NUPGE Pension Manual, Module 6

How Much Pension Will an Individual Need?

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PUBLIC GOOD

The National Union of Public and General Employees (NUPGE) is a family of 13 Component unions. Taken together, we are one of the largest unions in Canada. Most of our 425,000 members work to deliver public services of every kind to the citizens of their home provinces. We also have a large and growing number of members who work for private businesses.

The office of the National Union of Public and General Employees is on the traditional and unceded territory of the Algonquin peoples and is now home to many diverse First Nations, Inuit, and Métis peoples.

We recognize the crimes that have been committed and the harm that has been done and dedicate ourselves as a union to moving forward in partnership with Indigenous communities in a spirit of reconciliation and striving for justice.

Bert Blundon, President

Jason MacLean, Secretary-Treasurer

Table of Contents

How Much Pension Will an Individual Need?

There is really no generic answer to the question of how much income an individual or couple will need in order to live their retirement years in comfort and dignity. Each individual retiree will spend differently and have different needs. Accordingly, there is no scientific way of determining how much an individual will require.

Retirement Income Above the Poverty Line

One thing that all individuals who are planning for retirement can consider is how their retirement income will compare to 3 of the measures Statistics Canada uses to determine whether the incomes of individuals, families, and households are so low that they may be living in poverty. These are the market basket measure (MBM), Low-income measures (LIMs) and the Low-income cut-offs (LICOs).

The MBM is the official poverty line in Canada. It reflects the costs of basic goods and services for a household of 2 adults and 2 children. Data showing MBM income levels from the Canadian Income Survey is updated annually. And there are different figures for 66 geographic areas to reflect how the cost of living varies, depending on where people live in Canada.

The LIM is set at 50% of median household income. There are different figures for different household sizes, but no provincial/territorial or regional breakdown is provided.

LICO’s are the incomes people need to avoid spending a larger than average share of their incomes on necessities. Unlike the MBM income levels, there are different LICOs, depending on household size. Data showing LICOs both before and after taxes is available for communities and households of different sizes. However, the calculations for the LICOs are based on 1992 spending patterns and don’t account for changes over the last 3 decades.

So, at a minimum, an individual or couple will want to try to ensure their annual retirement income will at least meet the MBM, which corresponds to their geographic area, and the LIM, which corresponds to their family size.

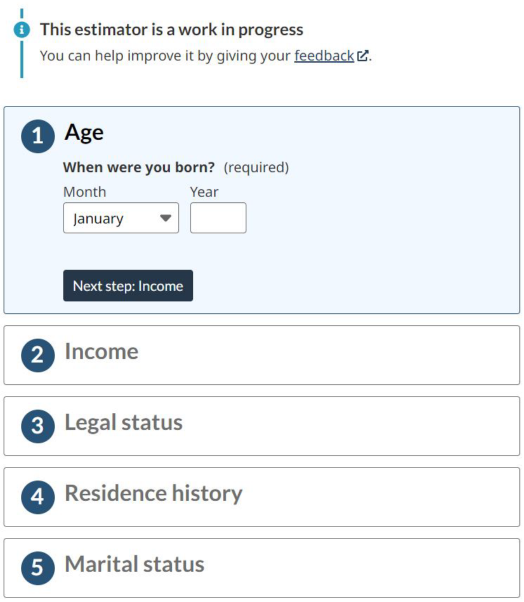
If people’s annual retirement incomes are below the MBM and LIM thresholds, it’s safe to say a large portion of their retirement years will be spent living in poverty.

OAS and GIS Will Not Provide Above-Poverty Income

For those persons whose only retirement income consists of the maximum available benefits under Canada's Old Age Security (OAS) and Guaranteed Income Supplement (GIS), most will live below the poverty line.

The amounts people receive through OAS and GIS will vary depending on the following factors:

- Age
- Net income
- How long they have lived in Canada
- Whether they have a spouse or common-law partner and, if so, how much the spouse or common-law partner earns



The federal government [Old Age Security Benefits Estimator](#) will let people know how much they can expect to receive from OAS and GIS. However, if they have no other retirement income, in most parts of Canada, they will be living in poverty.

That is particularly true if they live in a large city. The single elderly are particularly vulnerable. The difference in living costs for a couple and living costs for an individual is lower than the difference between what a couple will receive from OAS and GIS and what a single person will receive. That means what the single elderly receive is less likely to be enough and they are more likely to be living in poverty. As is commonly the case elsewhere too, most of the single elderly in Canada are women.

