

7 Steps Toward Better CPP/QPP Claiming Decisions

Shifting the paradigm on how we help Canadians

Step #1:

(Re)Introducing the Retirement Income System: A New Framework Tailored to the Retiree's Perspective

STEP
1



National Institute on Ageing



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Paper Series Background: 7 Steps Toward Better CPP/QPP Claiming Decisions



Paper Series Overview:

Shifting the Paradigm on How We Help Canadians.



Introduction:

Opportunities and Obstacles to Shifting the Paradigm.



Step #1.

Educate the public about the Canadian retirement income system.



Step #2.

Help retirees understand the advantages of secure pension income.



Step #3.

Improve mainstream practices, perspectives and narratives.



Step #4.

Explain the mechanics of delaying CPP/QPP benefits.



Step #5.

Help Canadians overcome the systemic cognitive biases and motivational barriers associated with this decision.



Step #6.

Develop new approaches to better communicate the financial advantages of delaying claiming CPP/QPP benefits.



Step #7.

Offer additional insights and actions for policymakers, employers and industry professionals.

When to claim benefits from the Canada Pension Plan (CPP) — or its Quebec counterpart, the Quebec Pension Plan (QPP) — is one of the most important retirement financial decisions Canadians will make.

By waiting until age 70 to claim these benefits, Canadians can receive more than double (2.2 times) the monthly pension than if they had claimed them at age 60. These higher payments last for life and are indexed to inflation. That's why, for people who can afford to wait without hurting their lifestyle – either by drawing on personal savings or by working longer – choosing to wait is a safe and inexpensive strategy to increase their lifelong income.

Yet, although most people can afford to wait, an overwhelming majority (9 in 10) choose to take their CPP/QPP benefits by age 65, reducing the lifetime income security they say they want and will most likely need.

This paper series aims to shift the paradigm toward more informed decision-making. Its purpose is simple: to propose new ways that those in a position of influence – such as human resource leaders, policymakers and the financial services industry – could help Canadians understand and benefit from the value of delaying CPP/QPP benefits.

The solutions are aimed at retirees for whom delaying CPP/QPP benefits is in their best financial self-interest, but it also supports choosing not to delay CPP/QPP benefits where circumstances warrant it.

In either case, improving the clarity of the decision and helping people understand their choices – and the consequences of those choices over the short and long term – will lead to more informed and confident decisions, peace of mind and, ideally, better retirement outcomes for all.

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Paper in Brief

As discussed in the first paper in this series, workers are used to focusing on their account balances as they prepare for retirement, making it difficult to switch gears and contemplate drawing down those balances to sustain their lifelong spending needs.

This mindset leads them to undervalue financial strategies that protect their financial well-being long after they retire — including choosing an optimal balance between their lifelong monthly income flows (to finance ongoing routine expenses) and accumulated savings (to finance any non-routine expenses that arise). The decision on when to start Canada Pension Plan/Quebec Pension Plan (CPP/QPP) benefits is just one of the choices impacted by this mindset. Others include deferring Old Age Security (OAS) benefits, purchasing an annuity and electing lump sum commuted value settlements from defined benefit (DB) pension plans.

Retirement income adequacy means sustaining living standards in retirement. From this perspective, the focus of retirement planning communication tools should be on retirees' capacity to achieve this goal with the financial resources available.

Canada's retirement income system has traditionally been presented to the public as three pillars, consisting of government-

sponsored retirement income programs (CPP/QPP, OAS and GIS), workplace pension plans and personal savings. However, this traditional framing is a missed opportunity to help workers mentally transition into retirement, encouraging them to shift their attention toward the adequacy of their financial resources to successfully and sustainably finance their entire retirement.

How do we encourage workers approaching retirement to turn their focus from accumulating savings to making the most of those savings during the decumulation phase? How can we shift their attention away from their short-term saving balances toward long-term spending? How do we help people understand the financial risks and consequences of the choices they make now to protect their future selves throughout a potentially long retirement?

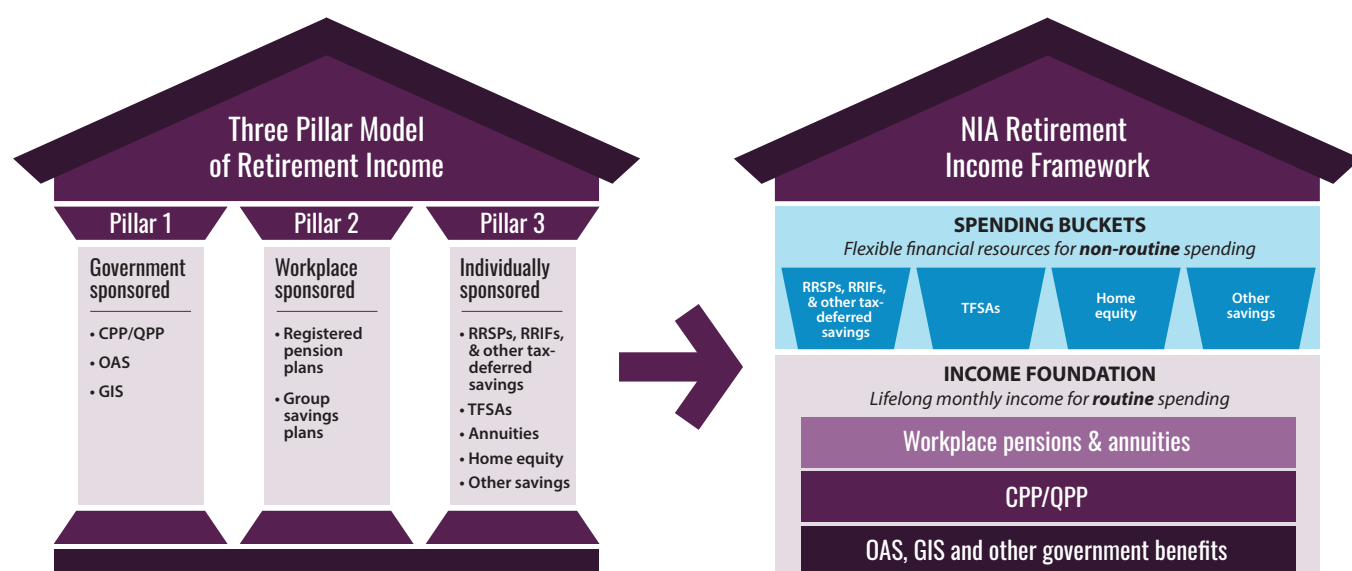
How information is framed strongly influences people's choices, and humans have a propensity to take mental shortcuts when encountering decision-making complexity. For individuals transitioning into retirement, therefore, the presentation of the retirement income system must be intentionally designed as a visual roadmap that reduces the decision-maker's effort while improving the match between their personal preferences and their choices. In addition to enhancing the speed and quality of decision-making, the framework should nudge their focus away from a savings mindset (accumulation) to a spending one (decumulation).

