Canadian Association of Family Enterprises

Canadian Bar Association

Canadian Dental Association

Canadian Federation of Agriculture

Canadian Federation of Independent Business

Canadian Medical Association

Canadian Pharmacists Association

Canadian Physiotherapy Association

Canadian Psychological Association

Canadian Society of Customs Brokers

Canadian Veterinary Medical Association

Certified General Accountants Association of Canada

THE REGISTERED RETIREMENT SAVINGS PLANS ALLIANCE

"The Need for Pension Parity"

Ending the Disparity Between Registered Retirement Savings Plans (RRSPs) and Registered Pension Plans (RPPs).

March, 2001

<u>The RRSP Alliance (RRSPA)</u>:

The RRSP Alliance is comprised of 12 national organizations representing close to 600,000 members, who employ an additional 2 million Canadians. The Alliance was formed in 1994 for the purpose of preserving and improving Canada's retirement savings system. The following organizations are members of the Alliance:

- Canadian Association of Family Enterprises
- Canadian Bar Association
- Canadian Dental Association
- Canadian Federation of Agriculture
- Canadian Federation of Independent Business
- Canadian Medical Association
- Canadian Pharmacists Association
- Canadian Physiotherapy Association
- Canadian Psychological Association
- Canadian Society of Custom Brokers
- Canadian Veterinary Medical Association
- Certified General Accountants Association of Canada

For more information contact the RRSP Alliance Chair Mr. Garth Whyte at the Canadian Federation of Independent

Business at (613) 235-2373 or the RRSP Secretariat at (613) 731-8610 ext. # 2269

Introduction:

The Registered Retirement Savings Plans (RRSP) Alliance is comprised of 12 national organizations representing close to 600,000 members, who employ an additional 2 million Canadians. The RRSP Alliance (RRSPA) was formed in 1994 with the primary purpose of contributing to the public policy debate when it comes to preserving and improving Canada's retirement savings system.

During the past six years, the RRSPA has participated in the federal government's pre-budget consultation process by submitting briefs in regard to retirement income issues. The RRSPA has also reviewed and commented on government actions and policy with respect to RRSP contributions and other retirement policy issues.

One of the major goals for the federal government announced recently in the Speech from the Throne is to ensure that Canada remains a major player in the new economy and provide Canadians with equal opportunity to succeed. Canadians not having access to Registered Pension Plans (RPPs), be they self-employed, professional partners or employees, remain disadvantaged and do not have the same opportunity to succeed in this new economy when it comes to protecting and enhancing their retirement savings due the disparity that exists between RPPs and RRSPs. The recommendations contained within this document are focused at removing this disparity and creating a level playing field between all Canadians when it comes to retirement planning.

The RRSPA believes that, to improve the standard of living for Canadians in the future, the federal government must act today to protect and enhance RRSPs. In last year's report to the House of Commons (December 1999), the Standing Committee on Finance adopted several of the recommendations of the RRSPA in regard to RRSPs including the foreign property rule and increasing the contribution limits. While there was no actual change in the RRSP contribution limits we do applaud the work of the Committee in moving the federal government to act on the foreign property rule.

There are at least two fundamental goals of retirement savings: to guarantee a basic level of retirement income for all Canadians; and to assist Canadians in avoiding serious disruption of their pre-retirement standard of living upon retirement.

For RRSPA members and a growing number of taxpayers, private retirement savings plans are an essential component of their retirement planning. The self-employed and small business sectors of the economy are the fastest growing sectors in terms of new job creation, and they depend on RRSPs. As a result, RRSPs are increasingly critical when it comes to supporting the overall Canadian retirement income security system.

The RRSPA believes that a fair balance must be struck between those Canadians who are members of Registered Pension Plans (RPPs) and those who rely on RRSPs for their retirement – in short, the immediate adoption of the fundamental principle of pension parity. The federal government has already accepted this general principle in a number of policy papers from the 1980s that proposed increasing the RRSP contribution limits to levels equivalent with RPPs. Now is the time to move from principle to reality.

