



OFFICE OF THE
PARLIAMENTARY
BUDGET OFFICER
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BUDGET

**Cost Estimate for Bill C-
261: An Act to amend
the Canadian Forces
Superannuation Act
and the Royal Canadian
Mounted Police
Superannuation Act
(increase of allowance
for survivors and
children)**

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The Finance Committee of the House of Commons has directed the PBO to prepare cost estimates of all private member's bills placed on the order of precedence, that have been deemed fiscally material by the PBO.

This cost estimate was prepared by the staff of the Parliamentary Budget Officer. Please contact pbo-dpb@parl.gc.ca for further information.

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1. Background

This private member's Bill amends the *Canadian Forces Superannuation Act* and the *Royal Canadian Mounted Police Superannuation Act* in order to increase the allowance for survivors and children.

Upon the death of a contributing member of the Regular Canadian Forces (CF), certain members of the Reserve Forces, as well as members of the Royal Canadian Mounted Police (RCMP), who at the time of death were entitled to an annuity or an annual allowance, the survivor and children of these contributing members are eligible for an immediate annual allowance.

The purpose of this enactment is to increase the allowance given to the survivors and children of CF or RCMP contributors from 50% to 70% of the contributor's annuity or allowance.

2. Methodology

At the request of the Department of National Defence, the RCMP and the PBO, the Office of the Chief Actuary of Canada (OCA) has undertaken the analysis.

The OCA undertakes regular actuarial reviews of all public service pension plans, including the Canadian Forces- Regular Force pension plan, Canadian Forces - Reserve Force, and the RCMP Pension Plan. These reports provide the government with the state of the various pension accounts and their ability to meet the financial requirements outlined in the various pension acts. As such, the OCA possess all of the details and underlying assumptions necessary to undertake any analysis of changes to the various pension programs.

The actuarial reports identify two financial components of a pension plan: the Actuarial Liability, which is an estimate of the present value of the total amount of funds required to be paid out under the pension acts; and the Current Service Cost, which represents the annual contribution required by members and the government to ensure that the respective pension funds are able to meet their actuarial liability.

In undertaking the analysis, the OCA used the information from the latest actuarial reports, dated March 31 2103.¹ The actuarial liability and current service costs are as at March 31 2015.

Incremental Cost of Raising the survivor benefit to 70%

| Increase in Actuarial Liability at 2015-03-31 (\$Million) | | | |
|--|---------------|---------------|----------|
| | CF Regular | CF Reserve | RCMP |
| Active Members | 1,447.0 | 5.70 | 540.0 |
| Pensioners | 2,342.0 | 1.10 | 536 |
| Current widows(ers) | 1,257.0 | 0.20 | 244 |
| Total | 5,046.0 | 7.00 | 1,320.00 |
| Increase in annual Current Service Cost at 2015-03-31 (\$ millions) | | | |
| | CF Regular | CF Reserve | RCMP |
| Government | 112.55 | 0.91 | 39.00 |
| Members | 0.00 | 0.00 | 0.00 |
| Total | 112.55 | 0.91 | 39.00 |

Source: Office of the Chief Actuary

Active Members denotes the liability attributed to increasing the survivor benefit to that group.

¹ <http://www.osfi-bsif.gc.ca/Eng/oca-bac/ar-ra/cf-fc/Pages/default.aspx>, accessed June 21 2016.

The calculation involves taking the number of active member contributors applying a mortality table against that population to derive an estimate of the survivor benefit payout that would be required.

Pensioners are no longer active members, nor are they contributing to the plan, but they are entitled to the survivor benefit. Current widow(ers) are those who are in receipt of a survivor benefit. The incremental actuarial liability for this group is simply the value of the grossed up payments (from 50% to 70%) of the survivor benefit currently being paid.

One key cost driver is the fact that the survivor benefit is being raised to 70%, which is in excess of the 2/3 lifetime benefit as defined under the *Income Tax Act*.² The reason for this is as follows. In order for a pension plan to be considered 'registered', and thereby exempt from income tax, there are a number of constraints put on the plan.

Paragraphs 8503(2)(d) to (f) of the *Income Tax Regulations* stipulate that the maximum payout for survivor's benefits is 66 ^{2/3} % of the amount of retirement benefits that would have been payable to the member had they been alive. In order for an employer to provide a benefit in excess of this amount, a taxable Retirement Compensation Arrangement (RCA) plan must be set up. A RCA is a plan where:

- the employer or employee makes contributions to a custodian of the RCA trust; and
- the custodian may be required to make distributions to the employee or another person on, after, or in view of the employee's retirement...³

The employer must deduct a 50% refundable tax on any contributions made to the custodian of the RCA. As benefit payments are made from the account, the the tax that was originally deducted is then refunded to the employer.⁴

In the case of the CF and RCMP pension plans, RCA-92 is the plan from which the extra benefits are paid. RCA-92 was initially sized to accommodate a survivor benefit of 50%.

² *Income Tax Act*, s.36 (1) and (2)

³ <http://www.cra-arc.gc.ca/tx/bsnss/tpcs/pyrll/clcltng/spcl/rrngmnt-eng.html>

⁴ http://www.cra-arc.gc.ca/E/pub/tg/t4041/t4041-e.html#P78_4135, accessed June 21 2016.

Because the survivor benefit is now being raised to 70%, significantly more funds will have to be paid from this plan to accommodate the increased benefit. In addition to having to have more funds available in the RCA, the rate of return used to value the cost of the liability is lower because of the 50% refundable tax deduction (there being only 50% of the funds available on which to earn income), thereby increasing the amount of the liability and the servicing cost for that plan.

3. Conclusion

The changes proposed by Bill C-261 will result in an incremental increased pension liability of \$5.046 billion for the regular CF pension plan, \$7 million for the Reserves CF pension plan, and \$1.32 billion for the RCMP pension plan. The annual servicing costs will increase by \$112.55 million for the regular CF pension plan, \$910,000 for the reserves CF pension plan, and \$39 million for the RCMP pension plan.

The total incremental pension liability of \$6.373 billion would be payable by the federal government. The total incremental annual service cost of \$152 million would also be payable by the government. Pension members would not bear any of this increase under the current pension laws.⁵

⁵ The *Public Service Superannuation Act* sets out the contribution rates for the government and pension plan members for all pension plans, including the CF and RCMP plans.