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The Association of Canadian Pension Management
L'Association canadienne des administrateurs de régimes de retraite

November 27, 2019

Increasing Support for Retirement Savings:

Proposals to Modernize Canadian Tax Rules Applicable to Registered Plans

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FOREWORD

ACPM (THE ASSOCIATION OF CANADIAN PENSION MANAGEMENT)

ACPM (The Association of Canadian Pension Management) is a national, non-profit organization acting as the informed voice of plan sponsors, administrators and their service providers in advocating for improvement to the Canadian retirement income system. Our membership represents over 400 companies and retirement income plans that cover millions of plan members.

ACPM believes in the following principles as the basis for its policy development in support of an effective and sustainable Canadian retirement income system:

Diversification through Voluntary / Mandatory and Public / Private Options
Canada's retirement income system should be comprised of an appropriate mix of voluntary Third Pillar and mandatory First and Second Pillar components.

Third Pillar Coverage
Third Pillar retirement income plan coverage should be encouraged and play a meaningful ongoing role in Canada's retirement income system.

Adequacy and Security
The components of Canada's retirement income system should collectively enable Canadians to receive adequate and secure retirement incomes.

Affordability
The components of Canada's retirement income system should be affordable for both employers and employees.

Innovation in Plan Design
Canada's retirement income system should encourage and permit innovation in Third Pillar plan design.

Adaptability
Canada's retirement income system should be able to adapt to changing circumstances without the need for comprehensive legislative change.

Harmonization
Canada's pension legislation should be harmonized.

INTRODUCTION

Governments in Canada have long encouraged saving for retirement. Part of this encouragement is recognizing that a sufficient array of choices must be available to meet the diverse needs of people and the changing circumstances they will face throughout their lifetimes; and part is deferring taxes on contributions to retirement savings until those contributions generate income for Canadians in the future. The *Income Tax Act* (Canada) (the "ITA") rules within which the available vehicles operate should be aligned with and reflect today's economic realities and longevity data. In addition, the ITA must also be amended to reflect new plan designs; in particular, target benefit plans (TBPs) already implemented in New Brunswick, British Columbia, Alberta and being considered in other jurisdictions as well.

PERSPECTIVE ON THE CONCEPT OF TAX DEFERRAL

Before we examine possible changes in tax rules, it may be useful to reflect on the concept of tax deferral. Deferring taxes on contributions paid into retirement savings vehicles is properly seen as an encouragement to save. Many people are pleased to see their contributions practically double immediately and seem to pay little attention to the fact that when they eventually withdraw sums, those will be reduced significantly by income tax. Governments have traditionally shown the immediate impact of the tax deductions as an expenditure for budget purposes, so whenever rules change to increase limits on deductible amounts, budgets show an increase in the coming years' deficits. But it should be understood that the vast majority of those tax amounts are not foregone but simply deferred, so that future governments can expect tax revenues when the individuals receive taxable payments out of those savings vehicles during their retirement years.

This factor was presented in a special research report issued by the Ministry of Finance in 2001[1], which compared current cash flow impacts of tax-sheltered retirement savings contributions and investment earnings, as included in yearly budgets, to the present value of long term impacts that include future withdrawals from retirement savings vehicles. However, the assumptions used in that report, prepared almost two decades ago, might need to be updated to reflect current market realities, which could produce revised results that show tax-sheltering impacts in a more positive light.

In addition, the accumulated savings in retirement vehicles grow at the rate of return produced by the assets in which they are invested, so future governments benefit from the deferred taxes growing in parallel, without even reflecting some tax concessions that apply to investments outside those vehicles, such as the dividend tax credit and the recognition of capital gains only in part (currently 50%). In most cases, we can expect those investment returns to be far higher than the rate being paid by the government on its bonds that finance its current debt.

