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Règles fiscales régissant les régimes de pension agrées collectifs

**SECTION NATIONALE DU DROIT DES RÉGIMES DE RETRAITE ET DES AVANTAGES SOCIAUX
ASSOCIATION DU BARREAU CANADIEN**

Août 2011

AVANT-PROPOS

L'Association du Barreau canadien est une association nationale qui regroupe plus de 37 000 juristes, dont des avocats, des notaires, des professeurs de droit et des étudiants en droit dans l'ensemble du Canada. Les principaux objectifs de l'Association comprennent l'amélioration du droit et de l'administration de la justice.

Le présent mémoire a été préparé par la Section nationale du droit des régimes de retraite et des avantages sociaux de l'Association du Barreau canadien, avec l'aide de la Direction de la législation et de la réforme du droit du bureau national. Ce mémoire a été examiné par le Comité de la législation et de la réforme du droit et approuvé à titre de déclaration publique de la Section nationale du droit des régimes de retraite et des avantages sociaux de l'Association du Barreau canadien.

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I. INTRODUCTION

C'est avec grande satisfaction que la Section nationale du droit des régimes de retraite et des avantages sociaux de l'Association du Barreau canadien (la Section de l'ABC) participe au processus de consultation mené par le ministère des Finances Canada au sujet des enjeux reliés aux projets de règles fiscales régissant les régimes de pension agréés collectifs (RPAC). La Section de l'ABC regroupe des membres de tous les coins du pays, qui travaillent dans les domaines du droit des régimes de retraite et des avantages sociaux, dont des avocats qui conseillent des administrateurs de régimes de retraite et d'avantages sociaux, des employeurs, des syndicats, des employés et des groupes d'employés, des fiduciaires et des compagnies d'assurance, des conseillers en matière de régimes de retraite et d'avantages sociaux, ainsi que des gestionnaires de placements et des conseillers en placements.

Ce mémoire vient compléter le mémoire, intitulé « Régimes de pension agréés collectifs », que la Section de l'ABC avait présenté au ministère des Finances Canada en avril 2011, ainsi que le mémoire de la Coalition pour la bonification des revenus de retraite (CBRR) sur les règles fiscales régissant les régimes de pension agréés collectifs. Même si l'ABC est membre de la CBRR et qu'elle a collaboré à la rédaction du mémoire de la CBRR, celui-ci reprend les commentaires pénétrants de membres de l'ABC qui ont une expertise confirmée dans les domaines des régimes de retraite et des avantages sociaux.

La Section de l'ABC a abordé celles des questions posées par le ministère des Finances Canada dans son document de consultation du 15 juin 2011 sur les règles fiscales régissant les régimes de pension agréés collectifs, pour lesquelles elle était en mesure de proposer des solutions utiles. Les membres de la Section de l'ABC s'intéressent à différents aspects de leur domaine de pratique, et les réponses à certaines des questions reflètent ainsi plus d'un point de vue. C'est notamment le cas des questions 3*a*), *b*) et *d*), ainsi que 4*a*) et *c*). Dans chacun de ces cas, la Section de l'ABC n'adopte pas de position ferme par rapport à la question du ministère.

II. ISSUES FROM THE CONSULTATION PAPER

A. Administrator

1. What restrictions, if any, should there be on the type of entity that would be permitted to be the administrator of a PRPP?

The CBA Section recommends placing restrictions on the type of entity permitted to be a PRPP administrator. For example, administrators of Registered Pension Plans (RPPs) must generally be residents of Canada. This restriction should also apply to PRPP administrators.

However, the group of eligible administrators should not be subject to restrictions that will unnecessarily impede the development of a price competitive functioning market. Finance Canada's *Proposed PRPP Framework* document, dated June 24, 2011¹, states that eligible administrators could include entities such as financial institutions, public pension plans and government bodies. We believe that non-corporate entities should be permitted to act as PRPP administrators. The standards and restrictions should be the same for all PRPP administrators.

The CBA Section agrees that the tax rules would need to be consistent with the pension benefits standards rules.

