



August 25, 2010

Ms. Louise Levonian
Assistant Deputy Minister – Tax Policy
Finance Canada
140 O'Connor Street
Ottawa, ON K1A 0G5
Tel: (613) 992-1630/797-0421
By e-mail to louise.levonian@fin.gc.ca

Dear Ms. Levonian:

Re: Tax and Retirement Savings Innovations to Promote Retirement Income

I attach a copy of our pre-budget submission to the House of Commons Standing Committee on Finance, which focuses on pension and retirement-related issues in the context of consultations across Canada by the federal, provincial and territorial governments.

In particular, in the 2011 budget, we hope to see the announcement of:

- greater equivalency between those in pension plans with those in group or individual registered retirement savings plans (RRSPs);
- greater fairness between those in permanent jobs with employer-sponsored plans and those with alternative work arrangements or patterns; and
- greater equity between the tax treatment of equivalent financial instruments and, in particular, a commitment in the fall economic statement to review the tax treatment of financial services under the *Excise Tax Act*.

Many of the specific measures identified require or would benefit from inter-jurisdictional collaboration. It was encouraging, therefore, to see the sense of co-operation that emerged from the June 13 and 14, 2010 Finance Ministers meeting in Charlottetown.

As many of our recommendations have a tax policy implication, I thought this submission would be of interest you. Don't hesitate to get in touch with me directly or Barb Amsden, Director – Strategy and Research at bamsden@ific.ca (416 309-2323) if you have questions on anything in the submission.

Yours sincerely,

Cc: Jeremy Rudin, ADM – Financial Sector Policy
Brian Ernewein, General Director, Tax Policy Branch



August 13, 2010

Mr. James Rajotte and
Members, Standing Committee on Finance
c/o M. Jean-François Pagé, Clerk of the Committee
131 Queen Street, 6th Floor
House of Commons
Ottawa ON K1A 0A6
E-mail: fina@parl.gc.ca

Dear Mr. Rajotte and Members:

Re: Pre-Budget Submission of the Investment Funds Institute of Canada

The Investment Funds Institute of Canada (IFIC)¹ welcomes the opportunity to provide recommendations for the pre-2011-budget review by the House of Commons Standing Committee on Finance. Our attached submission sets out ways to promote more retirement savings through taxation and other innovative retirement savings measures, while helping reduce complexity, uncertainty and compliance costs.

IFIC members include mutual fund management companies, fund distributors and organizations that provide services to the industry. The mutual fund industry currently manages \$648 billion of client assets – approaching 30% of Canadians' financial wealth. It provides services to 12 million investors nationwide through 300,000 advisors and other fund company and distributor staff. Our industry also delivers on government policy initiatives by promoting the use of tax-assisted savings plans.

Because of our members' integral role in Canada's retirement income system, we reviewed Report 4, *Retirement Income Security of Canadians*. It reflects the diversity of views across the country, and many of our members' conclusions from participating in federal and provincial retirement savings consultations². We would be pleased to elaborate on our perspectives on this subject through an appearance before your committee when it holds hearings later this year.

Please contact Barb Amsden, Director – Strategy and Research, at (416) 309-2323 (bamsden@ific.ca) if you would like additional clarification of our views.

Yours sincerely,

¹ IFIC is the national association of the investment funds industry. Mutual funds provide Canadians with access to capital markets while diversifying (reducing) risk, professional money management and expert financial advice to help them plan for and cope with important life events.

² See www.ific.ca/, Policy, Retirement Savings for IFIC submissions on retirement savings and the value of advice.



Pre-budget Recommendations

The House of Commons Standing Committee on Finance report *Retirement Income Security of Canadians* describes the broad range of views witnesses had regarding the Canadian retirement income system.

Canadians are judged to be doing well by the following measures: old-age poverty is comparatively rare, retirees' incomes compare favourably with those of the population as a whole, long-term projections show that public retirement income provision is financially sustainable and the retirement income system in Canada is well diversified.