[1] "Tax Expenditures and Evaluations", 2001 Department of Finance Canada (https://www.fin.gc.ca/taxexp-depfisc/2001/taxexp01_e.pdf)

Furthermore, as the gradual aging of the population can be expected to impose some strain on future government budgets because of unfunded pension benefits (OAS and GIS) and health costs, it will be useful to see withdrawals from savings vehicles produce tax revenues for governments when more workers reach retirement. Knowing that the accumulated sums in savings vehicles currently amount to trillions of dollars, it is interesting to consider that a significant portion of this represents a source of future government revenues that could offset its current and future debt.

In short, it is important to recognize that changing the ITA rules applicable to registered plans to increase allowable contributions should not be considered only as an expenditure for current budget purposes. Instead, it is a public investment by the Government of Canada in future federal budgetary objectives.

TAX REFORMS ARE NEEDED NOW

In ACPM's view, ITA reforms are needed now to build on government initiatives aimed at increasing retirement savings by modernizing the tax rules released in 1992 to reflect today's socioeconomic environment and Canadians' increased life expectancy. In this paper, ACPM identifies specific ITA and tax policy reforms relating to registered plans that would assist in meeting these objectives.

1) PENSION ADJUSTMENT AND RELATED TAX DEFERRED SAVINGS LIMITS: UPDATE FACTOR OF 9 TO FACTOR OF 12

The government decided long ago that it is good social policy to have tax rules that encourage retirement savings by deferring taxation of contributions to registered plans and their investment earnings until amounts are paid out as retirement benefits. However, there has always been some limitation on such amounts in order to maintain an appropriate balance between encouraging savers and the cost to current tax revenues. For many years, rules differed considerably between DB plans and DC plans or RRSPs, and many observers noted in the 1980's that DB plans could receive greater tax assistance than DC plans and RRSPs.

The Pension Adjustment (PA) rules were introduced in the early 1990s as part of a major reform that was intended to create a "level playing field" between DB plans and DC plans or RRSPs in the level of tax deferral assistance. The PA was created as the key to record the value of the DB accrual and therefore how much tax shelter room remained available. The carry forward of unused tax sheltering room was another new measure that allowed DC plans and RRSPs to be treated in a manner that is comparable to DB plans. It was understood that the PA calculation was not perfect but could be considered reasonable over a typical career.

The most important component of the PA calculation was the "Factor of 9", which was meant to approximate the aggregate contributions needed over a full career to provide a pension benefit comparable to a maximum plan[2].

Such a plan provided an annual benefit of 2% (which was the maximum rate allowed for a pension formula based on salary) of final-average-earnings, generous early retirement provisions and post-retirement indexing. The combination of this factor of 9 and the maximum 2% formula produced the maximum DC/RRSP contribution of 18% of earnings. The main assumptions required to estimate the value of such a pension were the discount rate, the inflation rate and life expectancy. These assumptions have changed drastically in the last 30 years.

Because of the changes in assumptions, the original "level playing field" can no longer be considered level. This inequity is directly linked to the use of the "Factor of 9", which was determined in the 1980s and is significantly out of date. The Factor of 9 should be amended to restore some equity in the system between DB and DC/RRSP plan members and how much savings may be tax sheltered. DB members can accrue a maximum benefit of 2% of earnings. DC contributions are limited to 18% of earnings (9 x 2% = 18%). Dollar caps maintain the 9:1 ratio as well - $2,959 for DB x 9 = $27,000 for DC for 2019. The 9:1 ratio between DB and DC plans for contribution purposes should at a minimum be changed to reflect current economic and demographic realities.

Adjustments for current demographic conditions

The original "Factor of 9" relied upon mortality tables that were in use at the time it was developed. Assuming it was the GAM83 table, we estimate that the more recent CPM14 table with generational mortality improvements under Scale CPM-B would on its own increase the "Factor of 9" by roughly 1.5.

Adjustments for current economic conditions

When the original "Factor of 9" was determined, it was reasonable to assume that long-term inflation would average 4% per annum and that a balanced portfolio would yield 7.5% per annum (after fees) with a real return of roughly 3.5% per annum (after fees).