Less Income May Be Needed for Retirement

Another point to consider is that experience shows workers generally need less of an income during retirement for a number of reasons:

- There are no more CPP/QPP or Employment Insurance contributions.
- There are no more pension plan contributions.
- There is an increased personal income tax exemption starting at age 65 (clawed back, subject to a means test for those with higher incomes).
- Many personal items, such as mortgage payments, life insurance premiums, clothing for work, transportation to work, and child-related expenses MAY not only be reduced, but may disappear entirely.
- There are benefits that may be available to people over 65, such as low-cost public transportation.

On the other hand, many workers may find themselves "retiring" at an earlier age than they anticipated as a result of corporate or government downsizing. In these circumstances, their savings might be a lot less than they expected. They will also have to rely on their retirement savings a lot longer.

There has also been an increase in both the percentage of senior families with debt and the amount of debt they are carrying.[i] This has been attributed to an increase in mortgage debt due to the rise in housing prices.[ii]

Even if they do retire when they intended to, workers' lifestyles may change at retirement, so that other expenses replace those of working expenses. Retirees may travel more or have more time to pursue hobbies, for example.

A related factor is that, even more than the population as a whole, seniors are affected by cuts to public services and the growing use of user fees. This will increase the cost of living for many seniors in their retirement years.

Where Will This Money Come From?

The usual rule is that your pension income from all sources should be about 70% of your pre-retirement earnings if you want to maintain your standard of living once you're retired.

Until 2019, the Canada Pension Plan (CPP) was intended to replace 25% of average work earnings up to the Yearly Maximum Pensionable Earnings ($57,400 in 2019). In recent years, someone getting the maximum OAS payment would be receiving between 12% and 13% of the YMPE.

That meant that, at best, the combination of CPP and OAS would have replaced about 37% of pre-retirement earnings. And that's at best—CPP benefits will be lower for people with periods of unemployment or precarious employment.

The CPP enhancement that the labour movement successfully fought for will increase the maximum CPP pension by 50% once it is fully in place. As of 2019, improvements to the CPP began to gradually increase the share of work earnings that the CPP replaces. However, the extent to which people will benefit will depend on how many years they have been contributing at the higher rate that took effect with the enhancement.

That means that, in the next few years, for pension income to reach 70% of pre-retirement income, a person needs to receive the equivalent of about a third of their pre-retirement income from other sources.

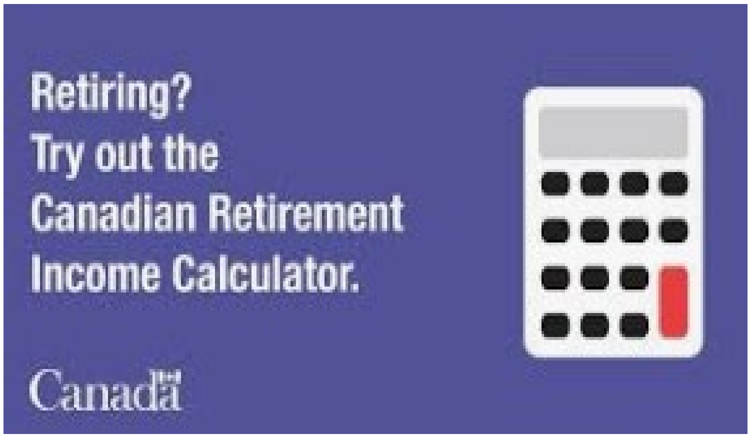
There are really only 2 other sources of income that a retired worker is able to tap from, and that is a workplace pension plan or private savings. And remember that fewer than 30% of workers belong to a workplace pension plan.[iii]

Personal Savings

For those workers who do not belong to a workplace pension plan, they will need to accumulate pre-retirement savings, usually through a Registered Retirement Savings Plan (RRSP) and/or a Tax-Free Savings Account (TFSA).

The federal government of Canada has developed an online Canadian Retirement Income Calculator to help Canadians plan for their retirement. The calculator takes users step by step through an estimate of the ongoing income they may receive throughout their retirement from

- Old Age Security (OAS)
- Canada Pension Plan (CPP), or Quebec Pension Plan (QPP)
- employer pension(s)
- Registered Retirement Savings Plans (RRSPs)
- other sources of ongoing income, including Tax-Free Savings Accounts (TFSAs)



Using the Canadian Retirement Income Calculator will help people figure out how much private retirement savings from their RRSP or other sources they will need to provide a certain income for a set number of years. By adjusting the amount they plan to contribute in the future to RRSPs on the Retirement Savings page, people can figure out how much they would need to be saving for their retirement income to be 70% (or whatever other target they have picked) of their pre-retirement income.

Even if people have a workplace pension plan, the calculator is still useful, particularly if their workplace plan is a defined-contribution plan.

There are several other factors that affect how much people need to put aside.

