AS 1021 Introduction to Financial Security Systems
Winter 2020

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Office Hours: MWF 10:00-11:30 AM, 12:00-1:00 PM, WSC 107

Words of advice

- A lot of material is covered in this course and you are strongly advised to:
  - Attend lectures on a regular basis to help you understand material
  - Review lecture notes on a regular basis – This trains your mind to be better at studying which makes studying for tests and exams easier
  - Ask questions – Good science is good questions… so ask them – in class, by email, by forum on OWL
  - Draw connections between the concepts taught – they are all related
  - Contact me if you have any questions or are having any difficulty with the course material or tests/exams – That's what I'm here for
- Many students in the past have waited until it is too late to do these things – DO NOT be one of those students
- In addition to my office hours, there is a Help Centre in the Dept. of Statistical and Actuarial Sciences with graduate students who are able to help with most questions related to course material

Course Readings:

"Morneau Shepell Handbook of Canadian Pension and Benefit Plans, 16th Edition", Abridged Edition

Various articles posted on OWL website

Modules:

Module 1: Financial Security and Insecurity (Articles on OWL)

Module 2: Old Age (Chapters 1, 2, 3, 9, 14; Articles on OWL)

Module 3: Poor Health – Medical Needs (Chapters 17, 20)

Module 4: Poor Health – Disability (Chapters 18, 21; Articles on OWL)

Module 5: Premature Death (Chapter 23; Articles on OWL)

Module 6: Other Topics (time permitting)

Course web page: www.owl.uwo.ca

- Slides – lecture notes will be posted before each lecture
- Course Outline and Announcements

Evaluation:

- Participation: 7.5%
- Report: 10%
- Midterm: 32.5%
- Final Exam: 50%

Calculators:

- Although this is not a mathematical course, you may need a calculator in class or for the test and exam, therefore it is recommended that you always bring your calculator!

Participation:

May include written reflection and other activities

Report:

Written report due by end of term (date TBA)

Midterm Test:

February 26, 2020, 6:00-8:00 pm

Final Exam:

TBA in April 2020

Please refer to the course outline for what to do if you miss a test or exam due to illness or a conflict with another course

Today's Objectives

- To introduce the concept of **financial/economic security**

Introduction to Financial Security Systems

- People often seek protection against events that threaten their financial security; these events include:
  - Job loss
  - Illness or injury / disability
  - Premature death
  - Old age