As well, a July 29, 2010 Statistics Canada report, *Replacing Family Income During the Retirement Years: How Are Canadians Doing?*, concludes that more recent cohorts tracked from their mid-50s to their late 70s across a 26-year period from 1982 to 2007 had higher family incomes in retirement than did earlier cohorts due to higher earnings and private-pension income. Another recent Statistics Canada report confirms how home ownership effectively adds to income in retirement.

However, Canada's population is aging, and the July 29, 2010 Statistics Canada report shows that some middle-income Canadians may not be saving enough. While on average Canadians are doing fine today, there may be gaps to be addressed for the future. In this regard, our submission focuses on fostering retirement savings through further innovation in Pillar 3, which includes registered retirement savings plans (RRSPs), including group RRSPs (GRRSPs).

Recent studies have commented on the proportional decline in the number of Canadians with occupational or company pension plans. At the same time, RRSPs (including GRRSPs), as well as new plans such as tax-free savings accounts (TFSA), and "Pillar 4" non-registered savings have been growing. Without diminishing the value of traditional DB and DC pension plans, we would like to see a balance of benefits and opportunities for all Canadians and believe that this can be achieved by tax changes, legislative amendments and intergovernmental collaboration on pension rule changes along the following lines:

1. Establish greater equivalency between those in DB/DC plans and those in RRSPs (including GRRSPs)

- a. Amend the *Income Tax Act* (ITA) to extend the minimum income-splitting age with a spouse or partner from 65 to 55 for RRSPs, consistent with rules governing DB and DC plans.
- b. Reduce registered retirement income fund (RRIF) minimum withdrawal factors and increase eligible DB-to-RRSP transfer limits in Income Tax Regulations 7308 and 8517 to reflect an older population, longer life spans and today's lower interest-rate environment.
- c. Make the pension credit available to people receiving income from a RRIF including life income funds (LIFs) regardless of age, as it is to recipients of annuities from pension plans.
- d. Allow employers to contribute directly to group RRSPs for their employees so that – as for DB and DC pension contributions – Canada Pension Plan (CPP), employment insurance (EI) and other payroll taxes will not apply. By removing the payroll tax burden, employers will be incented to make these contributions, rather than penalized.

2. Establish greater fairness between those in permanent jobs for larger companies and those with alternative work arrangements or patterns

Change the RRSP contribution limit and dollar maximum to a maximum lifetime limit to achieve greater equivalency among all Canadians' accumulation possibilities or make other supportive changes such as:

- a. Allowing those who leave the workforce for specified reasons (e.g., childcare, job loss) to accumulate RRSP room.
- b. Permitting those who are self-employed and may have widely varying incomes from year to year to base RRSP contributions on average income, allowing the carry-forward or back of earned income above the annual limit to maximize RRSP deductions.
- c. Considering relief for those who may have faced or face substantial market losses, from which most members of DB plans were shielded, to be able to deduct some losses from ordinary income.

3. Increase equity between the tax treatment of equivalent financial instruments

- a. Review and address the unfair, non-neutral and administratively complicated application of the goods and services tax (GST) and harmonized sales tax (HST) (which apply more heavily to mutual, segregated and other funds than to non-fund investment products) by applying a single low federal-provincial rate of sales tax to management, advisory and administrative services provided to funds. For nearly 20 years, the GST has applied at effective rates of four to five times more on mutual and other investment fund instruments as on non-fund financial products. Sales tax harmonization, economically desirable in principle, is exacerbating the long-standing unequal treatment of fund-holders under the GST. The inequity of the GST, and greater inequity of the HST, are not because of the higher “value-added” in a mutual fund, where additional taxation would be expected, but because the labour/salaries and net earnings that are part of delivering a financial product are fully taxable for funds, but tax-exempt in the case of holdings of guaranteed income certificates (GICs), equity and debt.
- b. Eliminate the double taxation of dividends in registered plans that does not exist in Pillar 4. Also as regards dividends, we suggest that the Finance Committee recommend use of actual dividends received (not the grossed-up amount of 125% for ineligible dividends or 145% for eligible dividends) in the means-tested “net income” calculation for Old Age Security (OAS) and Guaranteed Income Supplement (GIS) benefits. Some seniors try to avoid dividend income due to the dividend gross-up, meaning seniors with the same income may have different net income for purposes of social benefits calculations and hence receive substantially and unfairly varying net benefits.