Background:

The issue of pension parity dates as far back as 1983. In 1983, the House of Commons Special Committee on Pension Reform recommended in *The Tax Treatment of Retirement Savings* that the limits on contributions to tax-assisted retirement savings plans be amended so that the same comprehensive limit would apply regardless of the retirement savings vehicle or combination of vehicles used. In short, the fundamental principle of pension parity was clearly established and accepted. Nevertheless, the disparity on limits on contributions between RPPs and RRSPs continues to this day.

In February 1984, a proposal from the Minister of Finance entitled *Improved Tax Assistance for Retirement Saving*, had as the primary objective placing all taxpayers on the same footing in terms of retirement savings plans. The proposal stressed that securing savings patterns helps limit the size and amplitude of business cycle swings. Specifically, two improvements to tax assisted retirement savings were adopted by the federal government: "(1) the limit on deductible contributions to retirement savings plans will be raised to 18 percent of earnings up to a maximum of $10,000 in 1985. **By 1988, this dollar limit will rise to $15,500;** (2) equivalent access to tax assistance will be provided regardless of the type of retirement savings vehicle used." Once again the principle of pension parity was firmly established.

Further support for the policy of pension parity was provided in the 1987 *White Paper on Tax Reform*. It was reiterated that the primary purpose was to provide equal access to tax assistance by individuals who save for retirement through different arrangements. The phase-in, however, was deferred by the then government. This, regrettably, was the first in a succession of such deferrals.

In the 1989 discussion paper, *Pension Reform: Improvements in Tax Assistance for Retirement Saving*, the government stated that: "Tax assistance for retirement saving is based on a simple principle: within clear limits, income set aside for retirement should be taxed when it is received as a pension. By allowing taxpayers to defer tax on savings, and on the years before retirement, the tax system encourages and assists Canadians to arrange for their financial security in later years." Over the medium and longer-term, when RRSPs are converted to annuities, they bring tax revenues to government. As the proportion of Canadians over the age of 65 grows, this will become an increasingly important source of tax revenue for government.

The proposed contribution limit for RRSPs, $15,500, was the result of extensive consultation and consideration by the federal government and would have achieved the objective of restoring equity between members of RPPs and those who rely on RRSPs for their retirement income.

In 1996, however, the government froze RRSP annual contribution limits at $13,500. In response, the RRSPA recommended to the government to increase the annual RRSP contribution limits to those initially proposed in the 1984 and 1987 tax reform proposals. We recommended that the dollar limit of RRSPs at $13,500 increase to $14,500 and $15,500 in 1998/1999 and 1999/2000, respectively. Subsequently, dollar limits should increase at the growth rate in the Yearly Maximum Pensionable Earnings (YMPE).

In its 1996 budget statement, the federal government announced that the contribution limits of RRSPs was to be frozen at $13,500 through to 2002/03, with increases to $14,500 and $15,500 in 2003/04 and 2004/05, respectively. As well, the maximum contribution limit for defined benefit registered pension plans will be frozen at its current level of $1,722 per year of service through 2004/05. By any other name, this is a *de facto* increase in tax payable that many Canadians have had to bear. In effect this policy of deferral only serves to implement the principle of pension parity in reverse; that is, by not increasing RRSP contributions to $15,500 in 1998, the current approach only serves to keep RRSP contribution limits "down with the Jones', and not up".

In December 1997, the Standing Committee recommended in its pre-budget consultations report, *Keeping the Balance: Security and Opportunity for Canadians,* "…that the schedule of contribution limits set out in the 1996 budget be revised so as to allow contributions to increase before 2002."[1]

While pension parity will be achieved between RPPs and RRSPs in 2004/05, it will have been accomplished on the backs of Canadians whose RRSP contribution levels have been frozen for far too long. As a consequence, the current policy of freezing RRSP contribution limits and RPP limits without adjusting the RRSP contribution limits to achieve pension parity serves to maintain inequities between the two plans until 2004/05.

