department of Human Resources and Skills Development respectively. Operationally, the department is known as Human Resources and Social Development Canada (HRSDC).

The names of the departments previously responsible for the CPP, namely Human Resources Development Canada (HRDC) and/or Social Development Canada (SDC), are used in this report in a historical context only.

Produced by the Department of Human Resources and Skills Development, in collaboration with: the Department of Finance, the Canada Revenue Agency, Public Works and Government Services Canada, and the Office of the Superintendent of Financial Institutions.

If you need additional copies of this report, it is available for printing at [www.hrsdc.gc.ca](http://www.hrsdc.gc.ca).

Or you may contact:

**HRSDC  
Publications  
Ottawa ON  
K1A 0L1  
Fax: (613) 948-9450**

Aussi disponible en français sous le titre  
*Rapport annuel du Régime de pensions du  
Canada 2003-2004*.

To give feedback on the Annual Report, see our form online at [www.hrsdc.gc.ca](http://www.hrsdc.gc.ca) under "Publications".

For more detailed information about subjects covered in this report, or about the Canada Pension Plan in general, please visit [www.hrsdc.gc.ca](http://www.hrsdc.gc.ca).

If you have questions, please call  
(free of charge from Canada and the U.S.):

**1 800 277-9914 (English)  
1 800 277-9915 (French)  
1 800 255-4786 (TTY)**



Her Excellency  
The Governor General of Canada

May it please Your Excellency:

We have the pleasure of submitting the *Annual Report of the Canada Pension Plan* for the fiscal year 2003-2004.

Respectfully,

---

James M. Flaherty  
Minister of Finance

---

Diane Finley  
Minister of  
Human Resources and Skills Development

# Contents

<b>2003-2004: THE YEAR AT A GLANCE</b> .....	1
<b>THE CANADA PENSION PLAN IN BRIEF</b> .....	2
<b>ENSURING FINANCIAL SUSTAINABILITY</b> .....	3
Actuarial Reporting .....	3
A Fair Approach to Funding .....	4
<b>2004 BUDGET CHANGES TO THE CPP</b> .....	6
<b>FINANCIAL ACCOUNTABILITY</b> .....	7
CPP Account .....	7
CPP Investment Board .....	7
<b>BENEFITS AND EXPENDITURES</b> .....	9
Retirement Pensions .....	9
Disability Benefits .....	10
Survivor Benefits .....	11
Death Benefits .....	11
Other Provisions .....	11
<b>IMPROVED SERVICE DELIVERY</b> .....	12
Reaching Out to Canadians .....	12
Delivering Service .....	12
Processing Benefits .....	12
<b>MANAGING THE CPP</b> .....	14
Collecting and Recording Contributions .....	14
Overpayment of Benefits .....	14
Changes Announced in the 2004 Budget .....	14
Administrative Costs .....	15
The Appeals Process .....	15
<b>LOOKING TO THE FUTURE</b> .....	17
CPP Online .....	17
Online Services .....	17
Simplifying the Application Process .....	18
Reaching All Canadians .....	19
<b>CANADA PENSION PLAN FINANCIAL STATEMENTS</b> .....	21

This report on the Canada Pension Plan (CPP) consolidates input from all departments involved in the administration of the Plan: Social Development Canada (now Human Resources and Skills Development Canada), the Department of Finance, the Canada Revenue Agency (CRA), Public Works and Government Services Canada (PWGSC), and the Office of the Superintendent of Financial Institutions (OSFI).



## 2003-2004: The Year at a Glance

### IN FISCAL 2003-2004:

- Following extensive consultations with the provinces, the Government of Canada proposed changes to both the disability benefit and the rules governing employer contributions in the 2004 Budget. The changes were included in the budget implementation bill, which was tabled in Parliament on March 23, 2004. [It received Royal Assent in May 2004. The CPP changes will come into force with the formal consent of two thirds of the provinces through an Order-in-Council process.]
- 3.8 million Canadians received benefits from the Canada Pension Plan, with a total value of approximately \$22.6 billion.
- About 3.0 million people received \$15.9 billion in CPP retirement pensions.
- About 928,000 surviving spouses or common-law partners and 86,000 children of deceased contributors received over \$3.4 billion in CPP benefits.
- About 288,000 people with disabilities and 90,000 of their children received almost \$3.1 billion in CPP disability benefits.
- 11.4 million people contributed to the CPP.
- 2.2 million people received Statements of Contributions.
- Changes to the *Canada Pension Plan Regulations* were implemented on January 1, 2004, to reflect the statutory increase in maximum pensionable earnings (\$40,500 for 2004). The contribution rate remained unchanged at 9.9 percent.
- Administrative costs amounted to approximately \$410 million, or 1.72 percent of the \$22.6 billion in benefits paid. This compares favourably with administrative costs for other large pension plans and individual RRSPs.
- On March 31, 2004, total CPP assets were valued at approximately \$72.5 billion and equalled about three years of benefits. The majority of the assets were held in provincial, territorial and federal government bonds, deposits with the Receiver General for Canada, domestic and foreign publicly traded equities, and private equity, real estate and infrastructure assets. Bonds, equities and real estate and infrastructure are stated at fair value.

## The Canada Pension Plan in Brief

Almost everyone who participates in the paid labour force in Canada contributes to the Canada Pension Plan (CPP) or to its sister plan, the Quebec Pension Plan (QPP), and will at some time benefit from their provisions.

Established by an act of Parliament in 1965 and implemented in 1966, the CPP is a jointly managed federal-provincial plan. Quebec manages and administers its own Plan, the QPP, and participates in the decision making of the CPP. Benefits from either Plan are based on pension credits accumulated under both. The Plans are financed through mandatory contributions from employees, employers and self-employed people, as well as from investment income. (Information on the QPP is available from the Régie des rentes du Québec at [www.rrq.gouv.qc.ca](http://www.rrq.gouv.qc.ca).)

While it is perhaps best known for its retirement pensions, the CPP also provides children's, survivor, disability and death benefits. The CPP administers the largest long-term disability insurance plan in Canada. Vocational rehabilitation services offered under the Plan help some disability beneficiaries regain their independence by helping them to return to the labour force, following a customized return-to-work plan.

Benefit calculations are based on how much and for how long a contributor has paid into the CPP, and in some cases, the age of the beneficiary. Benefits are not paid automatically—everyone must apply and provide proof of eligibility. Benefits are adjusted in January of each year as needed to reflect increases in the average cost of living, as measured by the Consumer Price Index.

Many Canadians live and work in other countries. Others move here after contributing to a public pension plan elsewhere. To help protect their pensions, Canada has entered into social security agreements with other nations. These agreements enable Canadians to receive public pensions from other countries and may help them receive Canadian benefits abroad. They also permit continuity of social security coverage when Canadians are temporarily working outside the country, eliminate duplicate contribution payments, and help them meet eligibility requirements for some CPP benefits and for other countries' public pensions.



## Ensuring Financial Sustainability

As joint stewards of the CPP, the federal and provincial ministers of Finance review the Plan's financial state every three years and make recommendations as to whether benefits and/or contribution rates should be changed. They base their recommendations on a number of factors, including the results of an examination of the Plan by the Chief Actuary. The Chief Actuary is required under the legislation to produce an actuarial report on the CPP every three years (in the year before the legislated ministerial review of the Plan). The CPP legislation also requires the Chief Actuary to prepare an actuarial report any time a Bill is introduced in Parliament that, in the view of the Chief Actuary, has a material impact on the estimates in the most recent triennial actuarial report. This reporting ensures that the long-term financial implications of proposed Plan changes are given due consideration.

Changes to the CPP legislation governing the general level of benefits, the rate of contributions or the investment policy framework can be made only through an act of Parliament. All such changes require the agreement of at least two thirds of the participating provinces, representing at least two thirds of the population. The changes come into force only after two years' notice, unless all the provinces waive this requirement, and after Provincial Orders-in-Council confirming the changes have been passed. Quebec participates in decision-making regarding changes to the CPP legislation, even though it administers its own plan. It is important that Quebec be involved in changes to the CPP to ensure the portability of QPP and CPP benefits across Canada.

The legislation requires that federal and provincial ministers make best efforts to complete the next financial review of the Canada Pension Plan by the end of 2005. Ministers will base their review on a number of factors, including the conclusions of the *Twenty-first Actuarial Report* on the Canada Pension Plan, prepared by the Chief Actuary of the Canada

Pension Plan for the purpose of the review. The previous triennial financial review of the Plan by ministers was in 2002. In the 2002 review, ministers concluded that the Plan was financially sustainable and agreed to make no changes to the Plan. Further information on this and previous reviews of the Plan can be found at [www.cpp-rpc.gc.ca](http://www.cpp-rpc.gc.ca).