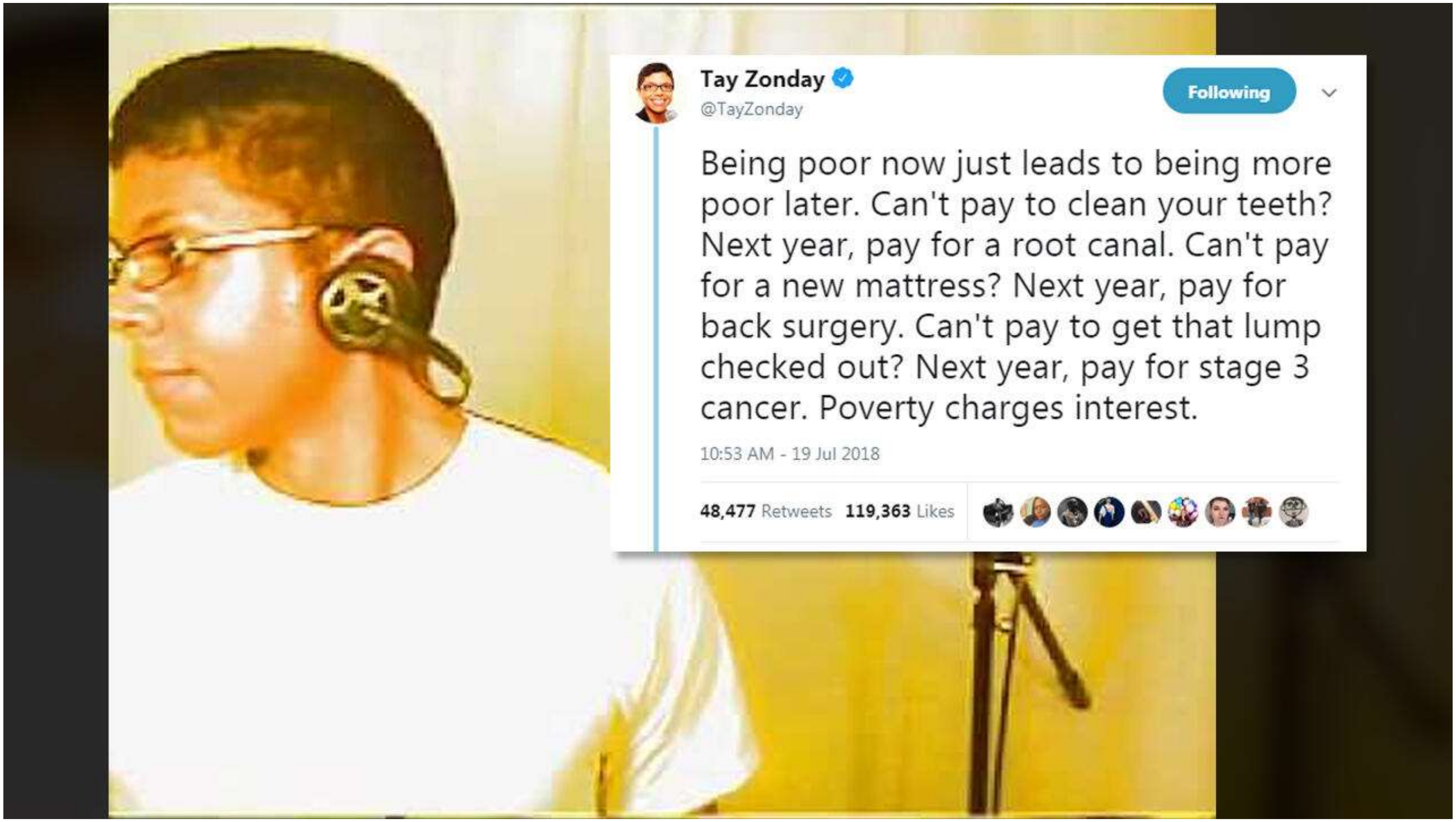
- There are various programs and products that are available to help reduce financial insecurity; sources include:
  - Individual
  - Employer
  - Government

Introduction to Financial Security Systems

- This course will give you some insight into financial security and insecurity and the differences between social / governmental programs and private programs, both on the individual and employer level

- We will discuss programs and products such as:
  - Retirement savings plans
  - Employer pension plans
  - Government social security programs
  - Long-term care insurance
  - Health insurance plans
  - Disability insurance

Poverty Charges Interest



Today's Objectives

- To introduce the concepts of **financial/economic security** and **financial/economic insecurity**

- To discuss sources and causes of economic insecurity

The Nature of Economic Security:

- What is **economic security**?
  - It is part of a person's total welfare
  - It is a "*state of mind or a sense of well being by which a person is relatively certain that he/she can satisfy basic needs and wants, both present and future*"
- A sense of economic well-being is dependent on the use of economic goods and services
  - An individual must have access to sufficient goods and services to attain economic security
  - For this to happen, an individual must have income

- The more income a person has, the greater the level of economic security

- Income comes in several forms - **what are they?**
  - Wages
  - Savings
  - Public or private transfer payments
  - Ownership of property

Some Key Points:

1. The receipt of income must be continuous
   – A person must have a reasonable expectation that income will continue into the future

2. **Real income** must also be considered
   – This is the amount of goods and services that can be purchased with income
   – This can be affected by increases in income and inflation and regional differences in cost of living

Some Key Points (continued):