The irony is, the traditional “three pillar” framework of the retirement income system comes from the perspective of providers (i.e., government, employers and the financial services industry), not those it is intended to inform. When viewed from the end user’s perspective, pensions are not a financial pillar of the retirement income system. They are the income foundation on which other financial resources rest.

NIA’s Retirement Income Framework to Better Support Retiring Canadians

From an accumulation (saving) perspective

... to a decumulation (spending) perspective



When we view pensions as a foundation rather than a pillar, the resulting framework provides a structure that is more focused on spending, with an “income” foundation that securely and sustainably replaces employment income. Private assets accumulated on an individual or collective basis — including tax-deferred savings such as registered retirement savings plans (RRSPs), registered retirement income funds (RRIFFs), and defined contribution (DC)

pension plans — are “spending buckets” on top of this foundation, providing flexibility to support non-routine spending throughout different retirement stages.

The visual distinction between the lifelong monthly income and the spending buckets contrasts their different uses and risk profiles, clearly demarcating the type of financing suited to cover routine versus non-routine expenses. Retiring Canadians will want to

ensure their monthly retirement income (from CPP/QPP, OAS, GIS, workplace defined benefit (DB) pension plans and annuities) is sufficient to securely cover routine expenses that last for life — such as food, utilities and other ongoing costs — enabling them to safely maintain their living standards into older age regardless of the ups and downs of the economy, inflation and financial markets. After ongoing spending needs have been addressed, there is more flexibility to focus on non-routine spending, such expensive repairs and luxuries.

When a retirement income system offers choices, those choices and their consequences must be clear and understandable to the decision-maker. This paper proposes that the retirement financial services industry “boost” the competencies of individual Canadians transitioning into retirement by adopting the NIA’s new retirement income framework, which emphasizes the character and associated risks of programs and products as they relate to retirement spending. This reframing provides context to explain the system from the retiree’s perspective, fostering an enhanced understanding of how to balance post-retirement finances.

A personalized visual aid of the retirement income system can help an individual or a couple better understand their financial circumstances as they relate to retirement consumption, illuminating the gaps and giving them the insights necessary to take action. This simple tool could — and should — be tailored to individual Canadians by filling in the appropriate relative amounts with personalized data. To achieve the framing impact, the explanation accompanying the visualization will need to be intentional. Recommendations on supporting a helpful narrative are explored in forthcoming papers of this series.

The goal is to provide a streamlined public-facing representation of the Canadian retirement income system that emphasizes retirement income adequacy and security. To keep the framing simple and intuitive, it does not include a comprehensive enumeration of retirement income and consumption categories, nor does it depict the risk profile of each component. It also does not replace personalized retirement income projections that show how different components will evolve over a lifetime.

Characteristics of the New Framework	How It Helps Canadians Transitioning to Retirement
Focused on the retiree’s perspective (spending) rather than that of providers.	Helps individuals and couples contemplate, understand, prepare and manage post-retirement finances in line with their consumption needs and preferences.
Clearly distinguishes between lifelong monthly retirement income and other financial assets.	Catalyst to discuss the trade-offs (opportunities and risks) between a secure, ongoing allowance for routine spending and flexible financial resources for non-routine spending.
Shows how pensions are the foundation on which the other financial resources rest.	Highlights the benefits of deferring claiming benefits to generate higher lifelong monthly pension income.

While financial advisors are best positioned to focus on tailoring this visualization to the individual, other influencers — including employers, federal and provincial governments, professional organizations, financial institutions and other agencies — would benefit from supporting this move

toward a more productive framing of the Canadian retirement income system. Having these key stakeholders adapt the new framework will be important to advance the ultimate objective: helping workers transition to a decumulation mindset and make better retirement planning decisions.

“As humans we have a remarkable capacity to sacrifice for the future, and an equally remarkable capacity to shortchange it, leaving our future selves to pay the price.”

Bethany Burum, 2014, p.iii.



Background: The Importance of Information Framing for Better Retirement Decisions

When attempting to make complex computational decisions, people need to collect, compartmentalize and weigh information (Payne et al., 1993). Just like a library organizes books by sections, the mind creates categories to organize information, evaluate options and make decisions. When it comes to retirement, the challenge (as discussed in the first paper in this series) is that workers have long been encouraged to take an accumulation mindset as they focus on growing their account balances in preparation for retirement, making it difficult to switch mental gears to the decumulation mindset when transitioning into retirement.

In the **accumulation (savings)** mindset, growing net worth through saving and investing is key, and a later retirement date is an effective strategy to mitigate financial risk. In contrast, the **decumulation (spending)** mindset is focused on drawing down balances to optimally fund living standards over the long term. Although investment returns remain important and returning to the workforce could mitigate financial shortfalls in the early stages of decumulation, the risks of inflation, declining health, declining ability to manage investments and an indefinite time horizon become increasingly challenging in the later retirement stages.

Brown et al. (2017) explained that “the ubiquitous framing of retirement planning in terms of wealth accumulation has conditioned individuals to ignore the insurance aspects of annuities (or pension income) and view them through an investment lens” (p. 453).¹

Evaluating retirement financial planning success from an accumulation mindset leads a worker approaching retirement to analyze profitability without taking into account long-term income security and peace of mind (see Box A). This causes them to undervalue financial strategies and opportunities that would protect their financial well-being long after they retire, such as choosing an optimal balance between their lifelong monthly income flows (to finance their ongoing routine expenses) and their accumulated savings (to finance any non-routine expenses that may arise). This mindset impacts the decision to start or delay CPP/QPP benefits, as well as choices such as deferring OAS, purchasing an annuity, electing lump sum commuted value settlements from DB pension plans instead of lifetime income, and choosing when to start their benefits and other options within a workplace pension plan.

¹ See also Brown et al. (2008).

Shifting the Mindset

How do we help workers change this mindset?
How can we encourage them to ask themselves key questions like:

- Do I have enough retirement income to fund my lifestyle?
- What are the adverse financial consequences if the assumptions (investment returns, inflation, longevity, homecare needs, etc.) don't work out according to plan?
- What options do I have to create a better, more secure retirement for me and my family?

One solution is to improve the framing of mainstream retirement financial planning communications, so that they help people shift their mindset from accumulation (saving) to decumulation (spending).

Beginning with Tversky and Kahneman (1973), the critical importance of **framing decisions** is well-known and accepted in behavioural economics. "Put simply, experimental findings suggest that choices are not based solely on material consequences, but instead are filtered through the particular frame that individuals use to interpret the choices" (Brown et al., 2008, p. 304). Box A discusses the critical role of framing in shaping decisions as it relates to retirement financial planning.