### ACTUARIAL REPORTING

The *Twenty-first Actuarial Report* was tabled in Parliament by the Minister of Finance in December 2004. The report presented the financial status of the Plan as at December 31, 2003, and provided information to evaluate the Plan's financial sustainability over a long period, assuming Plan provisions remain unchanged. The findings of the report are an important element in the federal and provincial finance ministers' triennial financial review of the CPP slated for 2005. The last triennial financial review of the Plan by ministers was based on the findings of the *Eighteenth Actuarial Report* (as at December 31, 2000). Since this report, the Canada Pension Plan was subject to a series of amendments, the financial implications were outlined in the *Nineteenth* and *Twentieth Actuarial Reports*.

Canadians can have confidence in the results of the *Twenty-first Actuarial Report* and the conclusions reached by the Chief Actuary about the long-term financial health of the Plan. A panel of independent Canadian actuaries, selected through an arm's-length process, will review the report.

Federal and provincial finance ministers have endorsed regular peer reviews of triennial actuarial reports. The Office of the Chief Actuary has meticulously followed this recommendation. Panel reports and recommendations, as well as actuarial reports, can be found at [www.osfi.gc.ca](http://www.osfi.gc.ca).



## A FAIR APPROACH TO FUNDING

When it was introduced in 1966, the CPP was designed as a pay-as-you-go plan, with a small reserve. This meant that the benefits for one generation would be paid largely from the contributions of later generations. This approach made sense under the economic, financial and demographic circumstances of the time. The period was characterized by a rapid growth in wages and labour-force participation, and low rates of return on investments.

The pay-as-you-go approach also allowed the federal and provincial governments to keep contributions at a reasonable level while beginning to pay full retirement benefits as early as the mid-1970s. This was important—many of the seniors who received benefits at that time had been unable to accumulate sufficient retirement savings.

However, demographic and economic developments and changes to benefits in the 30 years that followed resulted in significantly higher costs. When federal and provincial finance ministers began their five-year statutory review of the CPP finances in 1996, contribution rates, already legislated to rise to 10.1 percent by 2016, were expected to have to rise again—to 14.2 percent by 2030—to continue to finance the Plan on a pay-as-you-go basis.

Continuing to finance the Plan on a pay-as-you-go basis would have meant imposing a heavy financial burden on Canadians in the workforce 25 years down the road, which was deemed unacceptable by the federal and provincial governments. Therefore, in 1997, they agreed instead to change the funding approach of the Plan to a hybrid of pay-as-you-go and full funding. Under full funding, each generation pays for its own benefits.

## Steady-state financing

To reduce the burden on future generations, the federal and provincial governments introduced “steady-state” financing as part of the 1997 reform agreement. This approach requires that contribution rates be set no lower than the lowest rate expected to ensure the long-term financial stability of the Plan without recourse to further rate increases. At the time of the reforms, this was determined to be 9.9 percent. Therefore, under steady-state financing, the contribution rate was scheduled to increase incrementally (from 5.6 percent in 1996) to 9.9 percent in 2003, and to remain at this level thereafter.

According to the Chief Actuary of Canada, steady-state financing will generate a level of contributions that exceeds the benefits paid until 2021. Funds not immediately required to pay benefits will be transferred to the CPP Investment Board for investment.







Plan assets will accumulate rapidly over this period and over time will help pay the growing costs that are expected as more and more “baby boomers” begin to collect their retirement pension.

After 2021, when most of the baby boomers have retired, and benefits paid begin to exceed contributions, investment revenues from the CPP’s accumulated assets will provide the funds necessary to make up the difference. However, contributions will remain the main source of funding for benefits.

The steady-state financing approach has moved the CPP away from pay-as-you-go financing (with a small reserve) towards fuller funding. By 2025, the Plan is expected to be about 25 percent pre-funded (i.e., Plan assets cover about 25 percent of benefits in pay and earned to that date). The move to steady-state financing has improved fairness across generations. Moving to full-funding would have contributors during the transition paying much higher contributions—they would have had to pay for the benefits of current retirees and for the development of a reserve to cover their own pensions. Continuing with a pay-as-you-go approach would also have been unfair, as it would have meant a sharp increase in the contribution rate over the coming decades.

According to the *Twenty-first Actuarial Report*, as at December 31, 2003, the Plan is 12 percent funded. The relative size of the unfunded liability

(\$516.3 billion at the end of 2003) will decline over time as Plan assets grow more rapidly than Plan liabilities over the next few decades and at least as quickly thereafter. As a result, by 2025, Plan assets will cover about 25 percent of the Plan’s actuarial liabilities. According to the Chief Actuary, the evolution of the funding level and the projected growth rates of assets and liabilities are better measures of the future financial health of the CPP than is the notion of the unfunded liability at a particular point in time.

A partially funded CPP not only balances the two approaches to funding, but also contributes to diversifying the funding of Canada’s retirement income system:

- the Old Age Security program, funded by federal government revenues, and
- private savings, including tax-deferred, fully funded employer-sponsored pension plans and registered retirement savings plans (RRSPs).

A diversified funding approach allows Canada’s retirement income system to be less vulnerable to changes in economic and demographic conditions than are systems in countries that use a single funding approach. In addition, the Canadian approach to pension provision, based on a mix of public and private pensions, is an effective way to provide for retirement income needs, according to international organizations.

## 2004 Budget Changes to the CPP

Following extensive consultations with provincial finance ministers, the Government of Canada's 2004 Budget proposed a number of changes to the CPP, including some to the disability benefit and to the Plan's contribution requirements. The changes to the disability benefit are intended to encourage more clients who believe that they may be able to

work to try to return to regular employment. The changes to contribution requirements are intended to reduce the compliance burden on employers.

The proposed changes were included in the budget implementation bill that was tabled in Parliament on March 23, 2004.



## Financial Accountability

Since 1999-2000, the CPP has used the accrual basis of accounting for revenues and expenditures. This method gives administrators a detailed financial picture and allows accurate matching of revenue and expenditures in the year in which they occur.

As at March 31, 2004, total CPP assets were valued at approximately \$72.5 billion. Net plan assets are contributions and investment income that have accumulated since the Plan's inception in 1966—less benefit and administrative expenditures over the same period. According to the Chief Actuary, Plan assets are expected to increase appreciably over the next decades.

### CPP ACCOUNT

A separate account, the CPP Account, has been established in the accounts of the Government of Canada to record the financial elements of the Plan: contributions, interest, pensions and other benefits paid, and administrative expenditures. The CPP Account also records the amounts transferred to or received from both the CPP Investment Fund and the CPP Investment Board. Spending authority is limited to the Plan's net assets. The CPP assets are not part of the federal government's revenues and expenditures.

Prior to the coming into force of Bill C-3 (*An Act to Amend the Canada Pension Plan and the Canada Pension Plan Investment Board Act*), the Canada Pension Plan Investment Board was responsible for investing net new funds, while the CPP Account's operating balance and bond portfolio were managed by the Government of Canada. The amended legislation provides for the transfer of CPP assets that were previously administered by the federal government to the CPP Investment Board, beginning in 2004. These assets consist of the bonds held by the CPP

Investment Fund and a portion of the deposit with the Receiver General for Canada. The CPP Investment Board and the federal government have signed an agreement governing the transfer of the assets.

The bonds will be transferred to the Board over a three-year period beginning in May 2004. Funds on deposit with the Receiver General for Canada will be transferred over a period of 12 months beginning in September 2004.

### CPP INVESTMENT BOARD

The CPP Investment Board was created by an Act of Parliament in December 1997 to invest funds not required by the Canada Pension Plan to pay current benefits.

The Board is independent of the CPP. It operates at arm's length from government and is overseen by an independent board of directors. Its legislated mandate is to manage funds transferred from the CPP "in the best interests of the contributors and beneficiaries of the Plan." The Board is to invest CPP assets "with a view to achieving a maximum rate of return, without undue risk of loss." It must also consider the factors that affect the Plan's funding and its ability to meet its financial obligations.

The CPP Investment Board has a long-term investment horizon. In his most recent report, the Chief Actuary of Canada estimates that contribution revenues will exceed CPP benefit payments and expenses well into the future, and that the CPP will not need money from investment income until 2022.

Further information on the Board's mandate, governance structure and investment policy can be found at [www.cppib.ca](http://www.cppib.ca).



### **CPP Assets**

As at March 31, 2004, CPP assets consisted of \$39.7 billion in fixed-income securities, cash and other assets, and \$32.8 billion in publicly traded stocks, private equities, real estate and infrastructure assets.

The CPP reserve fund earned \$10.3 billion for a return of 17.6 percent for the fiscal year ending March 31, 2004.

### **Investing for our future**

The CPP Investment Board believes that publicly traded equities will outperform fixed income assets over the long term. Consequently, the Board will continue to invest in publicly traded equities or stocks so that CPP assets are allocated in a way that reflects the long-term funding requirements of the Plan.

To complement its \$30.1 billion passive public equity portfolio, the CPP Investment Board has expanded into private equities through externally managed funds that provide venture capital and expansion financing to private companies. These investments

are made through limited partnerships or pooled funds managed by investment firms in Canada and around the world.

As at March 31, 2004, private equity commitments by the CPP Investment Board were approximately \$6 billion, of which \$2 billion had been invested. These commitments covered 42 limited partnerships managed by 36 general partners, representing investments in more than 2,500 underlying companies.