The RRSPA, along with others, has been frustrated that twelve years of careful and deliberate planning by the federal government around pension reform has not come to fruition. **In fact, if the current policy remains in place it will have taken more than 17 years to implement needed reform to achieve pension parity (from 1988 to 2005). This demonstrated indifference by the federal government to retirement planning in Canada is not acceptable.**

<u>Tax Relief and Tax Reform Policies Supporting Canada's Social Infrastructure</u>

Reviewing the demographic picture in Canada, we know that an increasing portion of society is not only aging, but is living longer. By 2002, it is estimated that 444,000 more Canadians will be over the age of 65. It is projected that individuals over the age of 65 will increase from just over one in ten (12.2%) in 1996 to one in five (21.7%) in 2031.[2] Assuming that current trends continue and peak in the first quarter of this century, retirement income will increasingly play an important factor in the living standards and health of Canadians. Therefore, the role of private retirement income plans, such as RRSPs, will be critical in ensuring that Canadians continue to live in dignity and in good health well past their retirement from the labour force.

It is predictable that an aging population will place an even greater burden on Canada's already strained social support system. Therefore, individual and collective interests can be met by investing in retirement income plans today, which offset future costs to the Canadian social support infrastructure.

As indicated earlier in this document, a 1984 proposal recommended that the dollar limit for RRSPs be set at $15,500 by 1988 in order to achieve pension parity. Subsequently contribution limits for RPPs and RRSPs were to be adjusted by the growth in Yearly Maximum Pensionable Earnings (YMPE).

Currently RPPs and RRSPs are frozen and therefore they are unable to grow at the YMPE rate (see Table A). If the recommended policy of pension parity had been implemented in 1988, the growth in RPP and RRSP contribution limits could have grown in line with the yearly maximum pensionable earnings - and would be approximately $21,000 today.

TABLE A – RRSP Contribution Limits Adjusted by the Yearly Maximum Pensionable Earnings (YMPE)			
Year	**YMPE**[3]	**% change**	**RRSP Limits**
1988	$27,700		$15,500
1989	$28,500	2.89	$15,948
1990	$28,900	1.40	$16,171
1991	$30,500	5.54	$17,067
1992	$32,200	5.57	$18,018
1993	$33,400	3.73	$18,690
1994	$34,400	2.99	$19,249
1995	$34,900	1.45	$19,529
1996	$35,400	1.43	$19,809
1997	$35,800	1.13	$20,032
1998	$36,900	3.07	$20,648
1999	**$37,400**	**1.36**	**$20,928**
2000	**$37,600**	**0.63**	**$21,039**

It is critical to understand the difference between *tax avoidance* and *tax deferral*.

RRSPs allow Canadians to set aside necessary resources to provide for their retirement years. Over the medium and longer-term, when RRSPs are converted to annuities they bring tax revenues to government. While current contributions exceed withdrawals, this will not continue indefinitely as the baby boom generation retires at an accelerated rate.

At a time when the government is reviewing the role of public benefits in society, there is a social responsibility placed on government to ensure a stable financial planning environment is in place, which encourages greater self-reliance on private savings for retirement. A tidal wave is coming defined by the ageing population. Unlike most tidal waves we are fortunate in that we are able to plan and prepare for its arrival. We know that in order to weather this storm we need to invest in the future of Canada's social support safety net. We can do this by creating a buoyant economy, which will be able to sustain the buffeting of future pressures on Canada's social programs. Fostering an environment that encourages Canadians to save today for those rainy tomorrows will provide the government with future streams of tax revenue to withstand the inevitable pressures on our social security safety net.

The RRSPA Recommends:

1.**That the federal government commit to achieving fair pension policies for Canadians and end the disparity between Registered Pension Programs (RPPs) and Registered Retirement Saving Programs (RRSPs).**

Those Canadians who depend on RRSPs should not be discriminated against when it comes to protecting and enhancing their retirement income. It is not fair that those in RPPs have greater rights over their retirement planning than those Canadians who utilize RRSPs. Therefore, fairness should be achieved through pension parity by addressing issues such as contribution levels and creditor-proofing.

2.**That the federal government increase RRSP contribution limits yearly.**

Increasing the limits for private saving is an investment, not an expense. From the standpoint of synchronizing good tax policy with good social policy, it is essential that the RRSP system be expanded to give Canadians the means and incentive to prepare for retirement, while at the same time lessening any future burden on social programs.