Another fundamental tenet of behavioural economists is that humans use **mental shortcuts** (heuristics) to reach adequate, though often imperfect, answers to difficult questions (Simon, 1955). Deliberately tapping into these heuristics and simplifying the information will help improve the effectiveness of decision-making by reducing the effort required to align choices with personal preferences (Payne et al., 1993; Shah & Oppenheimer, 2008).

To encourage a mindset shift and enhance

decision-making competencies, Grüne-Yanoff & Hertwig (2017) suggested going beyond general education to "target the individual's skills and knowledge, the available set of decision tools, or the environment in which decisions are made" (p. 152) — a concept they described as a "boost" intervention.

Boost interventions: "Rather than merely presenting pertinent and accurate information (as educative nudges do), boosts explicitly seek to foster existing decision-making competencies and to develop new ones, thus enabling individuals to translate their intentions (preferences) into behaviour — that is, to exercise personal agency" (Hertwig, 2017, p. 146).

The next section of this paper proposes a boost that builds on the mainstream approach to educating the Canadian public regarding the Canadian retirement income system, adjusting the framing to make it simple, clear and informative through the lens of Canadian retirees. The aim is to design a visual tool that provides a mental shortcut to improve the speed and accuracy of decision-making while nudging the focus away from short-term financial outcomes. The visual tool also adopts a consumption framing, which can help a person to move away from an accumulation mindset to a decumulation one. This framing shifts their attention toward long-term financial planning where the risk-mitigating properties of greater pension (or annuity) income are more apparent and better valued (see Box A).

Box A: Changing Decumulation Framing from “What are my investment returns?” to “How much can I spend?”

When making financial planning decisions, research finds retirees tend to focus on short-term risk and return rather than on lifelong consumption (Brown et al., 2008). In other words, **individuals view their retirement savings as an investment rather than a source of income to sustain their retirement.**

From this perspective, the prospect of using savings to purchase greater pension income — such as through delaying CPP/QPP benefits or buying an annuity — is risky and unappealing, since there is a positive probability, however small, of losing money in the short term (by dying). Through this lens, there is little value in delaying CPP/QPP benefits and augmenting its secure monthly income in the hope that having a higher pension income stream will pay off at some point in the distant future.

For this reason, Brown et al. (2008) found educating retirees using a “consumption frame” (i.e., evaluating a financial strategy based on the end result of what can be spent over time) helps make annuitized or pension income more attractive relative to the more standard financial planning practice of presenting alternative strategies using an “investment frame” (i.e., focusing on a financial strategy’s return and risk features). They found the preference for lifelong pension income (e.g., annuities) versus holding money in a savings account increased from 20% to approximately 70% of the population when moving from an investment to a consumption frame. The research concludes that its “(s)urvey evidence is consistent with our hypothesis that framing matters: the vast majority of individuals prefer an annuity over alternative products when presented in a consumption frame, whereas the majority of individuals prefer non-annuitized products when presented in an investment frame...This finding provokes the immediate question: if framing matters, why don't annuity providers use the consumption frame?” (p. 308).

(Re)Introducing the Retirement Income System²

The Traditional View

Like that of other countries, Canada's retirement income system has traditionally been presented as "three pillars" in which government-sponsored retirement income programs (CPP/QPP, OAS and GIS) are the first pillar, workplace pension plans are the second and personal savings are the third.

Governments and public policy experts similarly present the retirement income system as three pillars — except, from their perspective, the first pillar is old age income social support programs (OAS and GIS), the second is social security (CPP/QPP benefits) and the third is private sector supplementary saving.³ Quebec generally takes a similar approach, except it does so in layers (see Box B).

The traditional "three pillar" representation emphasizes diversification and strength, in that each pillar is managed by a different party and is subject to different risks. These variations reflect how the different methods of financing retirement are viewed by the pension industry. For example, from the government's perspective, each pillar shows how the Canadian system is financed as a fiscal expense: OAS/GIS is financed on a pay-as-you-go basis from general revenue, CPP/QPP is partially funded outside the public accounts, and employer-based plans and private savings are fully funded outside of government.

The irony is that this traditional presentation of the retirement income system comes from the perspective of providers (i.e., employers, the financial services industry and policymakers), not the public it is intended to inform. It emphasizes how funds are accumulated from a provider's funding perspective, rather how they are decumulated.

To help individual Canadians to navigate the system, it's essential to present it to them in a way that explains the role of each component from *their* perspective. Financial planning can be overwhelming, due to its long-time horizon and risks, so people tend to choose the path of least resistance.⁴ Given this well-documented human propensity to take mental shortcuts when encountering complex decisions, the framework should be intentionally designed as a visual roadmap to retirement spending that reduces the decision-maker's cognitive efforts while enhancing alignment with their personal preferences and self-interest. A more meaningful visualization can empower individuals to make informed, thoughtful decisions by highlighting the strengths and weaknesses of their retirement income sources relative to their personal needs and circumstances.

² Many insights in this paper on how to best measure retirement income adequacy were adopted from MacDonald et al. (2016), which carried out an extensive literature review on the topic, including an exploration of the treatment of savings post-retirement and the various sources of consumption that are conventionally not addressed. Please see that paper for a deeper background on this topic, including methodological weaknesses and examples of the varied approaches taken in literature.

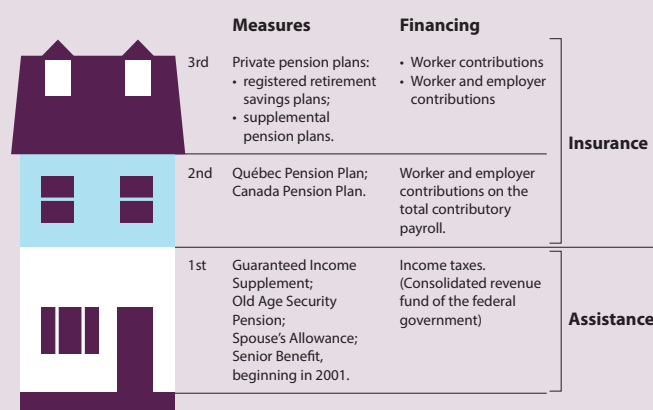
³ See, for example, Blackshaw and Cahill (2020).

⁴ See Gandhi and Yik (2019) for a review of supporting literature.