Like other major pension funds, the CPP Investment Board is looking for opportunities to increase investments in real return assets, such as real estate and infrastructure, because their value over time will likely track and surpass the general rate of inflation.

In compliance with its statutory requirement to hold a public meeting in each participating province at least once every two years, the Board held public meetings in the provincial capitals in January 2001 and June 2002. The next meetings are planned for September-October 2004.



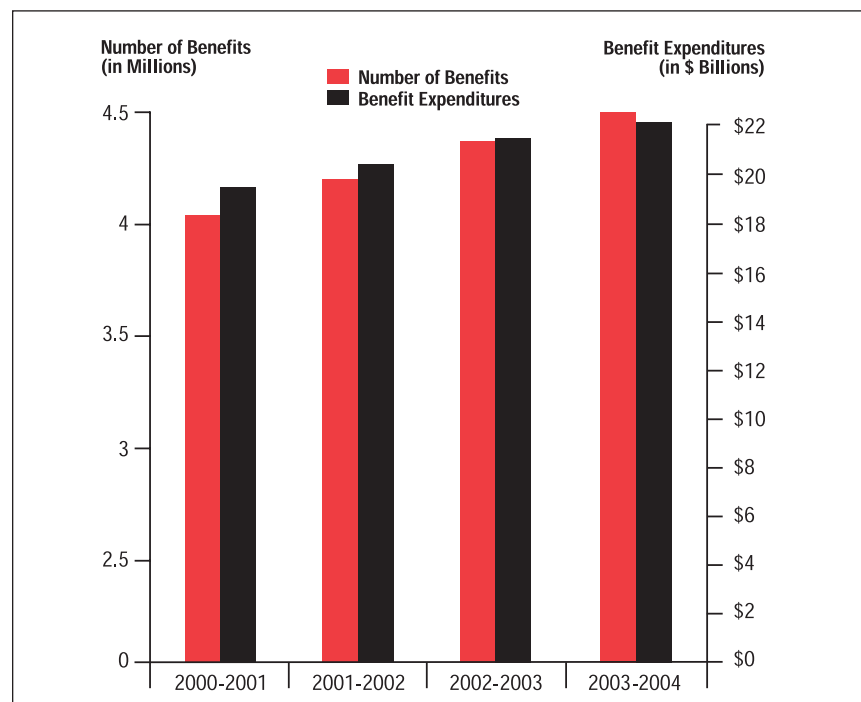


## Benefits and Expenditures

The number of people receiving CPP benefits has increased steadily over the past decade. As a result, Plan expenditures have increased. Figure 1 shows

the yearly increases since 2000-2001. Figure 2 (page 11) shows the percentage of CPP expenditures by type of benefit.

**Figure 1 – BENEFITS AND EXPENDITURES BY FISCAL YEAR**



### RETIREMENT PENSIONS

Retirement pensions represent 66 percent of the total number of CPP benefits paid and 70 percent of the total benefit dollars paid out by the CPP in 2003-04. The amount of each contributor's pension depends on how much and how long he or she has contributed and at what age he or she begins to draw the benefits. In March 2004, the monthly maximum retirement pension was \$814.17; the average payment was \$457.66.

The CPP offers flexibility with respect to the age of retirement. Seniors can take their pension as early as the age of 60 or receive a larger pension if they wait until after they turn 65 to begin receiving it. The CPP permanently reduces the pension by 0.5 percent per month for those who take their pension before their 65th birthday, reflecting the fact that these seniors will, on average, receive their benefits longer than someone who retires at the age of 65. For those who take their pension after their 65th birthday, the CPP permanently increases the pension by 0.5 percent

per month (up to a maximum of 30 percent), reflecting the fact that these seniors will receive their benefits for a shorter amount of time on average. The adjustments are intended to ensure that there is no advantage or disadvantage from taking the retirement benefit at a particular age. The Chief Actuary of the Canada Pension Plan completed a study on this issue in March 2003. It found that, given current Plan provisions, the adjustments for early/late pension take-up create an incentive to take the benefit early. Removing this incentive would require the downward adjustment of early pensions and upward adjustment of late pensions. The study also noted that the neutrality of the Plan's adjustment factors would be improved by changing the benefit calculation and contribution requirements.

The study is available at [www.osfi.gc.ca](http://www.osfi.gc.ca).

## DISABILITY BENEFITS

Disability benefits, paid to eligible contributors and their children, represent 8 percent of the total number of CPP benefits paid and 14 percent of the total benefit dollars paid out by the CPP in 2003-04. In March 2004, the maximum monthly disability benefit was \$992.80; the average payment was \$747.04. The children's monthly benefit was a flat rate of \$192.68.

The 2004 Budget Implementation Bill included amendments to the CPP to allow for reinstatement of a CPP disability benefit that had been stopped because a person had returned to work if the person again became incapable of working within two years after the stopping of the benefit.

The planned implementation date for the new automatic reinstatement protection is early 2005.





## SURVIVOR BENEFITS

Survivor benefits, paid to the surviving spouse or common-law partner of the contributor and his/her dependent children, represent 23 percent of the total number of CPP benefits paid and 15 percent of the total benefit dollars paid out by the CPP in 2003-04. The amount of the monthly survivor benefit varies depending on a number of factors, including the age of the spouse or common-law partner at death and whether the beneficiary also receives other CPP benefits.

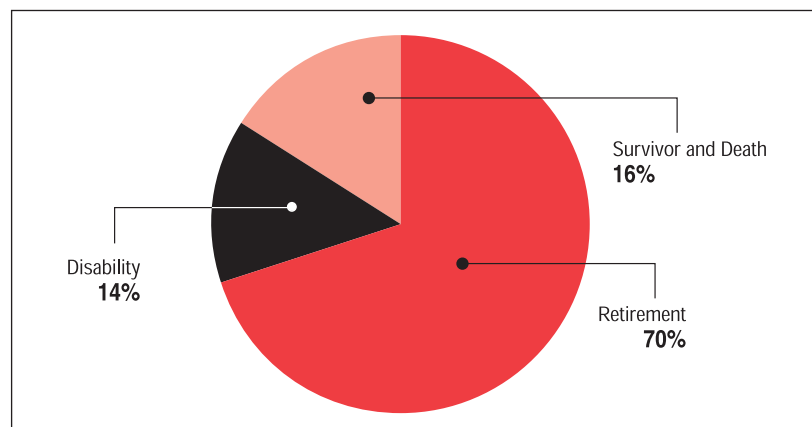
## DEATH BENEFITS

Death benefits represent 3 percent of the total number of CPP benefits paid and 1 percent of the total benefit dollars paid out by the CPP in 2003-04. The death benefit is a one-time payment. The maximum payable is \$2,500; the average payment in March 2004 was \$2,214.10.

## OTHER PROVISIONS

The CPP includes provisions that compensate for periods of low earnings, namely the child rearing provision (CRP) and the 15 percent general drop-out provision. The CRP allows the CPP to drop up to seven years of low or zero earnings (while caring for a child under the age of seven) from the calculation of a contributor's CPP disability, survivor and/or retirement benefit. The 15 percent general drop-out provision is for low or zero earning years and applies to all contributors. The Plan has other provisions under which married or common-law spouses may either share their retirement pensions (where the union is intact) or split their credits (where the union has dissolved).

**Figure 2 – PERCENTAGE OF BENEFIT DOLLARS PAID FOR 2003-2004**



## Improved Service Delivery

### REACHING OUT TO CANADIANS

During 2003-04, Social Development Canada continued its efforts to help Canadians better understand public pensions and the retirement income system, and to encourage them to actively plan and prepare for their own retirement. Information on the CPP is available in print, on the Internet, in person at local offices, by phone, and at electronic kiosks in government offices and public buildings.

Personalized contact with clients continued to receive high priority. In 2003-04, SDC issued personal CPP Statements of Contributions to more than 2.2 million contributors between the ages of 18 and 70. The statements were accompanied by information on the retirement income system in Canada.

### DELIVERING SERVICE

In 2003-2004, SDC continued to modernize CPP program delivery. With the multi-year Information Technology Renewal project, staff now have access to a consolidated view of complete CPP and OAS client and benefit information, benefit payment history and lifetime CPP contributions. In addition,

fully automated adjudication (determination of eligibility and calculations of entitlement) has been introduced for CPP retirement benefits. Capabilities for automated adjudication of additional benefits will continue over the next several years. At the same time, the Department continues to focus on maintaining the existing CPP information technology systems.

### PROCESSING BENEFITS

CPP services are offered in person, by telephone, online and by mail. In 2003-04, staff received 60,514 disability applications. Decisions on 82 percent of all CPP disability applications, which are complex and require medical information, were made within 120 calendar days of receipt of the completed application. Improved communication with clients and their physicians helped staff make well-informed decisions and helped CPP disability applicants better understand the reasons for decisions. As a result, close to 81.6 percent of the applications for disability benefits in 2003-04 were finalized in the initial stages. Retirement pension applications, which make up the bulk of the CPP applications, and which are less complex, were processed within an average of 22 days (see Table 1 below).