Based on actual experience over the past two decades, the Bank of Canada's mid-point target and implied inflation on real return bonds, it is generally assumed that inflation will average only 2% per annum in the future. The yields on Canadian bonds have declined dramatically, as has the projected GDP growth, the result suggesting that the same balanced portfolio will yield only about 5% (after fees) in the future, resulting in a lower real return of only 3% per annum (after fees).

[2] For a discussion of the need to update or eliminate the Factor of 9, see also William B.P. Robson, "Rethinking Limits on Tax-Deferred Retirement Savings in Canada." C.D. Howe Institute, 2017.

While various combinations of assumptions can be considered, we could suggest a range of new equivalent "Factors" ranging from 11 to 15, as demonstrated by the table below. The defined benefit (DB) formula used in the scenarios below was a 5-year average formula at the rate of 1.3% up to the 5-year average YMPE and 2% above the 5-year average YMPE. The DB pension is assumed to be indexed in retirement annually at the rate of increases in the Consumer Price Index less 1%, and payable unreduced from age 60 onwards. The corresponding contribution rate under a defined contribution comparator plan was at a rate of 1.3% of earnings up to the YMPE and 2.0% above the YMPE.

Scenario	Mortality	Discount rate	Inflation	Salary escalation	Retirement age	Ratio of Actuarial Value of DB benefits at Retirement over Final DC balance
(a) Original basis	GAM83	7.5%	4.0%	5.5%	63	9.3
(b) Updated mortality	CPM14 generational with scale CPM-B	7.5%	4.0%	5.5%	63	10.8
(c) Updated economic assumptions (optimistic)	CPM14 generational with scale CPM-B	5.5%	2.0%	3.5%	63	11.2
(d) Updated economic assumptions (pessimistic)	CPM14 generational with scale CPM-B	4.5%	2.0%	3.5%	63	15.0
(e) Updated economic assumptions (moderate) and age 65 retirement	**CPM14 generational with scale CPM-B**	**5.0%**	**2.0%**	**3.5%**	**65**	**11.9**

In the row (e) we illustrate a scenario assuming a retirement age of 65, reflecting the increases in longevity and the likelihood that the next generation of workers will end up retiring at a later age than the previous generation.

Using the moderate set of economic assumptions and an age 65 retirement date would suggest a "Factor of 12". This would not even reflect the significant value of early retirement subsidies available under DB plans. We note, however, that many would argue that a 5% net investment return may be an optimistic assumption for a DC pension plan under current economic conditions. That being said, a "Factor of 12" is certainly more representative of current economic and demographic realities, even if it doesn't fully reflect the expense differential typically associated between large DB plans and smaller DC Plans or retail RRSP investment options.

It should be pointed out that in order for the tax system to be internally consistent, raising the "Factor of 9" to a "Factor of 12" would have the following main consequences:

- The money purchase limit would increase from its roughly $27,000 level to roughly $36,000; and
- The RRSP Deduction Limit and PA calculation rule for DC Plans, in percentage of earnings, would increase from 18% to 24%, allowing DC plans and group RRSP arrangements to be on a more similar footing to the DB model.

2) TRANSFER VALUES – REPEAL REGULATION 8517 LIMITS

Allowing Canadians to invest in tax-deferred savings and pension arrangements during their working careers is desirable. Members who terminate their employment and choose the option of transferring the commuted value of their DB RPP to a DC arrangement (such as a Locked-In Retirement Account (LIRA), are subject to the "Maximum Transfer Value" limits outlined in Income Tax Regulation 8517. In many instances, particularly in low interest rate environments, the result is that the member will be forced to take a large portion of the commuted value of their pension benefit in cash, which is subject to immediate taxation.

Given registered pension plans are tax-deferred arrangements, this forcing of immediate taxation on the lump sum versus deferred taxation of the benefits received during retirement is punitive. It is also contrary to the general goal of reserving lump sum value of pension benefits exclusively for retirement income. The cash distribution of retirement savings can result in depriving Canadian plan participants of a timely or comfortable retirement.