Box B: Quebec's Layers

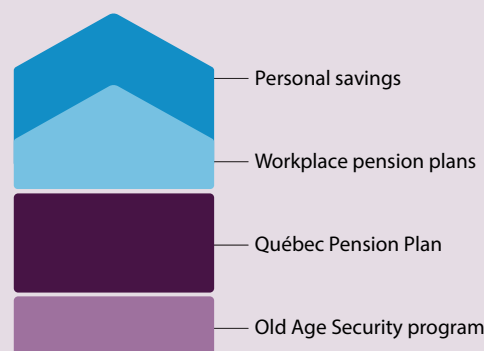
While the traditional representation of Canada's retirement income system uses pillars, Quebec has more often presented the system as layers — as far back as 1996.

1996



Gouvernement du Québec (1996, p.2)

2024



Retraite Québec (2024, p.13)

A New Framework

Retirement income sources vary in their ability to provide consistent and secure spending to sustain retirement expenses.⁵ A meaningful framework should help Canadians preparing for retirement to cut through the confusing features and gain clarity on what the system can do to finance their lifestyle safely and sustainably for the rest of their life.

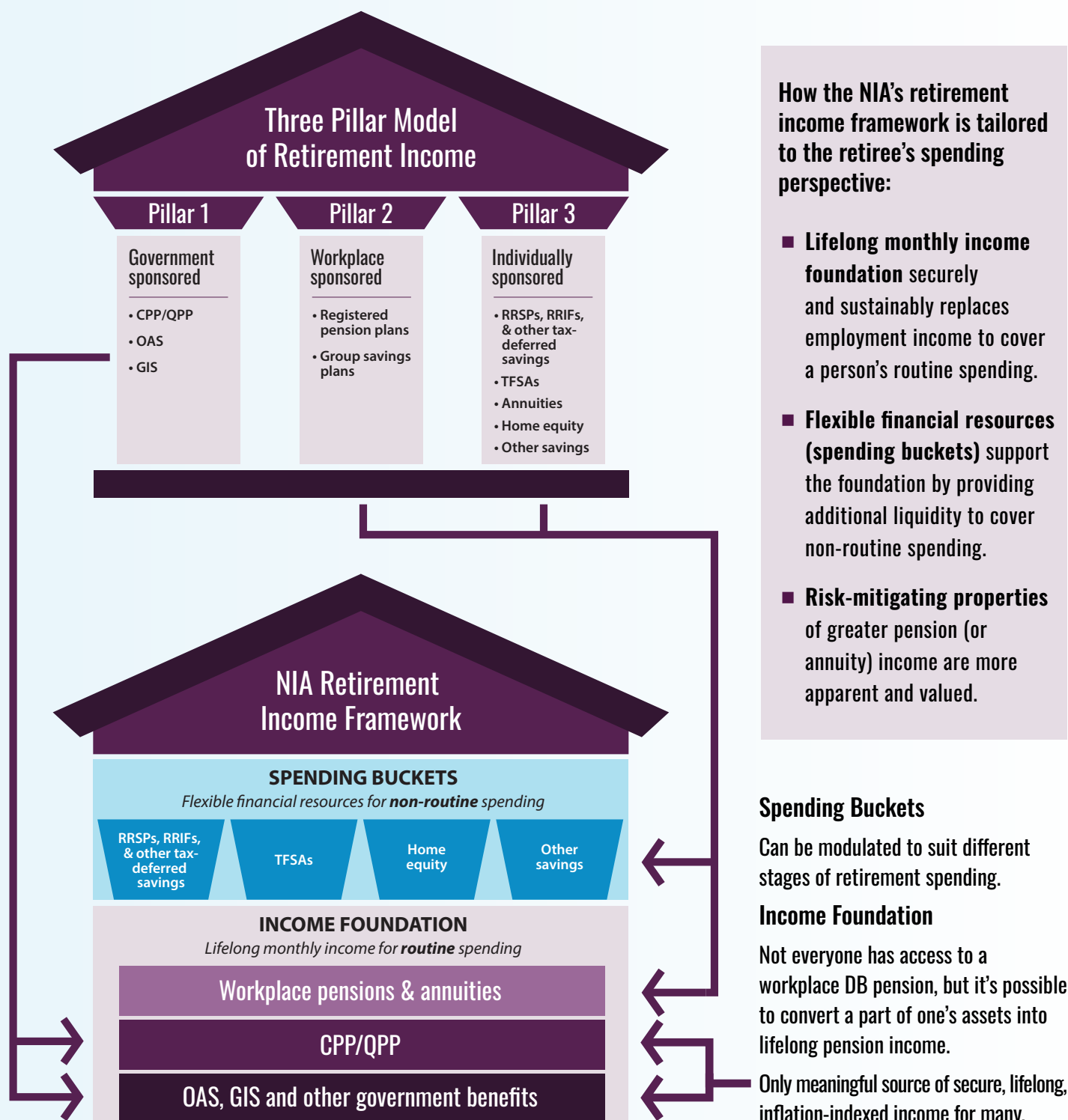
Communication tools relating to the retirement income system should reflect the goal of having sufficient ongoing income to sustain a person's living standards in retirement. These tools should highlight a retiree's ability to cover routine and non-routine expenses, focusing on income amounts and the risks that directly impact capacity to finance consumption needs, rather than on net worth.

When it comes to retirement financial planning, the Canadian retirement income system's framing should emphasize the role that each component plays in supporting the ultimate goal: retirement income adequacy and security. Through this lens, **pensions are not a pillar; they are the foundation on which the pillars rest** (see Figure 1 for an illustration).

By flipping the first two pillars on their side, the resulting framework represents a structure in which an "income" foundation enables retirement by securely and sustainably replacing employment income to cover ongoing, routine expenses. The flexible financial resources rest as spending buckets on top of this foundation, providing liquidity and flexibility to finance non-routine expenses. This new framework makes the risk-mitigating properties of greater pension income more apparent.

⁵ For example, savings in an RRSP are very different from lifelong monthly payments from a workplace DB pension plan — even if the two have the same lump sum value. From a wealth management standpoint, success is gauged by the capacity to increase an individual's net worth over time, rather than on ensuring secure and sustainable retirement spending.

Figure 1: A Redefined Visual of the Canadian Retirement Income System



Key Definitions:

- *The Canadian government retirement income system consists of the universal OAS program, the income-tested GIS and the earnings-based contributory social security plan, the CPP/QPP.*
- *Workplace pension plans, RRSPs and registered retirement income funds (RRIFs) are tax-deferred, meaning that contributions are tax-deductible and investment returns are tax-exempt, while the funds that are withdrawn are included as income for tax purposes and taken into account in determining eligibility for income-tested benefits and credits.*
- *Tax-free savings accounts (TFSAs) are tax-sheltered but not tax-deferred — contributions are not deductible, but investment income earned and funds withdrawn are not considered taxable income (for purposes of income tax and income-tested benefits and credits).*

In this redefined visual, the bottom two layers are retirement income sources that last for life, while the spending buckets on top are variable, flexible financial resources. More specifically:

1 The first two foundation layers are government-sponsored retirement income from CPP/QPP and OAS/GIS benefits. This is the most important source of retirement income for Canada's older population — in fact, for 70% of Canadians ages 65 and older, it makes up more than half of their income.⁶ It creates a solid base for all Canadians by providing a secure monthly income stream that keeps up with

inflation and lasts for life, regardless of the vagaries of the financial markets.