3. The receipt of income must be at a level above the poverty or subsistence level of living
   – **Poverty** can be defined as having insufficient material goods/services so that a person's basic needs exceed their means to satisfy them

4. Economic security is *relative* to the standard of living enjoyed by others
   – As the standard of living (including educational level, cultural background, and rate and stage of economic growth and development) changes over time, the concept of economic security will also change

The Nature of Economic Insecurity:

- **Economic insecurity** is the opposite of economic security
  - It occurs when a person is unable to achieve a sense of well being due to a fear that present and future needs will not be satisfied

- **Examples of sources of economic insecurity?**
  1. Loss of income
  2. Additional expenses
  3. Insufficient income
  4. Uncertainty of income

Economic insecurity consists of one or more of the following:

1. Loss of income
   - Due to loss of job (or other payments); either permanent or temporary
   - Due to erosion of real income over time
   - Unless a person has sufficient financial assets, past savings, or other sources of replacement income, they soon will be unable to satisfy basic needs/wants

Economic insecurity (continued):

2. Additional expenses
   - Such as medical bills due to being injured or having a serious accident or illness
   - These events can also lead to a loss of income if a person is unable to work
   - Other examples of additional expenses?

Economic insecurity (continued):

3. Insufficient income
   - Occurs when a person earns a total income that is less than the amount needed to satisfy basic needs/wants
   - Can occur even if person is steadily employed and regularly works throughout entire year

Economic insecurity (continued):

4. Uncertainty of income
   - Occurs when a person who is currently employed, is uncertain of the future continuation of present income
   - Could lose job due to downsizing, mergers, change in financial condition of economy, loss of public funding

Note:

- A retired person may have the certainty of a monthly pension cheque of say $1,500
  - That in itself does not assure economic security if the income is insufficient

Causes of Economic Insecurity:

- Major causes of economic insecurity include:
  1. Premature death of the family head
  2. Old age
  3. Poor health
  4. Unemployment
  5. Substandard wage
  6. Inflation
  7. Natural disasters
  8. Children born outside of marriage
  9. Personal factors

1. Premature Death of the Family Head

- We know that everyone will die
  - Insecurity is caused when the death is to a person with unfulfilled financial obligations – **such as**?
    - Dependents to support
    - Mortgages or other debt to repay
  - Future income is lost
  - Additional expenses may be incurred due to funeral costs, medical bills, estate and death taxes

- **What is meant by pre-mature death *in the context of economic security*?**

2. Old Age

- When an older person retires, there is a loss of income (no more work earnings)
  - Unless the person has carefully saved for their retirement, economic insecurity could occur
  - Many older people incur sizable medical expenses
  - Others may require long-term custodial care in nursing homes (which is expensive and not necessarily covered by provincial medical plans)
  - Seniors on a <u>fixed</u> monthly pension, will ultimately reach economic insecurity due to inflation

Today's Objectives

- To discuss causes of economic insecurity
- To introduce the concepts of **social security** and **social insurance programs**
- To discuss categories of social security programs
- To discuss characteristics of social insurance programs

Recall that:

- **Economic insecurity** is the opposite of economic security
  - It occurs when a person is unable to achieve a sense of well being due to a fear that present and future needs will not be satisfied

- Sources of economic insecurity are:
  1. Loss of income
  2. Additional expenses
  3. Insufficient income
  4. Uncertainty of income

Also recall that:

- Major causes of economic insecurity include:
  1. Premature death of the family head
  2. Old age
  3. Poor health
  4. Unemployment
  5. Substandard wage
  6. Inflation
  7. Natural disasters
  8. Children born outside of marriage
  9. Personal factors

3. Poor Health

- Due to medical reasons
  - Insecurity is caused by additional expenses not covered by provincial health plans (drugs for example)
  - **% of U.S. Population with no health insurance at all?**

    16%
  - **U.S. versus Canada?**

- Due to a disability
  - If they cannot work, a person suffers a loss of income
  - May be able to return to work part time or at a different job ⇒ could lead to insufficient income

