Standard Life

Legislation matters

April 2012

2012 Federal Budget – Nothing new on the Pooled Registered Pension Plan (PRPP) front for now

On March 29, 2012, the federal Finance Minister, Mr. Jim Flaherty, presented the 2012 federal budget. However, there are no new developments on the PRPP front, other than to indicate that the tax rules for PRPPs will be implemented in 2012. The comments received during the consultation period, which ended on February 14, 2012, are being reviewed.

The federal finance minister also announced the following measures:

- The Canada Pension Plan (CPP) will not be changed, because the CPP is sustainable at the current contribution rate of 9.9% of pensionable earnings.
- As expected, the federal government will gradually increase the age of eligibility for Old Age Security (OAS) and Guaranteed Income Supplement benefits from 65 to 67 starting in April 2023, with full implementation by January 2029. In addition, starting on July 1, 2013, Canadians will be allowed to defer take-up of their OAS benefits for up to five years – and receive a higher, actuarially adjusted, annual pension.
- The federal government will introduce technical amendments to strengthen the *Pension Benefits Standards Act*, 1985, which applies to federally-regulated private pension plans.
- The tax rules applicable to Retirement Compensation Arrangements (RCAs) and Employee Profit Sharing Plans (EPSPs) will be tightened:
  - **RCAs** – It is proposed that new prohibited investment and advantage rules will apply directly to prevent RCAs from engaging in non-arm's length transactions. These rules will be based very closely on existing rules for TFSAs and RRSPs. In addition, a new restriction will apply on RCA tax refunds in circumstances where RCA property has lost value.
  - **EPSPs** – A targeted measure is proposed to discourage excessive employer contributions by introducing a special tax. The tax would be payable by a "specified employee" who has a significant equity interest in their employer or who does not deal at arm's length with their employer. This special tax will be payable on an ''excess EPSP amount'', which will generally be the portion of an employer's EPSP contribution, allocated by the trustee to a specified employee, that exceeds 20% of the specified employee's salary received in the year by the specified employee from the employer. This measure will apply to EPSP contributions made by an employer on or after March 29, 2012, with the exception of contributions made before 2013, pursuant to a legally binding obligation arising under a written agreement or arrangement entered into before March 29, 2012.

2012-2013 Québec Budget – Québec acts on its commitment to promote the implementation of Voluntary Retirement Savings Plans (VRSPs)

In his March 20, 2012 budget, Québec Finance Minister Raymond Bachand acted on his commitment in the 2011-2012 budget to implement VRSPs in cooperation with the federal government and the other provinces.

The main parameters of the VRSP will be harmonized with the new pooled registered pension plan (PRPP) for which the federal government tabled Bill C-25 in November 2011. Please refer to the November 2011 special issue of *Legislation matters* for further information.

The Minister of Employment and Social Solidarity is expected to table a bill this spring setting forth the necessary legislative provisions for implementing VRSPs as of January 1, 2013. It has been announced that consultations will be held on the proposed bill.

The aim of VRSPs is to provide all workers with access to a group pension plan. More specifically, the 2 million workers who are currently unable to participate in an employer pension plan. In other words, with the VRSP, the government of Québec aims to offset the savings insufficiency of workers who have no personal savings and no access to an employer pension plan.

VRSPs will be:

- Easy for workers to access
- Simple
- Easy for employers to administer
- Flexible
- Inexpensive
- Tax deductible
- Advantageous for all

The main characteristics of VRSPs, as proposed in the Québec budget, are as follows:

- **Obligation to offer a VRSP to employees** – Companies that do not already offer employees a retirement savings plan through payroll deductions and have five or more employees with at least one year of uninterrupted service will be required:
  - To choose a VRSP to offer their employees
  - To enrol all employees with at least one year of uninterrupted service in a VRSP
  - Make source withholdings of employee contributions and remit them to the VRSP administrator

  Employers will have until January 1, 2015 to comply with the obligation of offering a VRSP to their employees.

  After January 1, 2015, an employer that is obliged to offer a VRSP will have one year to comply.

  Employers with fewer than five employees with at least one year of uninterrupted service will not be required to offer a VRSP, but they can opt to offer it voluntarily.

- **Automatic enrolment of workers** – If an employer is required to offer a VRSP, its employees will be automatically enrolled in the plan. However, they may withdraw from the VRSP within 60 days of enrolment. VRSP participants may also choose to suspend contributions for a certain time or to change their contribution rate.

- **Voluntary enrolment** – Individuals who are not automatically enrolled, such as self-employed workers or individual savers, may enrol in a VRSP of their choice by contacting a plan administrator directly. Employees may also enrol in the VRSP of their choice at any time. Plan administrators may not turn down an enrolment application.

- **Contributions** – Employers will not be required to contribute to a VRSP. Employers that make contributions for their employees will be exempt from payroll taxes on said contributions. The employer's contributions will be deductible from its taxable income for both Québec and federal income tax purposes.

  Employees may choose their VRSP contribution rate. A default contribution rate will apply to participants who do not make this choice. The default contribution rate will initially be set at:

  - 2% from January 1, 2013 to December 31, 2015
  - 3% from January 1, 2016 to December 31, 2016
  - 4% as of January 1, 2017

  Like RRSP contributions, employee contributions will be deductible from their taxable income.