For individuals under age 50, the maximum transfer value uses the Factor of 9. For individuals age 50 and over, the factor varies with age. These factors may have been appropriate three decades ago when originally established, but are no longer supportable, for the same reasons as explained in Section I above.

When large portions of pension benefits are paid in cash, it's extremely unlikely that the individual will be able to replicate the benefit that would have been paid from the DB pension plan. Portability options to plan members should not be subject to rules that result in materially smaller pension benefits that will be available during retirement.

The following table illustrates the impact on a member who chooses to transfer the commuted value of their pension upon termination to a LIRA. Unless this individual is an extremely savvy and lucky investor, it is highly unlikely that he or she will achieve the investment returns necessary to make up for the loss of funds due to immediate taxation.

Age	Annual Pension	Annuity Factor[3]	Commuted Value	8517 Factor	Maximum Transfer Value	Amount Subject to Immediate Taxation
32	$14,000	18.5	$259,000	9.0	$126,000	$133,000
48	$58,300	22.3	$1,300,090	9.0	$524,700	$775,390

[3] Assumptions: Fully indexed plan (including in the deferral period), optimal age / unreduced benefits at age 60, fully subsidized 60% joint and survivor normal form, CIA July 2019 discount rate assumptions of 1.2% for 10 years, 1.3% thereafter for a fully indexed plan with mortality table CPM2014 with generational projection using scale CPM-B, 50% male unisex (spouses same age as member).

Consideration should be given to repealing Section 8517 of the ITA Regulations. RPPs should maintain their special status as arrangements with taxation deferred to retirement years. Plan members who exercise portability rights should not be disadvantaged in comparison to those who choose to leave pension entitlements with former employers.

We acknowledge that the transfer values determined under pension legislation and guidance from the Canadian Institute of Actuaries use discount rates far less than assumed in the PA equivalence factor. Using the assumptions described in Section I above (age 65 retirement, 5% discount rate, 2% inflation, 3.5% salary escalation until pension commencement and CPI-1% inflation adjustments in retirement), the annuity factors would be as follows:

Age	Annuity Factor
40	11.5
45	12.3
50	13.1
55	14.0
60	15.0
65	16.0

3) TAX REFORMS TO ADDRESS INCREASED LONGEVITY

A. Raise Mandatory Retirement Income Commencement from Age 71 to 75

In a study published in *The Lancet* in February 2017, a girl born in Canada in 2030 is forecasted to live to 87 years and a boy to nearly 84 years. The life expectancy for females born in 2010 is nearly 84 years, and just over 79 for males. Longer lifespans will inevitably change how we live and change our savings and retirement goals. However, the ITA forces Canadians to start withdrawing from registered retirement vehicles not later than the end of the calendar year in which the individual attains age 71. Given current longevity projections, and the fact that investment returns and interest rates have been and may continue to be at low levels, the 71 age restriction for tax deferrals should be gradually raised to age 75 over time to provide more flexibility for Canadians saving for retirement[4].

B. Permit Longevity Pooling Through Group Self-Annuitization Arrangements

In previous ACPM papers and submissions, we have recommended that the ITA be amended to permit uninsured variable payment lifetime annuities (VPLAs) to be offered either within Capital Accumulation Plans (CAPs), or as related or unrelated group retirement income options. With an uninsured variable payment lifetime annuity, longevity and investment risk can be pooled, but not insured. Provided that adequate disclosure is provided to retirees, this option has the potential to significantly reduce the longevity risk currently faced by CAP retirees without creating a funding risk for the plan sponsor or provider.

[4] Proponents of this reform include William B.P. Robson and Alexandre Laurin, as discussed in "Less Debt, More Growth: A Shadow Federal Budget for 2019." C.D. Howe Institute, 2019.

