GOVERNMENT OF BERMUDA

The Ministry of Finance

Ministry of Finance Headquarters

Ministerial Statement
To the House of Assembly
By
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Minister of Finance

Actuarial Review of Contributory Pension Fund 2017
CPF Pension Increase

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Mr. Speaker, in accordance with section 35 of the Contributory Pensions Act 1970, I am pleased to table the Contributory Pension Fund (CPF or the Fund) Actuarial Report as at August 1st, 2017.

The main purpose of the 2017 Actuarial Review was to consider the implications for future contribution rates of maintaining benefits at their present levels in real terms and to consider the long-term sustainability of the Fund. The review includes projections of contribution income and expenditure (on benefits and administration), projections of the Fund balance (allowing for an assumed rate of investment return), and projections of the number of years' outgo secured by the Fund.

Mr. Speaker, the Contributory Pension scheme plays an important role in Bermuda's pension arrangements, providing a first tier or basic pension to more than 11,400 seniors and other beneficiaries the majority of whom live in Bermuda. The maximum benefit is currently about $1,545.63 per month. Altogether, some 13,298 persons currently receive benefits under the Act. Currently the average pension paid under the CPF is around 28 per cent of the median annual gross earnings for Bermudians as indicated in the "The Bermuda Job Market Employment Brief" produced by the Department of Statistics.

Mr. Speaker, even though the actuarial review is an excellent tool in overall pension management, it is important to recognise that the financial projections for future years are based on reasonable assumptions and they should not be taken as forecasts of the outcome. The projections should be updated at successive actuarial reviews in light of the latest information available.

The main findings of the actuarial review are as follows:

- The Fund earned a nominal rate of return net of investment expenses of 3.5% per annum and a real rate of 1.8% per annum over the three years since the last review (3.1% and 1.4% if investment expenses are excluded). This exceeded the policy index but compares with the real rate of return assumption of 3.5% per annum.

- The net assets of the Fund grew 3.46% over the three years from $1.80 billion to $1.83 billion. This was 8.8% below the projected value from the previous review.
- Contribution income in 2016/2017 ($121.7 million) was 13% higher than in 2013/2014 and benefit expenditure ($155.8 million) increased 16% over the three years since the last review.
- Total expenses for the three years averaged 0.37% of the average Fund, down from 0.52% over the previous 3 years. Pure administrative expenses averaged 0.15% of the average Fund over the 3 years and were 0.14% of the average Fund at the Review Date. As a percentage of contribution income, total expenses have been relatively stable over the last 10 years at 7.0%.
- Since the last review, the number of contributors remained relatively constant, from 34,806 in the year ending 31 July 2014 to 34,890 in the year ending 31 July 2017.
- Both the benefit and contribution rates increased during the inter-review period by 5% and 7.5% respectively effective August 2016.
- Based on the population projection figures, the old-age support ratio has declined since the last review. The ratio was 3.9 in 2014 and is 3.6 in 2017. The ratio is projected to decline to 1.6 over the next 50 years. The comparative ratio using the actual contributors and beneficiaries of the Fund declined from 3.0 in 2014 to 2.7 in 2017.

- The Asset / Expenditure ratio is a static measure of the size of the Fund to annual expenditure or the number of years cover provided by the Fund based on the current annual expenditure. This ratio decreased over the three years from 12.6 years to 11.5 years. Compared with 14 other regional social security schemes in a 2013 study, Bermuda's ratio is better than 9 of these countries (average 7.5 years). By comparison, the ratio for the Canada Pension Plan in 2017 was 6.56 years.
- The Fund is projected to increase gradually until 2023 then decline steadily until it is exhausted in 2047 under the best estimate scenario. This is 2 years earlier when compared to the previous review.

Mr. Speaker, Honourable Members are advised that the financial performance of the Fund over the three years was below expectations due to lower than expected investment returns and contribution income. This was offset by lower than expected administrative and investment expenses and benefit payments.

The viability of the Fund in the short to medium term is good with the Fund being able to cover at least 11 years of the current expenditure and being positive for the next 29 years. However, recognising the long-term demographic challenges of the Fund the Ministry will continue to closely monitor the performance of the Fund.

Mr. Speaker, it should also be noted that the funding policy for the Fund is not based on full actuarial funding but based on sustainable

funding. That is, contributions plus investment income should cover benefits and administration expenses on an annual basis while the fund builds up sufficient reserves to cover several years of benefits and expenses to withstand future adverse circumstances.

Mr. Speaker, Honourable Members should note that in order to improve the projected financial position of the Fund in the long-term, the Report has laid out various alternative scenarios that will be considered by the Ministry in seeking to preserve the long-term financial viability of the Fund.

Honourable Members are advised that the finalization of the 2017 Actuary Report was delayed due to problems in extracting data for the Report. In addition some of the data requests from the actuary had changed compared to prior years resulting in further delays in the data extraction.

Mr. Speaker, recent pronouncements about a change in the CPF contribution structure from a fixed-rate structure to one based on a percentage of income have not been included in this report. The Ministry considered it prudent to have an update on the current financial position of the Fund before any material changes were made to the design of the Fund noting that the last review was done as at 1st August, 2014.

The actuaries have started modelling the effect of changing the CPF from a flat-rate contribution to one based on a percentage of income, but more work has to be done on this proposal.

Mr. Speaker, the CPF was established in 1970 and thus has a rather simplistic design. Since the CPF was established there have not been any meaningful reforms to the Plan, even after the mandatory National Pension Scheme (Occupational Pensions) Act was introduced.

Accordingly, the Ministry is of the view that any reform of the CPF should take a holistic view of pensions for the various categories of workers to reduce coverage gaps, excessive amounts and/or anomalies. With the CPF as the first pillar of retirement income, reformed CPF benefits together with other pensions could provide for progressive benefits and a contribution formula at levels that can lead to the sustainability of the CPF in the long-term. Meanwhile it is important that Government review the 2017 Actuary Report and take the required actions to enhance sustainability of the Fund.

Mr. Speaker, the Ministry of Finance propose to engage the Government's actuary of record, and any other service provider required, to conduct a comprehensive review of all pensions in Bermuda. It is anticipated that this engagement will be completed by the end of 2020 and will be shared with the Honourable House.

Honourable Members are advised that the next actuary review of the Contributory Pension Fund is scheduled for the period ending July 31, 2020.

Mr. Speaker, despite the encouraging short to medium term outlook on the Fund, what is clearly evident from this latest review is that Bermuda, like most of the developed world, is faced with the challenges associated with the growth of an ageing population. During the next fifty years the number of people over pension age (65) are expected to increase from 10,484 to 17,665 an increase of 7,181 or 68%. This increase in our seniors will obviously place a greater strain on the country's pension system.

Honourable Members should note that in order to improve the projected financial position of the Fund in the long term the Ministry will carefully consider alternate scenarios included in the report.

Mr. Speaker, in closing I wish to assure members, and more importantly, current and future pensioners that the Government is sensitive to the challenges facing pension plans of this nature and will endeavor to take the appropriate steps to enhance the benefits paid from the Scheme as well as ensure the Fund has the ongoing ability to pay for such benefits.

Thank you Mr. Speaker.