B. Primary Purpose Requirement

2. Should there be a primary purpose test for PRPPs? If so, what should it be?

The CBA Section believes that there should be a primary purpose test for PRPPs as a condition of registration under the federal *Income Tax Act* and regulations. We agree with the proposed primary purpose on page two of the consultation document, i.e. to accept contributions from members and/or employers for the purpose of providing periodic payments in retirement.

The CBA Section recommends that the primary purpose rule be flexible enough to permit self employed and affiliate groups to sponsor PRPPs.

¹ Department of Finance, *Proposed PRPP Framework – Detailed Elaboration of Key Elements*, June 24, 2011, **Note:** this document was not published or posted on-line by Finance but was forwarded by email to CBA for comment/feedback.

Although not specifically addressed in the consultation document, the CBA Section also supports flexible plan designs within PRPPs, including the ability to create “target benefit” PRPPs.

C. Contributions / Limits

3. a) Which approach – using the existing system of dual PA/RRSP limits or permitting contributions under the RRSP limits only – is most practical?

Many CBA Section members prefer an approach in which PRPP contributions by both employers and participants are subject to limits similar to those for RRSPs, but modified to operate in a more equitable manner. They believe that this “modified RRSP approach” to PRPPs would be more practical and simpler than the dual approach. While many CBA Section members prefer the RRSP approach, they recognize that it has two main drawbacks, both of which can and should be addressed. First, RRSP limits are based on the previous year’s income, and trail the money purchase limit by a year. Second, employer contributions to RRSPs are treated as employment income, and result in additional CPP contributions, EI premiums and other payroll taxes that employees and employers must pay. These issues could be addressed by adopting a modified RRSP approach in which the dollar limits for a PRPP equal the money purchase limits in any given year, and employer contributions to a PRPP are exempted from CPP contributions, EI premiums or other payroll taxes.

Basing the PRPP limits on RRSP limits would reduce the paperwork for employers, making contributions easier to administer and increasing the likelihood that small employers will contribute to PRPPs. Treating PRPP employer contributions the same as employer contributions to an RRSP would enable employers to remit their contribution along with the employee's contributions to the administrator. The employer would not be responsible for monitoring any contribution limits or dealing with pension adjustments (PAs).

Many CBA Section members are concerned that under the dual approach employers would have the additional obligation of calculating and reporting PAs. Alternatively, groups of employers could provide their employee data to the administrator and have the administrator perform the PA function. For most medium and large employers, the extra tasks involved in the dual approach could be of minimal consequence, but for businesses with under 25 employees (of which there are many, and which are a particular target of the PRPP project), the dual approach would likely discourage employer contributions.

However, other CBA Section members favour a “modified dual approach” in which administrators could issue PAs on employers’ behalf. This modified dual approach would ensure flexibility in plan design, including facilitating the transfer of benefits from other locked-in arrangements to a PRPP. These are important factors for certain groups wishing to participate in PRPPs and could expand coverage.

For the self-employed and many professional groups, it will not matter which approach is taken, since employer contributions would not be available.

b) Would there be any administrative or compliance issues with reporting PAs for PRPP members of participating employers and issuing contribution receipts for other members?

Again, many CBA Section members believe these requirements may discourage some small business employers from participating and contributing to PRPPs. Administrators would incur incremental administrative costs when working with large numbers of small businesses on PA issues. These additional costs would constitute overhead that would ultimately be passed on to participants as higher fees. A PRPP system based entirely on RRSP limits, modified as proposed under 3(a), would not result in any incremental costs for PRPP participants because under either system plan participants must report contribution receipts on their taxes.

Other CBA Section members believe that the modified dual approach described in 3(a) would create more flexibility in plan design and portability, and the increased flexibility would likely outweigh any concerns with higher fees.

c) Should employers be solely responsible for determining and reporting PAs, as is currently the case for employers sponsoring an RPP, or should PRPP administrators determine PAs and provide them to employers to report on T4s? Alternatively, should administrators, instead of employers, be responsible for reporting PAs and employee PRPP contributions directly to members?

If the RRSP approach is adopted, there would be no need for PA reporting, and only contribution receipts would be required. Contribution receipts should be issued by the administrator to the PRPP participants based on actual contributions received from both employers and participants.