We welcome recent efforts announced in the 2019 Federal Budget in this regard, but believe the measure should be addressed through the ITA first, and that each pension jurisdiction that wishes to allow VLPA as a settlement option (for locked-in or non-locked-in) funds may elect to do so. Having multiple versions of a VLPA would reduce the odds of success for this measure. At the very least, consideration should be given to allowing provinces to adopt a common VPLA framework for those who access it through a PRPP.

4) TAX REFORMS TO ASSIST CAPITAL ACCUMULATION PLANS (CAPS)

Over the past two decades, we have seen a rapid growth of CAPs including Group RRSPs, DPSPs and even Group TFSAs. As CAP members start to approach and enter retirement, ACPM believes that there is both an opportunity and need to (i) develop decumulation products and services that will produce better outcomes and (ii) assist CAP plan sponsors in correcting errors in plan administration that inevitably occur from time to time.

A. Equalize the Taxation of Pension Income from Various Retirement Savings Vehicles

When variable DC benefits were created, a new form of retirement income was created. The *Income Tax Regulations* define variable benefits as "lifetime retirement benefits". Lifetime retirement benefits, whether paid from a DB or DC pension plan, must be periodic and cannot start until retirement. Taxes on variable benefits are calculated, withheld, and remitted to CRA in the same manner as DB pension payments.

Two years later, the ITA was amended to permit pension income splitting between spouses. As part of this change, the ITA was amended to add variable benefit payments to the definition of "pension income" but not to the definition of "qualified pension income". DB pension payments, however, were included under both definitions. As a result, DB pension plan members can claim the pension income deduction and split payments with a spouse immediately on retirement, whereas DC pension plan members must wait until they reach age 65.

The only difference between a variable benefit payment and a DB pension payment is that one is flexible and the other is not. Both are periodic payments of lifetime retirement income that cannot start until the member qualifies for retirement and terminates employment. An "age 65" limit is therefore not required to ensure that the taxpayer is retired. There is no reason to characterize the payment of periodic retirement income from DC and DB pension plans differently.

If one accepts that decumulation outcomes could be improved by encouraging DC pension plan sponsors to offer group retirement income options, then the payment of retirement income directly from a DC plan to its retirees in the form of variable benefits should be encouraged. Removing the disparity in taxation that currently exists between DB and DC retirees receiving retirement income directly from their plans would support this result.

Furthermore, it is difficult to understand why retirement income from RRIFs or LIFs would not deserve the same tax treatment; therefore, we would also recommend that such income be treated in the same fashion. As retirement income from Group RRSPs is often provided by way of a transfer to RRIFs or LIFs, revising the pension splitting rules to apply consistently for RRIFs and LIFs will further even the playing field between registered DC pension plans and other CAPs.

B. Assisting the Rectification of DC Pension Plan (DCPP) Contribution Errors

- ***Over-contributions to DCPPs***

Over-contributions arise under a DCPP for a variety of reasons. For example, an employer may change payroll providers, and the payroll provider cannot or does not program the ITA contribution limit correctly, resulting in employer and/or employee contributions continuing past the money purchase limit or being in excess of the contributions permitted by the plan text. This is not always discovered in the same tax year as the over-contribution occurs, leading to the need to refund contributions to maintain compliance with the plan text and the ITA.

The Canada Revenue Agency (CRA) has issued some guidance on refunds of over-contributions and 2014 amendments to the ITA provided some relief if the contribution is refunded by the end of the year following the year it was made, but there is little guidance on the overall process of handling a refund. For example, in the case of a member over-contribution, it is not always clear whether the employer must issue an amended T4 with a revised PA, and whether the deducted contributions reported on the prior year T4 must be amended.

In particular, we are not aware of any published guidance addressing how to handle a member who terminates and transfers his or her account balance out of the plan before the over-contribution is identified (i.e. treatment of the over-contribution that was transferred to the individual's RRSP: what are the obligations of the plan administrator who paid the over-contribution and the financial institution who is holding it? How does the employer retrieve an employer over-contribution held in the individual's RRSP?).