2 The top layer includes DB pension income and other forms of private lifelong monthly income, such as retail annuities, longevity-pooled investments and dynamic pensions (MacDonald et al., 2020). These sources are relatively uncommon, covering a minority of retirees. Annuitized income is minuscule, as discussed in the introduction paper in this series (MacDonald, 2024), and only approximately one in four paid workers participate in a DB pension plan, mostly in the public sector (Statistics Canada, 2023). The weakness in this top layer has come into increasing focus over the past decade, including the potential market opportunity for stakeholders who can help address it by expanding access to workplace pension plans that offer lifelong retirement income or by providing new pension-like programs and vehicles.⁷

3 The spending buckets resting on the foundational layers consist of personal savings as a potential source of retirement income. These buckets include RRSPs, TFSAs and home equity (i.e., housing value minus mortgage debt). They are expressed in terms of net worth (assets minus liabilities). "Other savings" include non-registered investments (e.g., stocks and bonds), real estate assets (other than a principal residence) and business equity (such as farms and professional practices).

⁶ Special tabulations by Richard Maaranen (Open Policy Ontario) based on Statistics Canada, Canadian Income Survey 2020 microdata. Income sources are defined by share of total individual income (before tax): employment earnings, private retirement pensions, RRSP/RRIF withdrawals, investment and other market income, OAS, GIS, CPP/QPP and other government transfers. Excludes persons with negative self-employment earnings.

⁷ See, for example, Deloitte (2023) and MacDonald et al. (2021).

Much more wealth exists in the spending buckets than in the top layer of private pension and annuity income, and the diversity of these holdings is high. For example, in 2019:

- 59% of Canadian households entering retirement (ages 60-69) had TFSA balances of less than \$5,000, and only 13% had balances of more than \$50,000.
- 27% had no home equity, while nearly 32% held more than quarter of a million dollars of equity in their primary residence.
- 38% had a zero balance in their RRSP account, while just 11% had more than \$250,000.⁸

Since the focus is on retirement income, the framing of the top spending buckets should lead the user to understand that these flexible financial resources do not ensure stable lifelong income. Instead, they represent what could be *potentially* consumed in retirement, subject to the availability of those funds when the funds are needed. Box C discusses the methodological challenges arising from these dynamics when it comes to making assumptions on wealth drawdown in retirement.

Box C: Drawing Down Wealth: Unsolved Methodological Mysteries

1 Why not just assume annuitization?

Rather than use spending buckets, an alternative simplified approach is to convert the spending buckets (sources of net wealth) into lifelong income flows by assuming the wealth is annuitized at retirement. By envisioning inflation-indexed annuities, the notional income from the wealth can be forced to be on par with retirement income flows that are mostly inflation-adjusted (i.e., CPP/QPP, OAS, GIS and some workplace pension benefits), facilitating a straightforward comparison among disparate sources of income.

Yet however tempting this approach may be, it is unrealistic.⁹ As discussed in the first paper in this series, voluntary annuitization is extremely rare, and inflation-indexed annuitization is nearly non-existent. Making this unrealistic assumption glosses over the financial risks to income security that retirees face by holding onto their savings: inflation rate uncertainty, investment risk and longevity risk. On the flip side, forcing net worth into an annuity assumption hides the value of accessible savings.

⁸ Special tabulations by He Chen. Source: Survey of Financial Security, 2019, Statistics Canada. See also HOOPP's recent survey, Abacus Data (2023).

⁹ See MacDonald et al. (2016) for examples of previous literature and its treatment of notional annuitization for financial assets.

2 Should home equity be treated as a flexible financial resource (spending bucket) or a foundational layer of lifetime income?

The treatment of home equity as a flexible financial resource is controversial.¹⁰ Although it is often a retiree's largest asset, evidence suggests retirees do not generally view it as a source of consumption after retirement. Rather, they regard it as contingency savings to be used in the event of large and unforeseeable expenses — particularly major life transitions, such as the death of a spouse or the need for long-term institutional care.¹¹

Survey data finds that, when asked, the vast majority of older Canadians say they plan to age at home independently for as long as possible (NIA & Telus, 2020). This desire to “age in place” is substantiated by empirical evidence: real estate activity data shows that “a large proportion of senior households (especially younger ones) are deciding to age in their home rather than put it on the market” (CMHC, 2023, p. 18).

As well as wanting to age in place, people don't generally regard their home as a flexible financial resource. In the 2023 NIA Ageing in Canada Survey, interest in financial instruments that tap into home equity were unpopular. Even among homeowners ages 50 and above who had expressed a desire to age in place for as long as possible, eight out of 10 reported they would be “not very” or “not at all” likely to tap into their home equity to finance their consumption in retirement.¹² Empirical data confirms this preference. Baldwin (2022) found the uptake of financial instruments that draw on home equity is rare in Canada, for example, with reverse mortgages making up approximately 1% of retirement income (Baldwin, 2022).

Overall, older people are unlikely to move or draw down home equity as a flexible financial resource to support their consumption after retirement. This behaviour is driven by a clear preference to age in place independently for as long as possible without acquiring any new debt on the home asset. For these reasons, some argue home equity is a special case, and an assessment of the retirement income system should not assume retirees sell their homes or otherwise deplete their home equity. However, excluding what is, for most Canadians, their single largest net asset distorts important disparities in the financial security between homeowners and renters, as well as among homeowners with very different amounts of home equity.

Given that home equity is not regarded (or treated) as an asset to finance retirement spending, the question becomes, How can we better capture the role home equity plays in the retirement income system from the perspective of retirees?

One approach not traditionally considered outside of the field of economics is to remove home equity as a spending bucket and instead treat it as a layer of theoretical lifelong income.

¹⁰ See MacDonald et al. (2016) for a discussion of the varied approaches adopted by the literature for housing equity as it relates to retirement income adequacy.

¹¹ For earlier literature, see Venti and Wise (2001, 2004).

¹² The NIA survey asked homeowners who indicated that they wanted to live in their homes as long as possible: “Looking ahead as you age, how likely would you be to consider securing the money you need by using some of the equity in your home to obtain a new or increased mortgage, a housing line of credit, or what is called a “reverse mortgage”?”. From among the 90% who chose an answer (10% responded “cannot say”), 4% reported “very likely”, 12% “somewhat likely”, 32% “not very likely” and 50% “not at all likely”.