**TABLE 1 – SPEED OF PROCESSING NEW APPLICATIONS**

<b>National speed-of-service measures</b>	<b>Objective</b>	<b>2003-04 National Average</b>
Number of working days to process initial CPP applications* (excluding disability applications)	28	22
Number of working days to process initial disability applications	70	82

\*Number of days between the date the application is received and the date of the decision.



**TABLE 2 – TELEPHONE SERVICE STATISTICS\***

	<b>2002-03</b>	<b>2003-04</b>
Percentage of clients served by a service agent within 180 seconds of placing a call**	96.3%	99%
Average waiting time to speak with a service agent	20 sec.	16 sec.
Average time clients spend talking to a service agent	237 sec.	229 sec.

\* Table includes CPP and Old Age Security totals. Speed of service does not vary between programs.

\*\* The objective is to serve clients within 180 seconds for 95 percent of calls.

SDC call centres received over 2 million calls about the CPP in 2003-04. Positive responses to the mail-out of personalized statements to CPP contributors and inquiries during the traditionally busy T4 period contributed to the high number of calls.

Despite higher call volumes, service to clients continues to improve. In 2003-04, enhanced call management allowed for improved telephone service. Results show in the reduction of client waiting time and a significant increase in the speed of service (see Table 2 above).



## Managing the CPP

### COLLECTING AND RECORDING CONTRIBUTIONS

Contributions to the CPP are paid on earnings between a minimum and a maximum amount. The minimum (which remains constant) is \$3,500 and the maximum is adjusted annually to reflect the growth in the average Canadian industrial wage. The maximum amount of pensionable earnings as of January 1, 2004, was \$40,500 (up from \$39,900 in 2003). Contributions stop once a contributor reaches the age of 70 or begins to receive a CPP retirement pension or disability benefit.

The contribution rates for 2004 are 4.95 percent for employees and 4.95 percent for employers. People who are self-employed pay both portions, for a total of 9.9 percent. Employers and employees make approximately 94 percent of contributions; the remaining 6 percent comes from the self-employed.

All CPP contributions are remitted to the Canada Revenue Agency (CRA). In 2003-04, contributions amounted to \$28 billion.

CRA also assesses and verifies earnings and contributions, advises employers and employees of their rights and responsibilities, conducts audits, and reconciles reports and T4 slips. To verify that contribution requirements are being met, CRA applies a compliance and enforcement process that can vary from a computerized data match to an on-site audit. There are approximately 1.5 million existing employer accounts. During 2003-04, CRA conducted 62,905 audits, concentrating on files with irregularities.

### OVERPAYMENT OF BENEFITS

Consistent with its mandate to manage the CPP effectively, the Department has procedures in place to detect benefit overpayments. During 2003-04,

overpayments totalling \$45 million were detected. Of this amount, \$37 million was recovered and remission was granted of debts totalling \$4 million. The remaining \$4 million was in the process of being collected at the end of the 2003-04 fiscal year and is included in the CPP's accounts receivable.

### CHANGES ANNOUNCED IN THE 2004 BUDGET

In 2004, the rules governing contributions to the Canada Pension Plan were amended. They now allow a new employer who immediately succeeds another as a result of a change in business structure to take into account the contributions the predecessor employer made for that same employee when determining amounts due. This change was extended to situations where self-employed individuals become employees of a corporation controlled by them or vice versa. The new rules apply for every year after 2003.

Before this change, when a business was restructured—notably as a result of a winding up and immediate reconstitution under a different legal structure (e.g., where a limited partnership is reconstituted as a corporation) or the acquisition of a major portion of the employer's property or of a distinct part of the employer's business (e.g., a distinct division of a business is sold to another enterprise)—employees were treated as if they had new employers. Employers were required to begin withholding CPP contributions anew and they could not take into account the contributions withheld at source by the previous employer—even if there had been no interruption of service by the employee.

Other amendments clarify the annual employers' contributions amount required under the Act and specify that only amounts remitted in excess may be refunded to the employer.



These changes will ensure harmonization of contribution requirements between the Canada Pension Plan and the Quebec Pension Plan. Further information about these changes can be obtained by contacting the Canada Revenue Agency at 1 800 959-5525.

### ADMINISTRATIVE COSTS

In 2003-04, it cost approximately \$410 million to administer the CPP, with Human Resources Development Canada (now SDC) accounting for the largest portion—\$309 million (see Table 3 below). CRA required approximately \$85 million and Public Works and Government Services Canada (PWGSC) \$15 million, for services to the CPP. The Office of the Superintendent of Financial Institutions (OSFI), where the Office of the Chief Actuary is housed, and the Department of Finance incurred costs of about \$1 million and \$425,000, respectively.

Since the administrative costs of the CPP Investment Board are drawn from the Board's investment income, they are reported in that organization's annual report. This is consistent with the arm's-length administration of the Board. In 2003-04, the CPP Investment Board reported \$24 million in operating expenses and external investment management fees.

CPP administrative expenses in 2003-04 represent 1.72 percent of the \$22.6 billion in benefits paid. This ratio compares very favourably with that of other pension plans. CPP administrative costs also compare favourably with those of RRSPs.

Table 3 presents the CPP's administrative expenditures for the last three years.

**TABLE 3 – CPP ADMINISTRATIVE COSTS 2001-02 TO 2003-04**

Department/Agency	Expenditures (in \$ thousands)		
	2001-02	2002-03	2003-04
Social Development Canada (formerly HRDC)	\$279,159	\$327,964	\$308,923
Canada Revenue Agency	77,618	80,229	85,258
Public Works and Government Services Canada	12,440	12,823	14,693
Office of the Superintendent of Financial Institutions	1,364	690	1,038
Finance Canada	492	495	425
Total	\$371,073	\$422,201	\$410,337

### THE APPEALS PROCESS

There are three opportunities for review of a person's CPP benefit application (as shown on page 16). Most requests for review concern an application for disability benefits.

The first opportunity involves a request to the Minister of Human Resources and Skills

Development (see note on the inside cover of this report) for a reconsideration (or administrative review) of a decision concerning a benefit or a division of pension credits. The number of requests for reconsideration in disability cases declined from 12,401 in 2002-03 to 10,207 in 2003-04, a decrease of about 18 percent.

The number of benefits awarded at reconsideration remained relatively unchanged from 2002-03 to 2003-04, increasing from 27 percent to 28 percent.

A person who is not satisfied with the decision made at the departmental reconsideration level can appeal to a Review Tribunal. A Review Tribunal is an independent body made up of three people chosen by the Commissioner of Review Tribunals from a panel of 100 to 400 part-time members appointed by the Governor-in-Council. In 2003-04, the Office of the Commissioner of Review Tribunals (OCRT) received 4,744 appeals under the CPP. In the same period, the OCRT issued 4,503 decisions, of which 2,312 (51.3 percent of the total) had been decided in favour of the appellant. In addition, another 853 cases were concluded as a result of settlements offered by Social Development Canada.

The final opportunity for review is the Pension Appeals Board (PAB)—a tribunal operating at arm's length from SDC. Board members are judges or former judges of the federal court or a superior court of a province. Hearings are not automatic at this level; claimants or the Minister must request "leave to appeal". Ninety-five percent of the 1,183 applications for leave received in 2003-04 concerned CPP disability benefits. Of the total number of applications for leave received, 84 percent were granted. With respect to final decisions, 53 percent were in favour of the claimant.

The Department continues to work with the Office of the Commissioner of Review Tribunals and the Pension Appeals Board to improve coordination and response times and to identify opportunities for the earliest possible resolution of appeals.

## THE APPEALS PROCESS

### INITIAL DECISION

Social Development Canada (SDC) issues a decision on CPP benefit eligibility.

If the client is not satisfied with the decision, he or she can submit a request for reconsideration to the Minister of Social Development.

### FIRST LEVEL OF REVIEW Review of client file and decision issued by SDC

If the client is not satisfied with the decision, he or she has 90 days to appeal to the Office of the Commissioner of Review Tribunals.

### SECOND LEVEL OF REVIEW Appeal to the Office of the Commissioner of Review Tribunals

The case is heard and a decision is issued.

If either the client or SDC is not satisfied with the decision, an application for "Leave to Appeal" may be submitted to the Pension Appeals Board.

### THIRD LEVEL OF REVIEW Appeal to the Pension Appeals Board

If leave is granted, the case is heard and a decision is issued.

The decision of the Pension Appeals Board is final, subject to judicial review by the Federal Court of Canada.



## Looking to the Future

Some 300,000 new CPP applications are received each year and a significant increase is expected as our population ages. The challenge will be to improve service delivery to ensure that Canadians continue to receive timely, accurate and client-focused service. Long-term initiatives aimed at meeting that challenge are now underway.