4. Amend tax and pension legislation to allow or require the locking-in of employer contributions to RRSPs, limiting how much can be withdrawn before retirement

While a benefit of RRSPs in emergency situations is the flexibility to withdraw funds, this can also lead to the undesirable depletion of accumulated capital. The ease with which Canadians can withdraw their savings from their RRSPs is cited by both employers and policy-makers as a drawback of this plan type (and there are now TFSAs for the precautionary savings that RRSPs previously may have been used for). Indeed, the *2009 Melbourne Mercer Global Pension Index* suggests that introducing a mechanism for ensuring that voluntary retirement savings are preserved for retirement purposes is a way to improve the Canadian retirement income system. Governments could agree to allow or require locking-in for at least employer-

offered RRSPs and TFSAs, with certain permitted withdrawals and re-contributions (e.g., home buyers plan, lifelong learning plan, registered education savings plan, etc.).

5. Examine automatic enrolment and contribution escalation to increase participation in, and contributions to, employer or individual retirement savings plans

The number of Canadians participating in retirement savings plans and the threshold of contributions can be improved by techniques that preserve choice, but make it easier for the saver/investor to avoid missing out on retirement savings opportunities due to forgetfulness or the lack of time, knowledge or interest. Research suggests automatic enrolment, even with an opt-out at the investor's choice, will substantially increase amounts saved with no loss of choice or flexibility. The adoption of automatic enrolment in 401(k)s in the U.S. resulted in employee participation rates rising often to above 90%, especially among lower-income and minority workers, who had frequently been disadvantaged in the past. Similarly, the private-sector-provided KiwiSaver – into which employees are auto-enrolled with the right to opt out – has achieved coverage of 73% of the New Zealand labour force since the plan's inception several years ago.

After consulting with employers, employees and financial service solution providers to ensure the minimum of administration for all parties, federal and provincial governments jointly should make the changes necessary to allow for automatic enrolment of employees and automatic escalation in contribution rates based on, say, salary or length of service, with the ability to opt out, to enhance both participation and savings rates. This would require provinces that prevent automatic pension enrolment and payroll deduction of contributions and contribution escalation to exempt these features from the explicit consent requirement in employment standards legislation. We have written to provincial ministers in this regard.

Conclusion

In the studies of retirement savings over the past several years, we have seen what appears to be a policy preference for pension plans over GRRSPs. In fact, we believe that the real goal should be not a single structure or approach, but different ways of optimizing retirement savings. Canadians' financial needs will vary throughout their lives and the tools they will need should similarly be flexible and diversified. We believe the rules governing RRSPs, which are national in scope, mean RRSPs, including GRRSPs, are simpler to set up, generally entail a lower regulatory burden than do registered pension plans and are easily portable. They are more attractive for smaller and medium-sized businesses than DB or DC plans as they are less complex, more transparent and generate fewer regulatory costs for sponsors and participants.

As research shows that the basic framework of Canada's retirement income system is strong and highly respected, and as the July 29, 2010 Statistics Canada report attests to the system's providing a well-balanced distribution of income from OAS/GIS (Pillar 1), CPP/QPP (Pillar 2), pension and retirement plans (Pillar 3) and other sources (Pillar 4), we believe that the role of governments now should be to facilitate saving. They can do so by enacting the above proposals and removing obstacles, such as the many examples of cross-jurisdictional pension legislation and administrative differences, including continued paper requirements, that provide little benefit.

We believe that making changes in the categories above, coupled with renewed efforts to standardize administrative rules, will result in more companies offering retirement savings plans and more Canadians saving for retirement, higher average contributions per person and reduced regulatory cost and risk.