This is accomplished by estimating the monthly value that a homeowner receives by virtue of the fact that they do not need to pay for shelter. This implicit income on owner-occupied housing, often measured as a percentage of its net equity, is known as “imputed rent”.

This approach is arguably appropriate, since it captures the reality that homeowners enjoy reduced shelter expenditures in retirement, recognizes the substantial investment that Canadians make in their homes and the value of this accumulated asset at retirement,¹³ and respects the widespread desire of retirees to age in place.

Considering these arguments, representing home equity through imputed rent is potentially a useful approach in the generic view of the retirement income system for retiring Canadians. However, financial planners may want to treat home equity differently based on the attitudes of their clients, particularly when doing a cash-flow projection of income and expenses.¹⁴ As previously noted, this visual is not a replacement for personalized financial planning but is intended to act as a springboard for deeper conversations.

3 How can we account for preferences and varying needs among people and over time in the drawdown of financial savings?

From an analytical perspective, there is substantial ambiguity in how decumulation of personal financial savings is treated, driven by data availability.¹⁵ Even with perfect population-wide data, however, there is substantial heterogeneity in decumulation behaviour based on needs and preferences, both of which vary among households and over time. This diversity makes it problematic to develop a single representation of converting financial savings buckets into flows of post-retirement spending. Attempting to represent this heterogeneous pathway in a generic way would result in a framework that represents nobody.

What the new framework does, however, is provide a catalyst for personalized financial planning, where the challenges of financial diversity and heterogeneous behaviour and preferences can be largely overcome. In personalized financial planning, the necessary information — including unique financial circumstances and preferences (e.g., past behaviours and intentions with respect to decumulation) — can be obtained directly from the individual. This information can be used to develop tailored financial planning visuals that anticipate how a person’s financial circumstances, including the risks, evolve over time. These visuals are a more powerful way to capture a person’s attention and help them explore the consequence of alternative decisions. Adding a time dimension can illustrate the effect of those decisions into the future, but only if the associated financial risks are incorporated and clearly communicated.

¹³ A Statistics Canada report estimated that adding the implicit income generated by home equity to traditional estimates of retirement income created a 12% to 15% increase for those ages 70 and above (Brown et al., 2010).

¹⁴ In a conventional cashflow analysis for a homeowner, for example, financial planners would compare actual income flows to actual associated homeowner expenses required to age in place, such as utilities, property taxes, insurance and maintenance costs or condo fees.

¹⁵ Analysts who are interested in retirement income adequacy at a population level — including policy-makers, pension plan sponsors and the financial services industry — have conventionally been restricted to those sources of income found in traditional income tax or administrative data, which adequately captures some sources but not others. Two notable blind spots are the drawdown of non-registered assets (including withdrawals from non-tax-sheltered savings) and home equity (since imputed rent, mortgage payments or consumption are not visible in traditional income data).

The demarcation between the spending buckets and the lifelong monthly income is intended to be a visual representation of the differences in opportunities and risks between lifelong monthly income and flexible financial resources. For example, while the emphasis of this paper series is to shift greater attention to the struggles of insufficient lifelong financial security, this demarcation could also help inform the decision-making of an individual transitioning to retirement with a DB pension that is more than sufficient to finance their lifestyle but with modest RRSP savings. In this situation, the individual's financial interests might be better served by the liquidity and flexibility of holding onto savings and forfeiting opportunities for converting them into lifelong income.¹⁶

Note that the proposed visualization of the retirement income system is intended to provide a superior alternative representation of the available sources of money to maintain a person's standard of living after retirement: the lifelong income and accessible wealth available to support consumption of goods and services. It does not, by any means, capture a comprehensive definition of retirement income and consumption sources. An additional caveat is that while the goal is to provide a streamlined, public-facing representation of the Canadian retirement income system that emphasizes retirement income adequacy and security, it is not intended to characterize the entire risk profile of each component. For example, pensions are broadly put into a single category under "workplace pensions and annuities", even

though Canadian pension plans can include a wide range of risk-sharing features (see Chandler (2020a) for discussion).¹⁷

In addition to signalling the fundamental differences in risk profiles, the demarcation between the lifelong monthly income layers and the spending buckets is intended to draw attention to routine versus non-routine spending needs. Retiring Canadians will want to ensure their secure lifelong monthly income from CPP/QPP, GIS/OAS, workplace pension plans and annuities is sufficient to cover routine expenses that last for life — such as food, shelter, routine health care, travel and other ongoing costs — enabling them to safely maintain their living standards into older age. After routine spending needs have been addressed, there is more flexibility to focus on non-routine expenses, including major purchases, health-related care, charitable donations and bequests.

Painting a Personalized Picture

The redefined Canadian retirement income system could — and should — be tailored to individual Canadians. For example, Figure 2 shows the structure by presenting median income and net asset values for a typical Canadian retiree with at least \$5,000 in retirement savings (older persons ages 70 to 79 with a minimum of \$5,000 in combined savings across TFSAs, RRIFs and RRSPs). There are no workplace pensions or other private lifelong monthly income in this personalized visualization because a typical Canadian household does not have these resources.