### CPP ONLINE

CPP Online supports the objectives of the federal Government On-Line (GOL) initiative and the commitment to provide Canadians with full electronic access to key federal information and services by 2005. CPP Online initiatives include the implementation of a web-based system that allows a wider range of inquiries and client transactions online and provides more integrated information on related benefits. The importance of strengthening our technological infrastructure is clear, especially since the fastest-growing group of Internet users is the senior population.

The Department made it a priority to update the systems that help deliver benefits. Evolving over the next four years, the systems will support better decision making by improving the information available to management, clients and staff through faster and more up-to-date technology. The improvements will further reduce the paper burden and the complexity of the application process.

Putting CPP information online is a multi-year project designed to provide Canadians with online access to information, data, and services essential to income security and retirement planning. A com-

prehensive review of legislation, regulations, policies, and procedures will lay the groundwork for an innovative, leading-edge approach to online services and their policy and program context.

### ONLINE SERVICES

By 2007, the Department will offer, in a secure environment, a number of online service options to allow access to information and services that are essential to income security and retirement. These services will include:

#### **View and update personal information**

In 2005, CPP clients will have secure online access to their personal information. Using this service, they will be able to view and update their mailing address and direct-deposit information, and view their monthly payment amount. Enhancements will continue to be made, allowing more information to be viewed and updated in coming years.

#### **Streamlined and automated CPP Statement of Contributions**

CPP contributors can now submit an online request to receive a copy of their Statement of Contributions by mail. In 2005, they will be able to view Statement of Contributions information online.

#### **Tax information slips online**

Since 2004, CPP clients have been able to view their CPP T4 slips online, starting with those for the 2003 taxation year. They also have the option to choose to use the online service to access their T4 slips in the future instead of having them sent by mail.

## SIMPLIFYING THE APPLICATION PROCESS

Simplifying the application process for the CPP retirement pension is part of the Department's planned service delivery improvements. The goal is to make the application process easier for clients through streamlined, client-driven and more effective services.

Making it easier to apply for the CPP retirement pension will be the first step in building a modern service system that is based on Canadians' needs and expectations. It will allow the use of alternative sources for proof of date of birth. As part of this initiative, services are being introduced that allow clients to apply for benefits online.

Since July 2003, a simplified CPP retirement application has been available for clients to fill out online. In March 2004, simplified OAS applications were also made available online. While clients could fill out these forms on the computer, they had to be printed, signed and mailed to SDC along with proof of birth. In 2005, SDC will remove the requirement for the majority of clients to provide documentary proof of birth when the client's age and identity can be validated with the Social Insurance Register electronically.

In March 2004, SDC launched its first benefit application form that can be submitted over the Internet. Clients are now able to fill out a CPP retirement pension application online and submit it electronically. To complete the application process, clients must print, sign and mail a "Signature Page" along with their proof of birth. When client authentication enhancements are completed, clients will be able to sign their applications electronically.





## REACHING ALL CANADIANS

Public pension programs help millions of people in Canada every day. The Department's primary objective is that every Canadian receive the benefits to which he or she is entitled under its programs.

There has been a dramatic decline in the low-income rate among Canadian seniors in recent decades. This is due in large part to the existence of public pensions such as the CPP.

Over the past several years, the Department has made a concerted effort to tell Canadians what they can expect from their public pensions and how they should prepare for their own retirement. Striving to communicate as directly as possible, the CPP will continue improving and personalizing its programs to reach its clients.

The Internet has a tremendous ability to reach Canadians. Social Development Canada has led the development of a cross-departmental website called Canada Benefits ([www.canadabenefits.gc.ca](http://www.canadabenefits.gc.ca)). The site's mandate is to provide central access to government-wide benefit programs and services for individuals.

The Canada Benefits site provides access to federal, provincial and territorial programs and services. These include, among others, public pensions, employment insurance benefits, and housing grants. The award-winning website supports the "citizen-first" principle—where information is organized according to the needs of Canadians and not the structures of government. For example, an interactive tool called the "Benefits Finder" provides citizens with a listing of programs and services relevant to their circumstances.

Since its update in January 2003, the Canada Benefits site has experienced significant success, receiving an average of 2,000 visitors every day. Through the Canada Benefits site and other means of communication, SDC was able to reach more Canadians than ever. Based on the firm conviction that all Canadians deserve financial security, the Department strives to make them aware of the benefits available and helps them obtain those to which they are entitled.







2003-2004

◦ **ANNUAL REPORT** of the Canada Pension Plan



Canada Pension Plan

# Financial Statements

for the year ended March 31, 2004

## Management's responsibility for financial statements

The financial statements of the Canada Pension Plan have been prepared by management of Social Development Canada in accordance with the Canadian generally accepted accounting principles.

Management is responsible for the integrity and objectivity of the data in these financial statements, including the amounts which must, of necessity, be based on best estimates and judgements. The financial information presented throughout the Annual Report is consistent with the financial statements.

In support of its responsibilities, management has developed and maintains systems of internal control and supporting procedures. They are designed to provide reasonable assurance that assets are safeguarded, recorded and properly maintained and transactions are properly authorized and are in accordance with the *Canada Pension Plan* and *Financial Administration Act* and accompanying regulations. These controls include the establishment of an organizational structure that provides a well defined division of responsibilities and accountability, the selection and training of qualified staff, and the communication of policies and guidelines throughout the organization. Internal controls are reviewed and evaluated by both internal and external auditors in accordance with its respective audits. Management also reviews the recommendations of its internal and external auditors for improvements in internal controls.

The Auditor General of Canada, the external auditor of the Canada Pension Plan, has conducted an independent audit of the financial statements in accordance with Canadian generally accepted auditing standards and has reported to the Minister of Social Development.

---

Janet Milne

Assistant Deputy Minister  
Financial and Administrative Services

---

Nicole Jauvin

Deputy Minister  
Social Development Canada

September 2, 2004



Auditor General of Canada  
Vérificatrice générale du Canada

## AUDITOR'S REPORT

To the Minister of Social Development

I have audited the statement of net assets of the Canada Pension Plan as at March 31, 2004 and the statements of changes in net assets and cash flow for the year then ended. These financial statements are the responsibility of the management of Social Development Canada. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Canada Pension Plan as at March 31, 2004 and the changes in its net assets and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Sheila Fraser, FCA  
Auditor General of Canada

Ottawa, Canada  
September 2, 2004

# Statement of Net Assets

## as at March 31

	2004	2003
		Restated (Note 3)
	(in millions of dollars)	
<b>Assets</b>		
<b>Investments</b>		
CPP Investment Fund – at fair value (Note 4)		
Provincial and Territorial bonds	25,397	26,080
Canada bonds	4,070	4,071
CPP Investment Board – at fair value (Note 5)	32,894	17,453
<b>Cash</b>		
Deposit with Receiver General for Canada	7,483	7,093
<b>Receivables</b>		
Contributions	1,946	1,631
Accrued interest	862	939
Régime des rentes du Québec	28	66
Beneficiaries (Note 6)	36	49
	72,716	57,382
<b>Liabilities</b>		
Accounts payable	55	74
Accrued pensions and benefits	51	55
CPP Investment Board's Liabilities, net of its other assets	99	2
	205	131
<b>Net Assets</b>	72,511	57,251
<b>Net Assets, represented by:</b>		
Canada Pension Plan Investment Fund	29,467	30,151
Accumulated transfers to Canada Pension Plan Investment Board	29,824	21,690
Accumulated net gain (loss) from Investment Board's operations	2,971	(4,239)
Canada Pension Plan Account (Note 7)	7,483	7,093
CPP receivables, net of liabilities	2,766	2,556
<b>Net Assets</b>	72,511	57,251

*The accompanying notes are an integral part of these financial statements.*

Approved by Social Development Canada:

Janet Milne

Assistant Deputy Minister  
Financial and Administrative Services

Nicole Jauvin

Deputy Minister  
Social Development Canada



## Statement of Changes in Net Assets

for the year ended March 31

	2004	2003
		Restated (Note 3)
	(in millions of dollars)	
<b>Net assets, beginning of year</b>	<b>57,251</b>	<b>55,094</b>
<b>Increase in assets</b>		
Contributions (Note 8)	<b>28,029</b>	25,203
Investment Income / (loss) (Note 9)	<b>10,248</b>	(1,049)
	<b>38,277</b>	24,154
<b>Decrease in assets</b>		
Pensions and Benefits		
Retirement	<b>15,880</b>	15,071
Survivors	<b>3,194</b>	3,071
Disability	<b>2,850</b>	2,779
Disabled Contributor's Child	<b>257</b>	251
Death	<b>255</b>	234
Orphan	<b>213</b>	210
Net overpayments	<b>(42)</b>	(41)
	<b>22,607</b>	21,575
Administration costs (Note 10)	<b>410</b>	422
	<b>23,017</b>	21,997
<b>Increase in net assets</b>	<b>15,260</b>	2,157
<b>Net assets, end of year</b>	<b>72,511</b>	<b>57,251</b>