If, however, the dual approach is adopted, PAs will be required. If so, the CBA Section recommends that employers be given a choice. They may calculate and report PAs directly or

have the administrator perform the function for them. The additional overhead required for administrators to follow up and verify data from a large number of small employers could in some cases impact the cost-effectiveness of the program. The choice should still be made available, particularly for affiliate groups whose preference for flexibility in plan design and portability would most likely outweigh the cost issues.

d) How should the tax rules address contributions in multiple PRPPs that exceed contribution limits that otherwise apply for RPPs?

Many CBA Section members believe that the dual approach would require the development of a new penalty regime for over-contributions. This is one of the downsides of the dual approach. Adopting the modified RRSP approach, described in 3(a), would avoid this problem.

Other CBA Section members recommend that, if the modified dual approach described in 3(a) is adopted, a new penalty regime be developed to deal with over-contributions that does not initially risk de-registration, but rather provides a gradual set of penalties that could ultimately result in de-registration.

e) Under the RRSP limits only approach, what would be the best way to take into account direct employer contributions to a PRPP that would reduce a PRPP contribution? Should the employer or the administrator be required to report such contributions to the member? Would this approach raise RRSP limit compliance issues for PRPP members with a participating employer?

The CBA Section recommends that the PRPP system treat employer contributions in the same manner as they are currently treated under the RRSP system. It is our understanding that when an employer contributes to an employee's RRSP account under a group RRSP, the contribution is added to the employee's taxable income, the employee can deduct the contribution provided they have sufficient RRSP contribution room, and the deduction is supported by a contribution receipt issued by the financial institution operating the RRSP. If the RRSP limits only approach were adopted, PRPPs would presumably operate in the same way. We recommend that the administrator be required to issue a contribution receipt for all plan participant and employer PRPP contributions.

D. Pensionable Service

4. a) Should any past service purchases (under a defined benefit RPP) of PRPP years of employment be permitted?

Many CBA Section members believe that the goal of simplicity would be impeded if past service purchases were permitted. The employer's associated reporting obligations would add to the complexity of the PRPP system. Other CBA Section members prefer PRPP rules with enough flexibility to permit past service purchases.

b) If so, should past service purchases be restricted to those PRPP years where a PA was reported?

If PAs are to be reported and past service purchases permitted, the purchases should be restricted to periods for which a PA was reported. Requiring employers to report employment periods outside of the PA will create an additional administrative burden.

c) If past service purchases were to be permitted for PRPP years where a PA was not reported but where there was employer oversight of PRPP participation (i.e., where an employer did not make direct contributions but oversaw the remittance of employee contributions), what mechanism could be used to verify years of pensionable service with an employer? What would be the associated compliance considerations?

An employer remitting employee contributions to a PRPP could be required to report the participating employee's period of employment during the year. However, many CBA Section members believe this reporting requirement would increase an employer's administrative burden and run counter to the desired simplicity of the PRPP system.

d) Are there any practical ways to recognize years of participation in a PRPP for past service purchases in respect of self-employed individuals (i.e., individuals for whom there is no employer oversight) that would not raise significant verification and compliance issues?

If the decision is to require PA reporting and to permit past service purchases, self-employed individuals should have the same rights as employed individuals. The CBA Section believes that neither significant verification nor compliance issues would arise because PRPP participation will be tracked yearly by the Canadian Revenue Agency and will be recorded in each taxpayer's notice of assessment.

E. Leaves of Absence and Periods of Reduced Pay or Disability

5. a) Should the RPP prescribed compensation rules be extended to PRPPs?

The prescribed compensation rules are a useful tool to permit continued accrual of benefits under an RPP for a period of time when the plan member is not receiving the usual level of earnings from the employer. If a modified RRSP approach is adopted as described in 3(a), contributions would operate under the RRSP limits only approach. Many CBA Section members recommend that, if the dual approach is adopted and applies RPP limits when an employer is contributing on behalf of its employees, the prescribed contribution rules should be extended to PRPPs, but only for employers operating under the RPP limits.