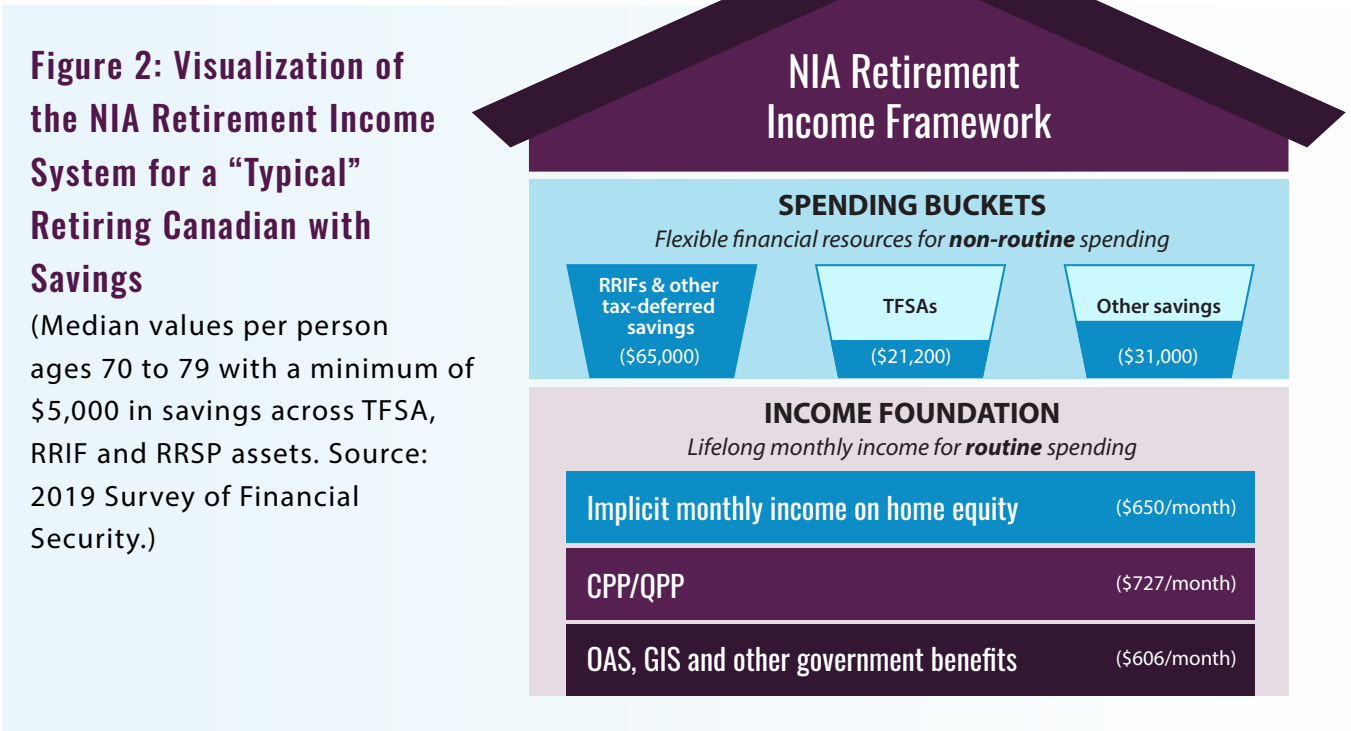
¹⁶ For example, having accessible savings is particularly attractive to retirees who, without steady employment income, may have difficulty securing loans from banks and other lenders when and if the need arises.

¹⁷ Reverse mortgages, annuities and most private sector DB pensions do not provide inflation protection. And, to some degree, annuities and pensions depend on the financial success (or non-failure) of the plan sponsor. The risks are different from those of unfunded government plans (e.g., the risk of benefit cuts for OAS/GIS).

Figure 2 reflects the “return” by drawing to scale the income value for each source. To make a relative comparison of size, it was necessary to convert the accumulated savings into a flow of monthly income by assuming a 4% fixed inflation-indexed withdrawal rate of net savings (other than primary housing).¹⁸

As already discussed, given that retiring Canadians want to “age in place” (see Box C), the typical Canadian is assumed not to draw down their home equity to finance consumption. Therefore, the implicit return on home equity contributes to the retirement income system as a flow of secure hypothetical income, reflecting the rent that homeowners would otherwise pay out of their retirement income if they did not own their home.¹⁹

This reframing clearly demonstrates the relative importance of government-sponsored retirement income programs for older Canadians. As discussed in the first paper in this series, the 2023 NIA Ageing in Canada survey found that nine out of 10 recipients say their CPP/QPP pension is an important source of their retirement income, with six out of 10 saying it’s essential and they can’t live without it (MacDonald, 2024). The dependence of older Canadians on government-sponsored retirement income programs — which is likely to be even greater going forward — reinforces the importance of getting the claiming decision right (ibid).



¹⁸ Known as the 4% Rule, this withdrawal rate has been traditionally a popular recommended self-managed strategy for people who intend to use savings as a source of retirement income in such a way that they do not run out of money. Its origins lie in Bengen (1994), which argues that funds are likely not to run out under a 4% inflation-indexed fixed withdrawal strategy. The validity of this approach continues to be debated by academics and industry (see, for example, the recent Berger and Curry article (2023)). Its use in a simple visualization should not be considered an endorsement of this rule for financial planning.

¹⁹ The 2019 SFS reported a median home equity value of \$226,000 per person in the sample population (ages 70 to 79 with a minimum of \$5,000 in savings across TFSA, RRIF, and RRSP assets). The net implicit return is assumed to be 3.45% of home equity per year, generating an implicit income of \$650 per month (Brown et al., 2010). Source: Median statistics were obtained through special tabulations by Richard Shillington; 2019 Survey of Financial Security (SFS). SFS data is at the household level. To represent the figures at the individual level, per capita income is assigned for couples (for example, if the savings of one spouse is \$100,000 and the other \$0, then each spouse would be assumed to have \$50,000).

While Figure 2 demonstrates the structure for a typical Canadian, this framework could be tailored to individual Canadians by filling in the appropriate relative amounts with personalized data. This would normally be done at a household level, recognizing that people sharing a dwelling pool their resources and benefit from economies of scale relative to living alone. Personalized visualizations will better reflect varying personal situations: for example, government-sponsored retirement income programs play a bigger role for low-income individuals, while higher-income individuals are more likely to have access to workplace pension plans. Also, with rising housing costs and preferences among younger generations, fewer people may have home equity in the future.

Personalized visualizations will give individuals a stronger basis to explore the consequences of different decisions. It helps them understand their financial circumstances as they relate to retirement consumption, illuminating the gaps and providing the insights necessary to take action. For example,

it could give them the insight of knowing they have sufficient income to cover ongoing expenses and the confidence to take their CPP/QPP benefits early without compromising living standards. Or, if retiring Canadians find their secure lifelong monthly retirement income is insufficient, they will be motivated to use their savings to purchase additional pension income to fill the gap — that is, sacrificing a portion of the spending bucket to purchase additional layers, such as delaying CPP/QPP benefits. These personalized financial projections can incorporate unique components that are time-dependent and highly individualized, such as post-retirement paid employment (see Box D).

Armed with a more meaningful alternative to the conventional “three pillars” visualization, experts in a position of influence can help facilitate more informed post-retirement financial planning. Those experts will be the intermediaries who bring the new framework to retiring individuals as part of their financial planning.

Box D: To Include or Not to Include Post-Retirement Paid Employment?

In a framework that attempts to represent the entirety of retirement spending, it's necessary to make decisions on which financial resources to include and how to include them. One resource not included on conceptual grounds is employment earnings. The main reason is that the purpose of a retirement income system is to have the capacity to replace working-life living standards after the end of paid employment. Although there is a clear trend of later-life employment, most people can work for only a finite period (owing to factors such as involuntary loss of employment, the need to care for an ailing spouse, or poor health), after which they will need to rely on the retirement income system without the assumption of continued paid employment.