Due to the lack of published guidance from the CRA on how to handle over-contributions to a DCPP, plan administrators must separately and in each case confirm with the CRA the steps CRA expects to be taken and/or approves to correct the problem. This process can result in administration expenses that are disproportionate to the amount over-contributed. A clear policy from the CRA on what plan administrators and employers are expected to do from a tax and registered plans compliance perspective would be of great assistance to administrators.

- ***Under-contributions to DCPPs***

Under-contributions can also arise from time to time due to a variety of inadvertent administration errors. Most commonly, this may be due to missed enrolment for members who must serve a waiting period or otherwise meet an eligibility condition in order to enrol, but can also be due to the challenges faced when administering situations that require manual intervention, such as continued contributions for employees on STD who are not receiving 100% of their earnings or other employees on leaves of absence.

Unlike the PSPA mechanism for DB plans, there is no mechanism under the ITA for making retroactive contributions in a current year that are allocated to prior years. All contributions made in a year must count towards the PA for the year in which the contributions are made. This limit often prevents an administrator and plan sponsor from making the employee whole in the same year that the error is discovered. ACPM recommends that that ITA be amended to explicitly permit retroactive catch-up contributions, up to the member's PA limit for the year to which the catch-up contribution relates, in the case of administration errors.

Even if the ITA is not amended, clearer guidance from the CRA would assist plan administrators. In the past, administrators have received inconsistent information from the CRA about whether CRA approval is required for catch-up contributions. In some cases, administrators were told that approval is required for each contribution, and in other cases, administrators have been told that amending the plan to include a general provision permitting catch-up contributions is sufficient. In a large plan, seeking CRA approval for each missed contribution would be onerous for both the plan administrator and the Registered Plans Directorate.

Clear guidance from the CRA on such issues as (i) whether CRA approval is required or not in order for catch-up contributions to be made, and (ii) the payment of "interest" or "lost investment returns" where the missed contributions are the fault of the administrator and/or employer, and the administrator and/or employer wants to make the employee whole, would assist administrators bring their DCPPs back into compliance with their terms while respecting the ITA rules.

5) TAX REFORMS TO ACCOMMODATE TARGET BENEFIT PLANS (TBPS)

As we noted in our *Target Benefit Plan Paper* published in 2012[5], there are two possible approaches under the *ITA* to apply tax rules and limits to TBPs: (i) apply the DB tax rules (which are benefits focused), or (ii) apply the DC tax rules (which are contributions focused). On the one hand, we noted that the DC tax rules would provide an element of simplicity to plan administration, as PAs would be simpler to calculate and there would be no need to administer PARs, PSPAs, the DB tax limit, etc. Many TBP administrators would see this as an attractive feature of a TBP. On the other hand, employing the DB tax rules, an employer (and plan members) could periodically elect to contribute additional funds to make up a deficit or to reduce contributions using a going-concern surplus, which would also be attractive features of a TBP.

We see benefits to both approaches. Therefore, rather than forcing TBPs to be treated as DB plans under the tax rules, we believe that administrators of TBPs should be given the choice to adopt the DB tax rules or the DC tax rules (both with some modifications) based on their individual sustainability levers and circumstances.

[5] ACPM Target Benefit Plan Paper dated March 2012.

In our view, TBP administrators should make their election at the time of establishment or conversion and be permitted to apply to the Minister of Finance or the CRA to elect the alternative treatment similar to the rules currently in effect for specified multi-employer plans (SMEPs)[6].

Each TBP would consider a number of factors in order to determine its election of DB versus DC tax treatment. For example, the election of the DC tax rules would be appropriate for a TBP that has a fixed contribution formula that does not exceed 18% of compensation, where the lever to ensure the sustainability of the TBP would be to reduce benefits (not increase contribution levels). In contrast, the DB tax rules would be more appropriate for a TBP design that focuses on the plan's base benefit formula and maintains the level of benefits (or require contributions in excess of 18% of compensation), where the lever to ensure the sustainability of the TBP would be to adjust contribution levels.