Other CBA Section members are concerned that the RRSP rules would preclude plan members (or their employer or a third party) from contributing to their PRPP accounts if the plan member becomes disabled or takes a leave of absence. They recommend a new rule to permit contributions to PRPP accounts under the RRSP system where plan members meet the conditions in the prescribed compensation rules. The rule could, for example, prescribe a plan member's earnings room at a level based on the prior three years' earnings and PRPP contributions.

b) If so, what should be the level of employer PRPP involvement required under such provisions? What would be the associated compliance considerations?

An employer could be required to report the actual earnings for the year, the employer and employee contributions remitted to the PRPP, and (if contributions were made for a period without earnings or with reduced earnings) what the compensation would have been if it had continued for the whole year without reduction. If the prescribed compensation is to be accumulated and tracked for the employee's overall participation in the PRPP, these tasks should be the responsibility of the PRPP administrator.

F. Transfers

6. Would it be feasible and appropriate to allow transfers of surplus from a defined benefit RPP to a PRPP? If so, to what extent should such transfers be permitted?

While it may be feasible from an income tax perspective to transfer surplus from a defined benefit RPP to a PRPP, the CBA Section believes that employers are unlikely to be interested in these transfers. Typically, employers will only be interested in utilizing a surplus if they can control its use following transfer. Currently, employers only consider the use of surpluses to cover their required contributions under a defined contribution provision of an employer sponsored RPP. An employer is unlikely to consider transferring surplus to a PRPP with multiple participating employers, unless the PRPP provides a mechanism to track the surplus and allows the employer to draw on it to make contributions for their employees. However, the mechanism would run counter to the desired simplicity of a PRPP. The CBA Section believes it is not worthwhile developing rules to permit these transfers.

In any event, pension standards legislation makes it difficult for an employer to transfer surplus from one RPP to another, except in limited circumstances where past service benefits are also transferred. It is unlikely that an employer could arrange to transfer surplus from an RPP to a PRPP under the current pension standards regime. The CBA Section recommends that, given the complexity of the rules on surplus entitlements under RPPs, the PRPP system not include provisions that might be perceived as creating rights to surplus that do not currently exist under the law.

G. Qualified / Prohibited Investments

7. a) What modifications, if any, should be made to the prohibited investment rules for RPPs to adapt them to PRPPs?

The prohibited investment rules under Income Tax Regulation (ITR) 8514 disallow investment of RPP assets in the securities of an employer or member participating in a RPP, except where those securities are acquired through the open market of a stock exchange. Other exceptions exist under ITR 8514(2.1) where the RPP is a multi-employer plan and the employer in question does not play a predominant role in the plan. PRPPs are likely to be run by an administrator at arm's length from those employers participating in the PRPP and will likely cover the employees of a large number of employers, as well as self-employed individuals. For these reasons, the CBA Section believes that PRPPs are unlikely to provide employers with an opportunity to manipulate the system and engage in improper self-dealing in the field of investments. Thus, an exception similar to that in subsection 8514(2.1) could be extended to PRPP investments provided the PRPP meets similar conditions, in particular the minimum

number of participating employers and the limit on the number of members employed by a particular employer.

b) Should there be qualified investment rules for PRPPs (for example, similar to those that currently apply to RRSPs)?

The CBA Section recommends that a PRPP be treated like other RPPs rather than an RRSP for purposes of investments. In this case, there would be no need for qualified investment rules.

H. Minimum Employer / Membership Requirement

8. a) Should there be rules requiring PRPPs to be established for a minimum number of employers or self-employed members?

PRPPs that provide low cost savings vehicles for individuals currently without a RPP will inevitably attract large numbers of employers and self-employed individuals. The CBA Section believes that such rules will not likely be required.

b) If so, how many employers/members should be required to participate?

No comment.

I. Forfeitures / Refunds

9. Are there issues around vesting and auto-enrolment that could increase complexity and compliance costs for employers and/or administrators in relation to the tax rules for PRPPs? If so, how could these issues be addressed?

The CBA Section recommends that PRPPs operate with immediate vesting. This would be consistent with the operation of individual and group RRSPs and would ensure simplicity in the PRPP's administration.

III. CONCLUSION

The CBA National Pensions and Benefits Law Section trusts these comments will assist Finance Canada in its work on this important initiative. We would be pleased to respond to questions and to provide further information regarding any of the issues addressed in this submission.