*The accompanying notes are an integral part of these financial statements.*

## Statement of Cash Flow

for the year ended March 31

	2004	2003
	(in millions of dollars)	
<b>Cash Flow Provided by Operating Activities</b>		
<b>Cash Receipts:</b>		
Contributions	27,714	24,950
Interest from CPP Investment Fund	2,572	2,839
Interest on Deposit with Receiver General for Canada	188	163
Recoveries from Régime des rentes du Québec	288	192
Recoveries from beneficiaries	37	37
	<b>30,799</b>	<b>28,181</b>
<b>Cash Payments:</b>		
Pensions and Benefits	(22,634)	(21,613)
Repayments to Régime des rentes du Québec	(251)	(235)
Administration costs	(430)	(395)
	<b>(23,315)</b>	<b>(22,243)</b>
	<b>7,484</b>	<b>5,938</b>
<b>Cash Flow Used In Investing Activities</b>		
Transfers to CPP Investment Board	(8,134)	(7,318)
Disposals of bonds – CPP Investment Fund	2,498	2,383
Reinvestments in bonds – CPP Investment Fund	(1,458)	(680)
	<b>(7,094)</b>	<b>(5,615)</b>
<b>Net increase in the Deposit with Receiver General for Canada</b>	<b>390</b>	<b>323</b>
Deposit with Receiver General for Canada, beginning of year	7,093	6,770
<b>Deposit with Receiver General for Canada, end of year</b>	<b>7,483</b>	<b>7,093</b>

*The accompanying notes are an integral part of these financial statements.*



## Notes to financial statements March 31, 2004

### 1. DESCRIPTION OF THE CANADA PENSION PLAN

#### **a) Description of the CPP**

The Canada Pension Plan (CPP) is a federal/provincial plan established by an Act of Parliament in 1965.

The CPP began operations in 1966. It is a compulsory and contributory social insurance program operating in all parts of Canada, except Quebec, which operates the Régime des rentes du Québec, a comparable program. The Plan's objective is to provide a measure of protection to workers and their families against the loss of earnings due to retirement, disability or death.

The Minister of Social Development is responsible for the administration of the *Canada Pension Plan* (the CPP Act); the Minister of National Revenue is responsible for collecting contributions. The Minister of Finance and his provincial counterparts are responsible for setting CPP contribution rates, pension and benefit levels and funding policy.

The financial activities of the Canada Pension Plan are recorded in the CPP Account (Note 7). The CPP Investment Fund (Note 4) holds the bond portfolio of the Plan, and the Plan's investments in capital markets are managed by the CPP Investment Board (Note 5). The financial transactions affecting the Account and the Investment Fund are governed by the CPP Act and regulations. The Investment Board's transactions are governed by the *Canada Pension Plan Investment Board Act* and the accompanying regulations.

As stated in the CPP Act, changes to this Act require the approval of at least two-thirds of the provinces having, in the aggregate, not less than two-thirds of the population of all included provinces.

#### **b) Financing**

CPP is financed by contributions and investment returns. Employers and employees pay contributions equally to CPP. Self-employed workers pay the full amount.

CPP was designed initially to be financed on a pay-as-you-go basis, which means that the Plan would operate on a current basis with pensions and benefits being paid out of current contributions. With changes made to the Act in 1997, CPP is now intended to be funded on a "steady-state" basis—that is, combined contributions increased to 9.9% of pensionable earnings in 2003 and have leveled off since.

From 1966 to 1986, the combined employer-employee contribution rate remained at 3.6% of pensionable earnings. In 1987, it was raised to 3.8% and increased yearly by 0.2% to reach 5.6% in 1996. In the years 1997 to 2002, the combined contribution rate was increased annually to reach 9.9% in 2003. The maximum combined contribution for 2004 was \$3,663 (2003 – \$3,604).

The CPP Act provides that an actuarial report shall be prepared every three years for purposes of the review of the financial state of the CPP by the Minister of Finance and his provincial counterparts. The Eighteenth Actuarial Report of the Chief Actuary of the Office of the Superintendent of Financial Institutions done as at December 31, 2000 was presented to the Minister of Finance in December 2001, then tabled in the House of Commons on December 10, 2001. Based on this report, federal and provincial ministers of Finance concluded at the end of the 2002 Triennial Review process that the CPP is financially sound and that the 9.9% combined employee-employer contribution rate reached in 2003 is expected to be sufficient to sustain the Plan in the face of an aging population. A number of assumptions such as long term rate of return on assets, inflation rate, mortality rates, increase in salary and benefit rates, among other things, were used in the 18th CPP actuarial report. These assumptions reflect best estimates of future economic and demographic events. The next actuarial report as at December 31, 2003 is expected to be completed by December 2004.

### **c) Net assets of the Plan**

The net assets of the Plan are composed of the deposit with the Receiver General for Canada, short term investments, long term investments in bonds held by the CPP Investment Fund and investments managed by the CPP Investment Board. The net assets represent funds accumulated for the payment of pensions, benefits and administration costs. This amount does not cover the actuarial present value of accrued pensions and benefits. As at March 31, 2004, the net assets of the Plan are of \$72.5 billion (2003 – \$57.3 billion). This amount represents approximately 3.2 times the total of pensions and benefits for the year 2003-2004.

### **d) Pensions and benefits**

**Retirement pensions** – A retirement pension is payable to each contributor at age 60 or older, according to the provisions of the Act. The monthly amount is equal to 25% of the contributor's average monthly pensionable earnings during the pensionable period. The amount may be reduced or increased depending upon whether the contributor applies for a retirement pension before or after age 65. This adjustment cannot exceed 30%. The maximum new monthly pension payable at age 65 in 2004 is \$814.17 (2003 – \$801.25).

**Disability benefits** – A disability benefit is payable to a contributor who is disabled, according to the provisions of the Act. The amount of the disability benefit to be paid includes a flat-rate portion and an amount equal to 75% of the earned retirement pension. The maximum new monthly disability benefit in 2004 is \$992.80 (2003 – \$971.26).

**Survivor's benefits** – A survivor's benefit is payable to the spouse or common-law partner (the beneficiary) of a deceased contributor, according to the provisions of the Act. For a beneficiary under the age of 65, the benefit consists of a flat-rate portion and an amount equal to 37.5% of the deceased contributor's earned retirement pension. A beneficiary between the ages of 35 and 45 who is not disabled or who has no dependent children receives reduced benefits. For beneficiaries aged 65 and over, the benefit is equal





to 60% of the retirement pension granted to the deceased contributor. The maximum new monthly benefit payable to a beneficiary in 2004 is \$488.50 (2003 – \$480.75).

**Disabled contributor's child and orphan benefits** – According to the provisions of the Act, each child of a contributor who is receiving disability benefits or who died is entitled to a benefit as long as the child is under the age of 18, or is between the ages of 18 and 25 and attending school full-time. The flat-rate monthly benefit in 2004 is \$192.68 (2003 – \$186.71).

**Death benefits** – According to the provisions of the Act, a death benefit is a one-time payment to, or on behalf of, the estate of a contributor. The benefit amounts either to 10% of the maximum pensionable earnings in the year of death or six times the monthly retirement pension granted to the deceased contributor, whichever is less. The maximum death benefit in 2004 is \$2,500 (2003 – \$2,500).

**Pensions and benefits indexation** – As required by the Act, pensions and benefits are indexed annually based on the Consumer Price Index for Canada. The rate of indexation for 2004 is 3.2% (2003 – 1.6%).

## 2. SIGNIFICANT ACCOUNTING POLICIES

### a) Basis of presentation

These financial statements present the financial position, the changes in net assets and the cash flows of the Canada Pension Plan. They include the financial position of the CPP Investment Board and the results of its operations. These financial statements are prepared in accordance with Canadian generally accepted accounting principles and conform to the disclosure and accounting requirements of the CPP Act.

These financial statements do not provide information on the actuarial estimates required to meet future obligations of the CPP since the CPP Act does not require that the pensions and benefits be pre-funded.

The CPP, which is under joint control of the Government of Canada and participating provinces, is not considered to be part of the reporting entity of the Government of Canada. Accordingly, its financial activities are not consolidated with those of the Government.

### b) Valuation of investments

**Bonds held by the CPP Investment Fund and CPP Investment Board investments** are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

**Bonds held by the CPP Investment Fund** – The fair value is determined by calculating the present value of bonds' projected cash flows. The discount rate used is based as appropriate on the provincial, territorial

or government of Canada market rates. The fair value includes a further discount for the non-marketable and non-transferable characteristics of the bonds.

Bonds issued by the provincial and territorial governments can be redeemed prior to maturity at the option of these governments or renewed for another 20 years. There are distinct calculation methods for bonds early redemption or renewal that do not take into consideration the non-marketable and non-transferable characteristics.

Any early redemption or renewal could therefore result in transactions at amounts that differ from the recorded fair value of the bonds.

**CPP Investment Board's investments** – The fair value is determined as follows: quoted market prices for publicly traded equities and unit values for pooled funds. Unit values reflect the quoted market prices of the underlying securities.