The question of how long individuals expect to live after retirement is one that is asked in the Canadian Retirement Income Calculator. For a Canadian male aged 65, the average Canadian life expectancy is 85 years of age. For a Canadian female aged 65, the average life expectancy is 87 years of age.[iv] However, the longer they live, the more they will need in retirement savings. This is particularly true if people don't have a defined-benefit pension plan or a target-benefit pension plan, which provides benefits for life.

Other factors that need to be considered when individuals are calculating how much to save are:

1. The annual rate of return that the private retirement savings will generate during years of retirement.
2. The annual inflation rate to ensure that the value of the income they will need each year is protected during each year of retirement.

When using the calculator, it is important that individuals keep in mind that the calculations can only provide a rough estimate of future retirement income. Further, those estimates are expressed in today's dollars and do not consider the amount of taxes an individual will have to pay on their retirement income.

Relying on Personal Savings Is Far More Expensive Than Having a Pension Plan

People who have to rely on personal savings for their retirement income will also **end up paying far more than if they had a workplace pension plan. One study estimated that, for the same retirement income, an individual relying on personal savings would pay almost 4 times what someone with a high-quality defined-benefit pension plan would pay.[v]

There are a number of reasons for this including risk pooling, lower fees, and lower costs.

Financial Literacy

Financial literacy refers to having the knowledge and skills to make decisions about personal finances. People who are financially literate will still need help from financial professionals with various aspects of their finances. But being financially literate means people are better able to make day-to-day decisions, decide which financial professionals to turn to, and evaluate the advice they are given.

The Financial Consumer Agency of Canada has a Financial Toolkit with modules that provide people with the information and tools they need to manage their finances. There are also groups offering courses in financial literacy. But because some finance industry professionals can use that type of course as a sales pitch, check who is offering the course and who is teaching it.

While financial literacy will help people make better decisions with the funds they have, it is important not to have unrealistic expectations. Problems like rising household debt levels are largely the result of the cost of many necessities rising much faster than wages. Financial literacy may help people make the best of a bad situation, but it isn't enough by itself to end the problems.

The Impact of Inflation

It's important to recognize that inflation over the years will impact seniors' income by reducing the income's purchasing power. The table below shows how different rates of inflation impact purchasing power over the years.

The Impact of Inflation on Future Purchasing Power:
The Future Value of One Dollar ($1.00)

Inflation Rate / Number of Years	2%	3%	4%	5%	6%	8%	10%
5 years	91¢	86¢	82¢	78¢	75¢	68¢	62¢
10 years	82¢	74¢	68¢	61¢	56¢	46¢	39¢
15 years	74¢	64¢	56¢	48¢	42¢	32¢	24¢
20 years	67¢	55¢	46¢	38¢	31¢	21¢	15¢
25 years	61¢	48¢	38¢	30¢	23¢	15¢	9¢

Inflation obviously will impose a major burden on pensioners with fixed income; it is often described as "a monster that dines on your future." On a somewhat positive note, however, today's inflation experience is more moderate. Yet, in the past, it has been severe, peaking in 1980 at about 12.5%.

Understanding Credit—How Debt Can Affect Budgets

As household debt rises, more people have been reaching retirement while still carrying debts such as mortgages, loans, lines of credit or credit cards. Retirement with household debt may be a challenge.

When people retire with debt, the costs of interest payments and repaying the principle are added to the costs retirees normally face. At the same time, they are having to make those payments with a reduced income. Rising interest rates can make that even more difficult.

This means that, when planning for retirement, people need to think about whether they will have household debt when they retire and how much those debts will be.

No Easy Solutions

There are 2 general observations and conclusions that can often be made about retirement planning.

1. Individuals generally underestimate how much is required to fund a flow of income after retirement (or for purchasing pensionable service).
2. And conversely, individuals generally overestimate how much a stream of income can be generated from a given amount of dollars.

Recognizing these factors early in an individual's working life is preferable to later in terms of retirement planning. It is also important that we recognize that Canada's public pension system plays a critical role, and that we can expect it to play a critical role in the future given the low pension coverage rates amongst Canadian workers.

Add to this the additional challenges faced by increasing life expectancy, early retirement aspirations of workers, and volatile investment markets.

Notes

[i] Sharanjit Uppal, "Debt and assets among senior Canadian families", Statistics Canada, April 3, 2019, https://www150.statcan.gc.ca/n1/pub/75-006-x/2019001/article/00005-eng.htm.
[ii] Ibid.
[iii] Statistics Canada Tables 98-10-0030-01 and 11-10-0133-01 (2022 figures).
[iv] Statistics Canada Table 13-10-0114-01 (2020 to 2022 figures)
[v] Healthcare of Ontario Pension Plan, *The Value of a Good Pension Plan, How to improve the efficiency of retirement savings in Canada*, 2018, 23, https://hoopp.com/docs/default-source/about-hoopp-library/advocacy/the-value-of-a-good-pension-102018.pdf.

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