In our view, permitting TBPs to elect the DB or DC tax rules at inception or conversion (and with the limited ability to change that election on approval from the Minister or CRA) would not require significant changes to the current provisions of the ITA. Our recommended reforms to the ITA to accommodate TBPs are set out below.

A. Recommended Reforms to the DB Taxation Rules

***PA/PSPA/PAR rules*:** PAs for TBP benefits should be determined on the basis of the actual benefits being accrued, rather than on the specified target benefit. TBPs should be exempted from reporting PSPAs in respect of reversals of past reductions in accrued base benefits. Alternatively, the rules should require that a PAR be reported when benefits are reduced.

Employee Contribution Limit: We recommend exempting TBPs from the limit on employee contributions to a DB plan under the tax rules.

Normal Cost Contributions: We do not recommend limiting TBP contributions to no more than normal cost funding requirements plus 25%, regardless of whether the pension standards legislation prescribes a Provision for Adverse Deviation (PfAD) or not. The 25% limit was developed to be applicable to DB plans with implicit funding margins. For example, a 1% Margin for Adverse Deviation (MAD) built into a going-concern discount rate may be equivalent to 20% to 25% additional normal cost, depending on the duration of normal cost.

[6] To avoid exploitation of the advantages of the DB versus the DC tax rules by electing back and forth between them, approval by the Minister or CRA of any subsequent election would presumably require a high threshold of justification to prevent this kind of election arbitrage such as on the basis of a significant change in the plan's characteristics, levers or economic circumstances. For example, a TBP might be set up with a fixed employer contribution, which would justify a DC treatment, and then future bargaining could change this to provide a corridor of X to Y% employer contribution that varies with the plan's funding level of the target benefit. We anticipate that TBPs will rarely be motivated to elect to change their tax treatment due to the significant complexity in administration this would cause (i.e. part of a member's service in the plan is determined on one basis and the rest on another).

Subjecting TBPs to the normal cost plus 25% could limit the sustainability of these plans in the long run, which would defeat the policy basis for offering them. We propose, therefore, a much higher limit (e.g. 150%) or allow the PfAD to be considered additional normal cost akin to the additional normal cost in a comparable MAD.

Surplus Rules: We recommend a change to the requirement that contributions cease once a DB plan's going-concern surplus reaches 25%. Firstly, as noted above, an explicit PfAD can be equated to a comparable MAD. Accordingly, the PfAD should be considered a liability rather than a "surplus". Secondly, if a TBP's funding excess (above the PfAD) exceeds 125%, rather than restricting employer contributions, we would recommend the rules require a cessation of 50% of normal cost (including PfAD), apportioned in whatever manner provided for under the plan's terms between employee and employer contributions.

Transfer Limits: In our view, the DB tax rules should be amended to specify that all potential benefits under the TBP and the funding policy for the plan be used to determine the maximum transfer limits, to the extent they remain a feature of the Income Tax Act.

Other Changes: We also recommend changes to the DB tax rules to exempt TBPs from the "equal and periodic pensions" rule to ensure a TBP can both reduce and increase pensions in pay, as necessary.

B. Recommended Reforms to the DC Taxation Rules

***PA/PSPA/PAR rules*:** A TBP that elects to calculate PAs using the DC rules would be restricted in annual funding to the applicable DC contribution limits. Accordingly, PSPAs or PARs would not be required when benefits are adjusted up or down.

***Employee Contribution Limit*:** Same comments as for DB Taxation Rules.

***Normal Cost Contributions*:** These would be governed by the applicable DC contribution rules.

***Surplus Rules*:** A TBP using the DC Taxation Rules should be exempt from surplus limits completely since the contributions into the plan are limited by the applicable DC contribution rules.

***Transfer Limits*:** Since contributions into the plan are limited by the DC contribution rules, there is even stronger arguments why the maximum transfer limits (if any) should not apply.

