he pooled registered pension plan (PRPP) announced by the federal government last year is the first step in the reforms needed to extend pension coverage to the more than 60% of the Canadian workforce not currently enrolled in a workplace plan. However, as the Ontario government hinted in its recent budget, there are a number of challenges with the PRPP design.

First and foremost is the fact that while employees will be automatically enrolled, with an option to opt out, employer contributions to the PRPP will be entirely voluntary. Employer contributions are a cornerstone of workplace pensions. Not mandating this element in the PRPP architecture undermines its value as a retirement savings tool compared with other options.

Without requiring employer contributions, the attractiveness of the PRPP for employees will be limited to the potential for reduced management fees through asset pooling. Yet how the market will respond to PRPPs in this regard remains uncertain. Although provincial regulators will likely follow Quebec’s lead and require some form of transparency and comparability in PRPP fees, this is not mandated in the federal architecture. Prior experience with similar retirement schemes in other countries (such as Australia) suggests that regulation is required to significantly bring down fees.

A Viable Alternative

A recent study by Tyler Meredith and Robert L. Brown, published by the Institute for Research on Public Policy, puts forward another model that holds the potential to fix many of the difficulties with the PRPP: the pooled target benefit pension plan (PTBPP). The plan would be target benefit in design, ensuring that members have an expected retirement benefit within a variable range based on market performance. Contributions would be based on a set objective for income replacement; a 50% starting point would provide most middle-income earners with retirement security. Employer contributions would be fixed, as in a DC plan, with members bearing the risk of future plan deficiencies.

While the target benefit design would not eliminate the risk that benefits could decrease due to market underperformance, the model would include mechanisms to mitigate this risk, such as an automatic rebalancing mechanism similar to that of the Canada Pension Plan. Actuaries and investment managers, rather than members, would manage the plan.

To ensure that economies of scale are fully realized, PTBPP pools would be required (after a prescribed implementation period) to maintain a minimum asset size of $10 billion, with management expense ratios (MERs) capped at 40 basis points. This cap is consistent with the MER profile of large pension funds with similar scale and pooling.

For many workers and employers, this plan would represent a vast improvement over their present situation. The PTBPP would provide better pension coverage, security in retirement savings and cost efficiency for members than PRPPs or most existing private group or individual plans. Employers would gain cost predictability, while employees would enjoy significantly lower fees and relatively predictable income in retirement.

Getting from the initial design of the PRPP to something more tangible is possible within the current model. With Ontario hesitant to proceed with the PRPP until a more comprehensive framework emerges, the PTBPP should be considered as a practical path for pension co-ordination across the country. It’s time for discussion.