In the case of private equity investments, where quoted market prices are not available, fair value is determined annually, commencing after the first year of ownership, based on carrying values and other relevant information reported by external managers of the limited partnerships in which the investments are made. These carrying values are determined by the external managers using accepted industry valuation methods.

The fair value of private market investments in income producing properties is determined annually, commencing after the first year of ownership, using accepted industry valuation methods, such as discounted cash flows and comparable purchase and sales transactions.

Fair value for the over-the-counter derivatives such as swaps is determined based on discounted cash flows and market prices for underlying assets with similar characteristics.

Money market securities are recorded at cost which, together with accrued interest income, approximates fair value.

### **c) Contributions**

**Contributions** include CPP contributions earned for the year. The Canada Customs and Revenue Agency collects contributions and measures them using the assessment of tax returns. In determining the amount of contributions earned for the year, the Agency considers cash received and contributions assessed, and makes an estimate for contributions related to tax returns not yet assessed. This estimate is subject to review and adjustments. Adjustments, if any, are recorded as contributions in the year they are known.

**d) Investment income recognition**

**CPP Investment Fund income** is recorded on the accrual basis and includes unrealized gains and losses on bonds held at the end of the year.

**CPP Investment Board's net income from operations** represents the Investment Board's investment income, less investment and administrative expenses. Investment income is recorded on the accrual basis and includes realized gains and losses on disposal of investments, unrealized gains and losses on investments held at the end of the year, dividend income (recognized on ex-dividend date), interest income, distributions from partnerships and trusts, and net operating income from private market real estate investments.

Realized gains and losses on investments sold during the year represent the difference between sale proceeds and cost, less related costs of disposition. Unrealized gains and losses represent in the difference between the fair value and cost of investments. The current year unrealized gains and losses represent the year-over-year change in this difference.

**e) Translation of foreign currencies**

**Transactions in foreign currencies** are recorded at the rates of exchange prevailing on the transaction date. Investments denominated in foreign currencies and held at the year end are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses are included in investment income.

**f) Pensions and benefits**

**Pensions and benefits** are recorded when payable.

**g) Net overpayments**

**Net overpayments** are composed of overpayments of pensions and benefits that were established during the year less remissions of debts granted.

**h) Administration costs**

**Administration costs** are recorded in the year to which they relate.

**i) Measurement uncertainty**

The preparation of financial statements in accordance with the Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as at the date of the financial statements and revenue and expenses for the year. Actual results could differ from these estimates. The most significant estimates are related to contributions, administration costs, allowance for doubtful accounts, the fair value of the bonds held by the CPP Investment Fund and the fair value of investments held by the CPP Investment Board.

### 3. CHANGE IN ACCOUNTING POLICY

During the year, a legislative amendment was approved which provided for the transfer of CPP assets to the CPP Investment Board (See Note 12).

In order to provide a consistent basis of accounting for the provincial, territorial and federal bonds between the CPP Investment Fund and the CPP Investment Board, the fair value accounting was adopted for bonds in 2004, unlike previous years where the bonds were accounted for at cost. This change in accounting policy was applied retroactively and the prior year's financial statements were restated accordingly.

As a result of this change in accounting policy, unrealized gains and losses on bonds are now recognized in the statement of change in net assets and the bonds are recorded at their fair value in the statement of net assets.

The following summarizes the changes to financial statements as a result of the change in accounting policy for the years presented:

	2004		2003	
	(in millions of dollars)			
	Bonds recorded		Bonds recorded	
	at cost	at fair value	at cost	at fair value
Statement of Net Assets				
Assets				
CPP Investment Fund				
Provincial and Territorial bonds	22,181	25,397	23,204	26,080
Canada bonds	3,352	4,070	3,369	4,071
Net Assets	68,576	72,511	53,673	57,251
Statement of Changes in Net Assets				
Net Assets, beginning of year	53,673	57,251	51,709	55,094
Investment income (loss)	9,891	10,248	(1,242)	(1,049)
Net Assets, end of year	68,576	72,511	53,673	57,251



#### 4. INVESTMENTS HELD BY THE CPP INVESTMENT FUND

The Canada Pension Plan Investment Fund was established in the accounts of Canada by the CPP Act to record the Plan's investments in bonds of the provinces, territories and Canada. The CPP Investment Fund's bond portfolio is administered by the federal Department of Finance.

Until the end of 1997, the investments in provincial, territorial and federal government bonds were made with the cash on hand in excess of the Plan's forecast three-month operating requirement. These bonds were not marketable and had a 20-year term (or less) as fixed by the Minister of Finance on the recommendation of the Chief Actuary of the Office of the Superintendent of Financial Institutions. The interest rate on the bonds was determined by the Minister of Finance based on the average yield to maturity of all outstanding Government of Canada obligations with terms of 20 years or more. When these bonds matured, funds not required for payment of pensions and benefits were re-invested in new bonds.

Beginning in 1998, a maturing provincial or territorial bond may be re-invested in a new bond only once for a term of 20 years, if both the issuer asks to do so and the operating balance is sufficient to pay current pensions and benefits. Excess funds not re-invested are transferred to the CPP Investment Board. The re-invested bonds remain not marketable and bear interest at a rate fixed by the Minister of Finance. The interest rate is substantially the same rate that the province would pay if it were to borrow the same amount for the same term through the issuance of a bond on the public capital markets. Interest earned on the investments is paid semi-annually to the CPP Account.

During the year, all disposals of bonds were made, at maturity date, at face value. The bonds are redeemable in whole or in part before maturity. Since January 31, 2001, the provinces and territories are permitted to redeem their bonds held by the CPP Investment Fund prior to their maturity at a value equivalent to market value. No bonds were redeemed by the provinces and the territories prior to maturity during the year ended March 31, 2004 (2003 – none).

The bonds held by the CPP Investment Fund are exposed to interest rate risk. Interest rate risk refers to the risk of an adverse change in the fair value of the bonds as a result of an unfavourable movement in market interest rates.

The following schedule provides information on the disposals, re-investments, unrealized gains / (losses) and balance of the Investment Fund:

## CPP Investment Fund

	(in millions of dollars)					
	March 31, 2003 at cost	Disposals	Re- Investments	March 31, 2004 at cost	March 31, 2004 at fair value	March 31, 2003 at fair value
Newfoundland	633	51	51	633	714	700
Prince Edward Island	140	11	11	140	159	156
Nova Scotia	1,079	91	91	1,079	1,232	1,212
New Brunswick	834	71	71	834	940	920
Quebec	96	5	5	96	111	108
Ontario	10,746	1,201	688	10,233	11,687	12,065
Manitoba	1,128	126	–	1,002	1,167	1,292
Saskatchewan	1,151	109	40	1,082	1,241	1,299
Alberta	3,385	441	200	3,144	3,661	3,860
British Columbia	4,008	375	301	3,934	4,481	4,464
Yukon Territory	4	–	–	4	4	4
	23,204	2,481	1,458	22,181	25,397	26,080
Canada	3,369	17	–	3,352	4,070	4,071
	26,573	2,498	1,458	25,533	29,467	30,151

The further discount included in the fair value to allow for the specific characteristics of the bonds is valued at \$1.26 billion (\$1.27 billion in 2003). The following schedule presents the bonds by maturity dates and the weighted-average annual rate of return on bonds currently held.

	2004 (in millions of dollars)		2003	
	Investments at cost	Average coupon	Investments at cost	Average coupon
Investments maturing				
Within 1 year	2,283	13.35%	2,498	11.77%
1 – 5 years	9,429	10.23%	9,700	10.99%
Over 5 years	13,821	8.37%	14,375	8.90%
Total – Investments	25,533		26,573	
Weighted-average yield on investments		9.50%		9.93%



## 5. INVESTMENTS HELD BY THE CPP INVESTMENT BOARD

The Canada Pension Plan Investment Board (CPPIB) was established by an Act of Parliament in 1997. The *Canada Pension Plan Investment Board Act* came into force on April 1, 1998. The purpose of the Board is to invest the funds transferred by the CPP in a diversified portfolio of investments. The Board is designed to operate at arm's length from the government. It is required to be accountable to the public, Parliament (through the federal Minister of Finance), and the provinces and provides regular reports of its activities and the results achieved.

The following schedule provides information on the Board's investments as at March 31.

	2004	2003
	(in millions of dollars)	
Canadian equities, at fair value		
Public Markets	18,046	11,051
Private Markets	282	261
	18,328	11,312
Non-Canadian equities, at fair value		
Public Markets	7,552	4,245
Private Markets	1,530	1,265
	9,082	5,510
<b>Total Equities</b> (Cost 2004 – \$25,034; 2003 – \$20,336)	<b>27,410</b>	<b>16,822</b>
Real Return Assets		
Public markets real estate	350	219
Private markets real estate	432	246
Private markets infrastructure	22	–
<b>Total Real Return Assets</b> (Cost 2004 – \$829; 2003 – \$645)	<b>804</b>	<b>465</b>
Money Market Securities (Cost 2004 – \$4,784; 2003 – \$575)	4,777	575
Investment Receivables (Cost 2004 – \$68; 2003 – \$41)	68	41
Investment Liabilities (Cost 2004 – \$170; 2003 – \$452)	(171)	(449)
Net fair value of Derivatives	6	(1)
<b>Total Net Investments</b>	<b>32,894</b>	<b>17,453</b>

The CPP Investment Board has established investment policies which set out the manner in which assets shall be invested. In determining the asset mix, the CPP Investment Board takes into consideration certain assets of the CPP which are held outside the CPP Investment Board.