3.**That the increase in dollar limit of RRSPs currently at $13,500 be accelerated to increase to $15,500 for the year 2001/02.**

Compared with other OECD countries, Canadians are at a distinct disadvantage in terms of their ability to save for their future retirement. To keep pace with two of our major trading partners (US, UK), Canada would have to nearly double existing contribution levels. While we are not suggesting that limits be doubled immediately it is nevertheless imperative for government to begin raising these limits. The current contribution ceiling of $13,500 is scheduled to rise to $14,500 by 2004 and $15,500 by 2005. The RRSPA recommends the increase in contribution ceiling be accelerated such that the 2001/02 limit is $15,500.

4.**That the federal government work with the provinces to creditor-proof RRSPs and RRIFs.**

The federal government can also take action in another important area when it comes to protecting Canadians and their ability to care for themselves in the future. Currently, if an individual declares bankruptcy, creditors are able to launch a claim against their RRSP or Registered Retirement Income Fund (RRIF) assets, except those held under an insurance contract. As a consequence, those Canadians who depend on RRSPs for retirement income have their quality of life in retirement at risk. In contrast, if employees with an RSP declare bankruptcy, creditors are unable to lay claim on their pensionable earnings. This is an inequitable situation that would be remedied if all RRSPs were creditor-proofed.

The RRSPA understands that this is a complicated issue falling under provincial, territorial and federal rules and legislation. As a result, creditor-proofing RRSPs (regardless of the vehicle in which they are held) on the same footing as RPPs, would require a co-operative approach at federal, provincial and territorial levels. We recommend the extensive work of the Uniform Law Conference of Canada on Creditor Access to Future Income Security Plans as a model for the necessary legislation.

5. That the federal government explores the regulatory changes necessary to allow easier access to RRSP funds for investment in small and medium-size businesses.

As part of the process to revitalize and sustain our economy, greater expectations are being placed on the private sector to create long-term employment opportunities. While this suggests a need to re-examine the current balance between public and private sector job creation, the government nonetheless has an important responsibility in fostering an environment that will accelerate job creation. In this context, the RRSPA strongly believes that current RRSPs should be viewed as an asset rather than a liability.

Financing is critical for the successful operation of any business and is especially important with respect to small and medium-sized enterprises. Financing has two components - debt and equity. Although there have been extensive deliberations on small business financing over the past decade, the focus has been on debt capital and access to equity has essentially been ignored. Access to equity capital is an issue faced by the small business sector in all nations. The issue in Canada has become more problematic because, as governments have changed investment and tax policy approaches in the past two decades, they have not examined the cumulative impact of these policies in restricting the flow of equity capital to the small business sector.

With proper mechanisms in place, the RRSP pool of capital funds can play an integral role in bringing together venture capital and small and medium-size business and entrepreneurs. Growing small business is a critical success factor in Canada's future.

Summary of Recommendations:

In summary, the RRSPA believes in the principle of pension parity, which the federal government clearly articulated and supported in a number of thoughtful papers released during the 1980s. The principle of pension parity should be accelerated and implemented immediately. To achieve the goal of developing a budget that will build a strong economy while, at the same time, protecting our national social infrastructure, the RRSP Alliance offers the following recommendations to the federal government:

1. That the federal government commit to achieving fair pension policies for Canadians and to end the disparity between Registered Pension Program (RSP) and Registered Retirement Saving Programs (RRSP).

2.**That the federal government increase RRSP contribution limits yearly.**

3.**That the increase in dollar limit of RRSPs currently at $13,500 be accelerated to increase to $15,500 for the year 2001/02.**

4.**That the federal government work with the provinces to creditor-proof RRSPs and RRIFs.**

5.**That the federal government explores the regulatory changes necessary to allow easier access to RRSP funds for investment in small and medium-size businesses.**

Endnotes: i Report of the Standing Committee on Finance, *Keeping the Balance – Security and pportunity for Canadians*, December 1997. ii. Statistics Canada, Medium Growth Scenario, 1997 iii YMPE Source: Revenue Canada, April 1999

1

Report of the Standing Committee on Finance, *Keeping the Balance – Security and Opportunity for Canadians*, December 1997.

2

Statistics Canada, Medium Growth Scenario, 1997

3

YMPE Source: Revenue Canada, April 1999