Individuals looking, however, at their own personal retirement plan can personalize their visualization and include post-retirement employment earnings as an ongoing or temporary source of income in retirement. Including post-retirement employment in an individual's personalized visualization provides a significant lever to balance the shortfalls between

consumption needs and available income flows, particularly in early retirement. Delayed retirement or scaled-back employment are powerful adaptive strategies to better finance retirement while maintaining health and social engagement. The end of a full-time career and eligibility for a workplace-based pension also does not preclude other unrelated paid pursuits. Some may choose to give up a high-pressure office job to take on a less intense form of paid employment, perhaps working part-time. Farmers, small business owners and professionals who work in partnerships tend to stay involved in their enterprises after they stop actively working.

A More Comprehensive View of Retirement Income

There are many sources of retirement consumption that are not included in the conventional representation of the retirement income system. Especially when it comes to personal financial planning, it is valuable to include all sources of consumption (including drains on assets) to make the picture more accurate. Here are some examples.

1 **Investment and income taxes** –

Potential sources of income are dramatically affected by its tax treatment. For example, RRSP and TFSA savings are not on par in terms of income available to fund consumption, given that withdrawals from the former are treated as taxable income while the latter are exempt. Tax treatment varies by income amount and source, as well as personal circumstances (such as location and eligibility for tax deductions and credits). Planning is best done on a case-by-case basis by representing the personalized retirement income system on an after-tax basis.

2 **Debt payments** – While debt balances are captured in net non-registered savings and home equity, future debt

payments are not captured in this typical representation. They are negative income and could be incorporated as such.

3 **Other financial transfers** – These include privately held health and life insurance, social assistance benefits, provincial supplements and cash transfers received from other households and institutions (e.g., alimony, support from relatives, bequests, etc.).

4 **Non-financial transfers** – Households also have non-financial resources to support retirement consumption, such as the following:

- **Income in-kind** – This encompasses goods and services produced by households for their own consumption, such as housekeeping, child-rearing and cooking, which lower the expense of maintaining living standards. Given their additional leisure time, this can be a relevant consideration for retirees (Brzozowski & Lu, 2010).
- **Other imputed rent** – In addition to housing, this is the value of the flow of services from durable goods purchased while working but consumed after retirement (e.g., the rental price an individual would otherwise have to pay for a cottage they already own).

- **Social transfers in-kind** – These are services such as:
 - Community support systems (e.g., meals on wheels and community groups/activities);
 - Family support (such as unpaid caregiving by adult children);²⁰ and
 - Government and social structures, including provincial programs and subsidies — particularly health care (doctors, hospitals and long-term care services) and support programs for older adults.²¹

An individual's retirement income visualization can be tailored in a variety of ways to include these components, depending on available data, intentions and preferences. They (or their advisor) could include post-retirement employment earnings to account for any work they plan to do in retirement, as well as home equity if they plan to sell their home. They can also include other anticipated income sources, such as large financial gifts.

Conversely, the visualization can incorporate specific intentions like desired bequests by highlighting the intended allocation of net worth within one of the flexible spending buckets. Non-financial transfers are more difficult to incorporate on the income side of a person's financial plan, although understanding and discussing these resources can provide important insight into a person's capacity to meet their evolving expenses as they move from employment into retirement and then into advanced age. This becomes particularly relevant if they are contemplating relocating to a municipality or country with different levels of government services, or if current levels of government services are unlikely to be maintained.

²⁰ As discussed in the first paper of this series, adult children have traditionally played a central role in supporting the care needs of the older population, although this will be increasingly difficult going forward owing to the reduction in fertility since the 1960s (MacDonald et al., 2019).

²¹ See Chandler (2020b) for additional discussion on these less often discussed components of retirement economic security.

Conclusion

“The objective of boosts is to improve people’s competence to make their own choices; the focus is on interventions that make it easier for people to exercise their own agency.”

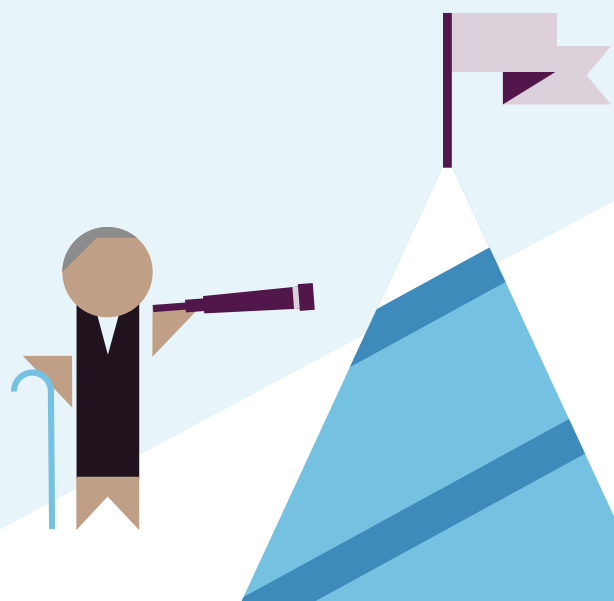
(Hertwig, 2017, p. 144).

The traditional “three pillar” framework of retirement income system undervalues opportunities to improve long-term financial well-being and caters to the perspective of the employers and governments who fund the programs, rather than the individuals who need guidance to navigate the system. This paper proposes that the industry “boost” the competencies of individual Canadians transitioning to retirement by moving from the traditional framework to a new retirement income system visualization that highlights a lifelong retirement income foundation (the layers) and flexible financial resources (the spending buckets).

Reframing the messaging will explain the system from the individual’s perspective, fostering a clearer understanding of how best to prepare and manage post-retirement finances. The visual demarcation between lifelong monthly income and flexible financial resources can also be used as a catalyst to discuss the financial trade-offs when making decisions, particularly when contemplating routine versus non-routine spending. Deciding whether to delay claiming CPP/QPP benefits to generate higher lifelong monthly retirement income in place of short-term accessible wealth is just one of the choices that will benefit from this reframing.

A variety of stakeholders could take advantage of this more productive framing. While financial advisors are in the best position, given the focus on customizing the message to the individual, other sources of influence – including employers, federal and provincial governments, professional organizations, financial institutions and other agencies – could also support the transition. Evaluating and adapting the new framework will be important to advance the ultimate objective: helping workers transition to a decumulation mindset at retirement.

Looking beyond the conventional retirement income system components to a framework that illustrates the intersection of retirement finances and social supports can encourage individuals transitioning into retirement to contemplate how their retirement will unfold and the role of each piece in supporting that future, including how one component substitutes for another (e.g., private pay for the potential lack of family support). With this in mind, financial advisors should consider incorporating more of these other components of economic security that are critical for ageing Canadians. This, in turn, will foster more thoughtful and comprehensive long-term retirement financial planning and decision-making, ultimately resulting in better outcomes for Canadian retirees.



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