  Contributions to a VRSP will be in addition to those made to an RRSP and will be subject to the same annual cap as RRSPs.

- **Locked in** – Employee contributions will not be locked in. Amounts paid into a VRSP may be before retirement but will be subject to both Québec and federal income tax.

  Direct contributions by an employer will be locked in but may be withdrawn by employees as of age 55.

- **Investment choices** – VRSP administrators must offer a default investment option based on a "lifecycle" approach where the risk level is adjusted based on the participant's age. VRSP administrators may also offer a maximum of five other investment options with prudent allocation of asset categories reflecting various risk levels.

- **Management fees** – Management fees of plan administrators will be the same for all VRSP participants (employees, self-employed workers, etc.). As one of the fundamental features of the VRSP is its low cost, the administrator will have to show the Régie des rentes du Québec that the management fees are comparable with those of institutional pension plans of a similar size.

  Certain additional fees may be charged to the participant, such as fees for personalized consulting services or transfers between VRSPs.

- **Oversight**

  - **VRSP administrators** – VRSPs will be administered by third parties, such as financial institutions or investment fund managers; they will have to hold a permit issued by the Autorité des marchés financiers (AMF).
  - **VRSPs** – All VRSPs must be registered with the Régie des rentes du Québec, as they'll be responsible for overseeing these plans and ensuring compliance with the legislation on VRSPs.
  - **Employers** – The Commission des normes du travail will be responsible for overseeing employers concerning their obligation to offer VRSPs and they will intervene, in particular regarding complaints, to enforce the provisions of the law.

The next step is for the Minister of Employment and Social Solidarity to table the required legislative provisions for implementing VRSPs as of January 1, 2013. The tabling is expected this spring.

2012 Ontario Budget - The Ontario government is not yet on board with the implementation of the PRPP

On March 27, 2012, the Ontario Finance Minister, Mr. Dwight Duncan, presented his 2012 budget. Several measures affecting pension plans are proposed.

On the federal PRPP framework front, the least we can say is that Ontario, the largest jurisdiction in Canada, is not yet on board with implementation. Ontario believes the implementation of pension innovation should be tied to the Canada Pension Plan (CPP) enhancement as part of a comprehensive approach. In fact, Ontario continues to support a modest, phased-in fully funded enhancement to the CPP.

Ontario's position on the federal PRPP framework is that the protection of plan members is critical to the success of PRPPs. In a for-profit environment, priority must be given to the interests of plan members.

Ontario has a number of concerns with the current federal PRPP framework, such as:

- PRPPs may simply replace one form of retirement arrangement with another, instead of expanding retirement income savings and coverage;
- it is unclear if the PRPP's fiduciary framework adequately protects plan members;
- it is uncertain whether compulsory employee contributions would be flexible enough to allow for various life events, such as divorce or periods of financial hardship;
- the extent to which PRPPs could achieve their low-cost objective is unclear; and
- each province would need to establish an effective licensing and regulatory regime — the cost of regulation must be reasonable since these costs would be passed on to PRPP participants.

In his budget, Mr. Duncan indicates that Ontario will continue to work collaboratively with other provinces as well as the federal government to develop this model.

The other proposed measures affecting pension plans are the following:

- **Ongoing Pension Reform** – Ontario is currently drafting regulations to implement many of the reforms introduced in the last two years that specifically address defined benefit pension plans issues, such as clarifying pension surplus rules or strengthening funding rules. Draft regulations will be released later this spring or later in 2012.

In addition, the Ontario government is announcing its intent to proclaim the following provisions effective July 1, 2012:

  - Immediate vesting of pension benefits
  - Elimination of future partial wind-ups
  - New measures on grow-in benefits, such as making these benefits available to all eligible members under defined benefit pension plans who are terminated other than for cause

- **Financial-hardship unlocking** – Ontario intends to restructure the program to make accessing locked-in funds a simpler and more streamlined process. Consent from the regulator would no longer be required to withdraw pension money for reasons of financial hardship. Instead, applicants would be able to request withdrawals directly from their financial institutions. Draft regulations will be released for consultations. Over the next two years, the government of Ontario will monitor the new application procedure to evaluate its effectiveness.
- **Public-sector defined benefit pension plans** – Measures have been proposed to enhance the financial situation of public-sector defined benefit pension plans in Ontario that are either jointly sponsored pension plans or single-employer pension plans. The objective of the proposed measures is to reduce the growth in pension costs. In addition, since many of Ontario's defined benefit public-section pension plans have a relatively small amount of assets and members, the Ontario government intends to introduce a legislative framework in the fall of 2012 that would facilitate the pooling of pension fund assets. The intention is to allow access to higher-return investment opportunities that are available to larger investment pools – i.e. avoid the duplication of costs and benefit from economies of scale. The government will appoint an adviser to lead the implementation process and to develop recommendations on a model for managing these pooled assets.
- **Solvency funding relief** – The Ontario government is proposing to extend the 2009 temporary solvency funding relief measures that are applicable to defined benefit pension plans. Ontario is also proposing additional funding measures applicable to defined benefit pension plans, like allowing the use of letters of credit from financial institutions to cover up to 15% of pension plan solvency liabilities.

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