In accordance with the Investment Policy, at least 70% of the book value of the CPP Investment Board's portfolio is allocated to Canadian investments and the remainder to non-Canadian investments.

The CPP Investment Board's investments are mainly allocated to equities. During the current year, the CPP Investment Board made its first investment in a private market infrastructure fund. The CPP Investment Board also obtains exposure to real estate through investments in publicly traded securities and privately held real estate. Private real estate investments are held by subsidiary and are managed on behalf of the CPP Investment Board by external advisors and managers through co-ownership arrangements.

### **Derivative Contracts**

A derivative is a financial contract, the value of which is derived from the value of underlying assets, indexes, interest rates or currency exchange rates.

The CPP Investment Board uses derivatives primarily to replicate the return of Canada and Non-Canadian equity indexes. As at March 31, 2004, the CPP Investment Board has equity swaps outstanding to exchange money market interest for equity returns. The CPP Investment Board also uses exchange-traded futures contracts to achieve the desired broad market exposure to the equity markets while cash is being held to fund investment activities.

All derivative contracts have a term to maturity of one year or less. Notional amounts of derivative contracts are used to compute the cash flows and for determining the fair value of the contracts.

Notional amounts are not recorded as assets or liabilities on the balance sheet. The notional amounts and fair value of derivative contracts held as at March 31 are as follows:

	2004		2003	
	(in millions of dollars)			
	Notional Amount	Fair Value	Notional Amount	Fair Value
Equity swaps	4,034	9	250	(1)
Equity futures	448	(3)	—	—
Total	4,482	6	250	(1)





Consistent with the investment policies, derivative contracts are fully covered by money market securities. The economic impact on the total asset mix is to increase Canada and Non Canada equities exposure by 12.9% (2003 – 1.4%) and 0.8% (2003 – Nil%), respectively, with a corresponding decrease in money market securities exposure.

### **Securities Lending**

The CPP Investment Board participates in a securities lending program to enhance portfolio returns. Credit risk associated with the securities lending program is mitigated by requiring the borrower to provide daily collateral in the form of readily marketable investments of greater market value than the securities loaned. As at March 31, 2004, the CPP Investment Board's investments include loaned securities with an estimated fair value of \$721 million (2003 – \$Nil). The fair value of collateral received in respect of these loans is \$758 million (2003 – \$Nil).

### **CPP Investment Board's Investment Risks**

The CPP Investment Board limits credit risk by dealing with counterparties that have a minimum credit rating of A or R-1 (short term) as determined by a recognized credit rating agency, where available, or as determined through an internal credit rating process. Credit exposure is limited to maximum amounts approved by the Board of Directors.

The CPP Investment Board is exposed to currency risk through holdings of non-Canadian investments, investment receivables and investment liabilities. Investments are not hedged against changes in foreign exchange rates.

### **Commitments**

The CPP Investment Board has committed to enter into investment transactions, which will be funded over the next several years in accordance with the agreed terms and conditions. As at March 31, 2004, these outstanding commitments total \$3.9 billion (2003 – \$3.9 billion). The organization has made lease commitments of \$21.0 million over the next 10 years.

### **Other Information**

The CPP Investment Board is exempt from Part I tax under paragraph 149 (1) (d) of the *Income Tax Act* (Canada) on the basis that all of the shares of the CPP Investment Board are owned by Her Majesty in right of Canada. The CPP Investment Board's subsidiaries are exempt from Part I tax under paragraph 149 (1) (d.2) of the *Income Tax Act* (Canada) on the basis that all of the shares of the subsidiaries are owned by a corporation whose shares are owned by Her Majesty in right of Canada.

The CPP Investment Board's audited financial statements for the year ended March 31, 2004 are publicly available and provide details concerning the Board's investment policy, its investments and portfolio returns.

## 6. RECEIVABLES FROM BENEFICIARIES

	2004	2003
	(in millions of dollars)	
Balance of pensions and benefits overpayments	81	77
Allowance for doubtful accounts	(45)	(28)
	36	49

Social Development Canada has procedures to detect overpayments. During the year, overpayments totalling \$45 million (2003 – \$45 million) were established and remissions of debts totalling \$4 million (2003 – \$4 million) were granted. A further \$37 million was recovered (2003 – \$37 million).

## 7. CANADA PENSION PLAN ACCOUNT

The CPP Account was established in the accounts of Canada by the CPP Act, to record the contributions, interest, pensions, benefits and administration costs of the Plan. It also records the amounts transferred to or received from the CPP Investment Fund and the CPP Investment Board.

The balance of the CPP Account included the Deposit with Receiver General for Canada and short-term investments, if any. As at March 31, the Deposit with Receiver General for Canada amounts to \$7,483 million (2003 - \$7,093 million).

## 8. CONTRIBUTIONS

Contributions for the year are measured by Canada Customs and Revenue Agency (CCRA) using the assessment of tax returns. In determining the amount of contributions earned for the year, the Agency considers cash received and contributions assessed and makes an estimate for contributions related to tax returns not yet assessed.

Actual results may differ from these estimates. Actual contribution amounts for calendar years 2003 and 2004 will only be known once CCRA has processed all employer's and self-employed workers' declarations of contributions for these years. An adjustment for the difference between actual and estimated contributions will be recorded in the fiscal year in which the adjustment is known.

**9. INVESTMENT INCOME/(LOSS)**

	<b>2004</b>	<b>2003</b>
	(in millions of dollars)	
CPP Investment Fund income:		
Interest on bonds	<b>2,500</b>	2,741
Net unrealized gains	<b>357</b>	193
	<b>2,857</b>	2,934
Interest on deposit with the Receiver General for Canada at a weighted-average annual rate of 2.59% (2003 – 2.64%)	<b>182</b>	169
CPP Investment Board net income/(loss) from operations:		
Net unrealized gains/(losses)	6,050	(3,264)
Fund distributions of capital gains and dividends	–	361
Net realized gains/(losses)	658	(1,533)
Dividend Income	<b>504</b>	288
Other investment income	<b>21</b>	9
Investment and administrative expenses	(24)	(13)
	<b>7,209</b>	(4,152)
	<b>10,248</b>	(1,049)

**10. ADMINISTRATION COSTS**

	<b>2004</b>	<b>2003</b>
	(in millions of dollars)	
Pension and benefit delivery, accommodation and corporate services (Human Resources Development Canada)	<b>309</b>	328
Collection of contributions (Canada Customs and Revenue Agency)	<b>85</b>	80
Cheque issue and computer services (Public Works and Government Services Canada)	<b>15</b>	13
Actuarial services (Office of the Superintendent of Financial Institutions)	<b>1</b>	1
	<b>410</b>	422

Administration costs of the CPP represent the cost of services received from a number of federal government departments and an agency. Those costs are based on estimated allocations of costs and are charged to the CPP in accordance with the memoranda of understanding.

## 11. CONTINGENCIES

At March 31, 2004, there were 4,403 (5,140 in 2003) appeals relating to the payment of CPP pensions and benefits. Claims for these appeals could reach a maximum estimated amount of \$22 million (\$22 million in 2003). Any award made in favour of beneficiaries will be accounted for as an expense of the period in which the amount becomes payable.

A class action has been filed against the CPP for discrimination against survivors whose same-sex common-law partners died on or after April 17, 1985 and before January 1, 1998. On December 19, 2003, the Ontario Superior Court ruled in favour of the class members. The Government has appealed the decision to the Court of Appeal for Ontario. The appeal was heard in Toronto in June 2004. At the time of the preparation of the financial statements, the outcome of the hearing was not known. This contingency is evaluated at an amount between \$71 and \$132 million.

## 12. LEGISLATIVE AMENDMENT

Legislation to amend the Canada Pension Plan and the *Canada Pension Plan Investment Board Act* was passed by Parliament on April 3, 2003, and approved by an Order in Council on March 22, 2004. The amended legislation and a related administrative agreement provide for the transfer of CPP assets currently administered by the federal government to the CPP Investment Board beginning in fiscal year 2005. These assets consist of the bonds held by the CPP Investment Fund and the Deposit with Receiver General for Canada. CPP Investment Board, the departments of Finance and Social Development have signed an agreement outlining the process for the transfer of assets. The bonds held by the CPP Investment Fund will be transferred to CPP Investment Board over a three-year period beginning with the first transfer on May 1st, 2004. The Deposit with Receiver General for Canada will be transferred over a period of twelve months beginning in September 2004.

## 13. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current year's presentation.





**ANNUAL REPORT OF THE**  
Canada Pension Plan ○  
2003-2004