4. Unemployment

- Loss of job means loss of income and uncertainty of future income
  - May have to take a part time job to support family $\Rightarrow$ could lead to insufficient income
  - Some groups of people may find it difficult to find a new job - **examples??**

5. Substandard Wage

- This is defined to be a wage that is below some specified minimum necessary for a person to support themselves or their families
  - Insecurity will be caused if this continues over an extended period of time

- **What are substandard wages versus insufficient income?**

6. Inflation

- Can cause insecurity if prices rise faster than money income
  - Occurs if there are no increase in wages/income above inflation
  - Occurs to retirees on fixed income pensions

7. Natural Disasters

- Floods, hurricanes, earthquakes, tornadoes, forest fires, etc.
  - Causes loss of life (e.g. working partner) and there could be property damage

8. Children Born Outside of Marriage

- Mothers may have limited work skills
- Child support payments, if any, may be insufficient

9. Personal Factors

- Personal attributes
- Divorce
- Alcohol and drug addiction
- Gambling
- Domestic violence
- Personal bankruptcy

Social Security:

- To help address economic insecurity, governments in all developed countries have created social security programs in response to a perceived need by society for certain types of measures/programs for which neither individuals nor private insurers can (or will) provide adequate coverage

- **Social security** refers to programs established by law that insure individuals against the loss or interruption of their earned income, and for certain expenditures arising from marriage, birth, or death and also includes family allowances

Social Security (continued):

- **Income-maintenance programs** provide money to at least partially replace income of individuals and families that have lost income as a result of:
  - Death, disability, and old age
  - Work-related injuries
  - Unemployment
  - Sickness and maternity

- **Benefits in kind** provide direct services for hospitalization, medical care, and rehabilitation

Social Security (continued):

- Income-maintenance programs can be classified into three broad categories:
  1. Employment-related programs
  2. Universal programs
  3. Means-tested programs

1. Employment-Related Programs

- Eligibility for pensions and other periodic cash payments are generally based on the length of employment and self-employment
- For work-related injuries and family allowances, eligibility is established based on an employment relationship

- Benefits are based on the worker's eligible earnings and are usually financed by contributions from eligible employees, employers, or both

- **Examples in Canada?**

2. Universal Programs

- Provides a flat cash benefit or tax break to individuals without regard to recipient's income, employment or wealth
  - Most countries also provide a second tier of benefits that are based on the worker's earned income

- Financed by government general revenues and paid to individuals who meet a minimum residency period requirement
  - In some countries benefits are partly financed by contributions from workers and employers

- **Examples in Canada?**

3. Means-Tested Programs

- Eligibility for benefits is determined by measuring the individual's or family's financial resources against some standard measure of need, which is typically based on a subsistence level of income
  - Applicants must meet a means test (aka needs test) and show that their income and financial resources are below thestandard of need established for the program

- Typically financed out of general revenues of government

- **Examples in Canada?**

Social Insurance:

- **Social insurance** programs are part of the overall structure of social security
  - Insurance can be considered a pooling of risks
  - Social insurance is *"a device for the pooling of risks by their transfer to an organization, usually governmental, that is required by law to provide cash or service benefits to or on behalf of covered persons upon the occurrence of certain specified losses"*

Characteristics of Social Insurance:

1. Primarily financed by contributions from employers, employees, or both
   – Contributions are usually kept in special funds administered by the government and the benefits are paid from these funds

2. The right to benefits is usually tied to the recipient's past contributions or coverage under the program
   – The size of the benefit and contributions usually varies according person's prior earnings

Characteristics of Social Insurance:

3. Participation and coverage is compulsory by law for certain categories of workers and employers

4. Eligibility for benefits and size of benefits are prescribed by law

5. There is a long-term plan in place for financing the current/future benefits

6. The plan is not established by the gov't solely for its employees