***Other Changes*:** Same comments as for DB Taxation Rules. We could also envisage target benefit plans using the DC Taxation Rules adopting the new VPLA framework for managing the lifetime retirement income option elected by retirees.

6) REFORM ANNUITY RULES: DEFERRED ANNUITIZATION

As discussed previously, we had recommended that the ITA be amended to permit individuals to allocate a portion of their deferred tax savings beyond the end of the year they attain age 71 (in a similar approach to the QLAC in the U.S.). We are pleased with the announcement in the 2019 federal budget on Advanced Deferred Life Annuities (ALDAs) and look forward to more details on these new vehicles.

7) OTHER TAX REFORMS FOR REGISTERED PLANS

A. Pre-retirement Death Benefits under DB RPPs: Amend Regulation 8503(2)(i)

Under ITA regulation 8503(2)(i), an RPP cannot pay lump sum death benefits and pension payments although the pension standards legislation[7] allows for this. Some pension plans have a provision that allows dependent children to receive a temporary monthly pension while they remain dependent (typically until they finish university). However, the full commuted value is still owed on pre-retirement death, so it is adjusted downwards for the value of the temporary pension stream. Even though the temporary pension and the lump sum commuted value are both RPP benefits, they can't both be paid from the RPP given the restrictions under 8503 which leads to significant administrative challenges. Regulation 8503 should be amended to accommodate this design feature permitted under pension standards legislation.

B. Review Minimum Withdrawals from Registered Retirement Income Funds (RRIFs)

The current rules requiring minimum annual withdrawals from RRIFs contribute to the problem of Canadian retirees' income insecurity since Canadians who have retirement savings in RRSPs are required under the current rules to convert their savings into RRIFs. The RRIF withdrawal rules deplete the assets of a RRIF by age 95, and often force retirees to take funds from their RRIFs before they need or want to, resulting in many Canadians outliving their retirement savings.

The RRIF withdrawal rules have not kept pace with increasing longevity rates, time spent in retirement and reduced access of the average Canadian to workplace retirement plans. When the RRIF withdrawal rules were first introduced in 1978, and increased in 1992, life spans and time spent in retirement were much shorter than today. Today, Canadians on average spend much more time in retirement than they did in 1978 and 1992 and are much more likely to run out of money in their later retirement years.

We are pleased that the ITA minimum withdrawal rates were reviewed and reduced in 2015 for individuals over age 70. We encourage CRA to proactively review these minimum withdrawal rates periodically to reflect any future changes in longevity.

[7] see, for example, Section 48 of the *Pension Benefits Act* (Ontario).

C. Proposed Changes to Tax Rules Relating to Tax-Free Savings Accounts (TFSAs)

Currently, an immediate annuity or deferred annuity is not a permitted investment under a TFSA. If an individual wants to use TFSA assets to buy an annuity, it is now necessary to withdraw assets from the TFSA and effectively purchase the annuity with non-registered assets (see above). This eliminates the exemption from tax on withdrawals from the TFSA. ACPM supports the inclusion of immediate annuities and deferred annuities as permitted investments within a TFSA. This would provide another way of funding a longevity annuity for a member on a tax-neutral basis.

8) CONCLUSION

The Canadian retirement system has undergone significant change and transition over the roughly three decades since the registered plan taxation system went through its initial major overhaul in the early 1990s. While some changes have been made since that overhaul, the federal and provincial governments have introduced and implemented significant changes to improve the retirement system and to facilitate innovations in the plan design, such as the introduction of TBPs, shared risk plans, and variable benefits from DC pension plans. Improvements continue to be considered to address current and emerging challenges, including low interest rates and increased longevity projections. The ITA rules applicable to registered plans must be modernized and updated to keep pace with today's socioeconomic environment, Canadians' increased life expectancy and innovations in retirement plan design. The implementation of the ITA and tax policy reforms identified by ACPM above would achieve these important goals. The time is now to reform the tax rules applicable to registered plans.