Advocis
390 Queens Quay West, Suite 209
Toronto, ON M5V 3A2
T 416.444.5251
1.800.563.5822
F 416.444.8031
www.advocis.ca

May 14, 2010

Retirement Income Adequacy Consultation
c/o Minister of Finance
Fiscal Policy Division
P.O. Box 6000
Fredericton, NB E3B 5H1

Dear Sir or Madam:

Re: New Brunswick Consultation on Retirement Income Adequacy

Advocis, The Financial Advisors Association of Canada, is Canada's oldest and largest voluntary professional membership association of financial advisors and planners. We represent life and health insurance licensees and mutual fund and securities registrants across the country. Advocis members pride themselves on the service and advice delivered to individuals and the business community, particularly small-and medium-sized companies through the provision of professional financial advice and insurance and financial service products. This includes group RRSPs, deferred profit sharing plans and defined contribution ("DC") plans (hereinafter referred to collectively as "Capital Accumulation Plans or "CAP Plans") and defined benefit ("DB") plans.

Advocis has established a Retirement Income Adequacy Committee whose mandate is to identify retirement and pension issues that are of concern to Canadians and to promote a sound retirement income system in Canada including reforms to improve retirement income adequacy for Canadians now and in the future.

Pension coverage, retirement income adequacy and the necessary reforms are major public policy issues. We commend the New Brunswick Government for making it a priority to consult with its citizens on this important issue.

Retirement planning is a priority for most Canadians and more than 10,000 members (over 250 who operate in the Province of New Brunswick) work with individuals, families and businesses in achieving their financial objectives. Our members provide comprehensive financial advice to Canadians through all stages of their lives including estate and retirement planning, wealth management, risk management, tax planning, employee benefits, critical illness and disability insurance. Our members provide retirement planning and investment advice to employees with CAP Plans, with RRSPs and TFSA's and our members also establish and administer CAP Plans and DB plans for small and medium sized businesses.

General Comments

Advocis would like to stress that a broad focus encompassing all types of retirement savings is required. Advocis has examined existing barriers to establishing and maintaining pension plans and incentives to encourage small and medium sized employers to participate in pension plans. We have looked at the important aspects of the retirement income system in Canada and we wish to offer some practical solutions for improvement. Last September Advocis commissioned a study entitled "*Encouraging Small and Medium Sized Firms to Participate in Pension Plans*"[1].

The study confirms that:

a. The number of Canadian employees who are participating in any form of employer sponsored pension plan has been declining;
b. Only one-third (35%) of Canadian employees have an employer-sponsored pension plan, with coverage being only 24% in the private sector; and
c. Only one-third of Canadians will have adequate income at retirement.

The study examined barriers to establishing and maintaining pension plans and incentives to encourage employers to participate in pension plans. The report makes practical recommendations to support the establishment of more pension plans and increased retirement incomes for Canadians.

The study concluded that the most appropriate type of employer sponsored pension plan is a defined contribution plan, especially for small and medium sized business enterprises. Public policy should focus on how to improve the regulatory environment for such plans. Indeed, Advocis believes that public policy should reinforce the strong financial attributes of all CAP Plans.

Advocis has a number of recommendations (set out below) to reform the pension and retirement income system so as to remove barriers to the establishment of CAP Plans and create incentives that will improve pension coverage and the retirement income system for all Canadians.

Advocis strongly believes that professional financial advice is needed by the majority of Canadians in order to lead to good consumer financial outcomes, not only in the areas of retirement income savings, but in a whole host of other areas as well such as planning for a child's education and long-term health care needs. Public policy should foster an expansive role for professional financial advice in order to ensure that Canadians can meet their retirement income and other financial goals. Canadians should not be expected to serve as their own financial experts but should have access to professional financial advice so that they have safe and adequate retirement savings.

Advocis would like to stress that what is required is the strengthening of existing means through needed reforms. This would include, but is not limited to, a combination of higher and more flexible tax assisted contribution limits, longer accumulation phases past age 71, deferred and

[1] Gunderson, Morley and Wilson, Thomas, 2009. "Encouraging Small and Medium Sized Firms to Participate in Pension Plans." Prepared for Advocis: The Financial Advisors Association of Canada.

reduced requirements for income commencement and substantially more "user friendly" rules for employer sponsors which will improve the system.

Advocis supports a national approach to reforms to the third pillar of the retirement income system as this will allow all Canadians to have the same opportunities to save and invest and be adequately prepared for their retirement. A national approach involving both the federal and provincial governments in harmonizing efforts would also likely lessen regulatory compliance costs and burdens for participants who operate in more than one province. Advocis urges governments to give serious consideration to harmonizing regulations, particularly with respect to locking-in rules, between provinces and federally to reduce complexities and costs for employers and employees.

Advocis believes that it is important to increase pension or retirement savings coverage among private sector workers and that this should be a policy priority for the New Brunswick Government. Employers and employees should be encouraged to participate in retirement savings plans and barriers should be removed and incentives put in place which will facilitate employers offering retirement savings plans for their employees and result in more employees being members of a plan.

Advocis urges the government to include as a principle that Canadians should have the choice of how they accumulate savings for their retirement.

Solutions should target those at risk of not being able to meet their non-discretionary expenses in retirement. To achieve a standard of living that is similar to that enjoyed during pre-retirement, the measurement of replacement rate of income is generally utilized. It should be stressed that the correct replacement rate is not a one-size fits all answer and depends on what the individual's standard of living was pre-retirement, and what a person's goals, expectations and plans are for their retirement years.

Policy should also recognize that people may choose to retire "early" or may choose to continue to work beyond the traditional retirement age of 65.

Advocis will provide comments on the following questions in the consultation document: 1, 2, 3, 5, and 7.

<u>Advocis' Response to the Questions in Consultation Document</u>

1. Are changes needed to further strengthen Canada's retirement income system?

Advocis believes that the New Brunswick Government should give serious consideration to implementing private sector pension and retirement income reforms so that pension coverage and retirement income adequacy can be improved.

The modernization of pension standards legislation to reduce complexities and costs to employers and harmonization of the legislation between provinces, will encourage more employers to offer a pension plan to their employees.

Reducing barriers will increase pension coverage but incentives to encourage employers to offer these plans are also required. Otherwise, pension coverage will not be increased as much as it otherwise could be. Governments should explore tax incentives to encourage small and medium sized businesses to offer pension plans to their employees.

Employers who are well-versed on the issues associated with retirement planning tend to be more interested and we would suggest more inclined to offer benefits to employees.

Advocis strongly believes that tax reforms should be implemented to promote pension coverage. Through tax reforms DC plans can be placed on a more equitable footing with DB plans. There are also reforms to RRSPs that can be made to improve that form of retirement savings. Our recommendations are:

a) Contribution limits for CAP Plans and RRSPs should be increased to help participants in CAP Plans and RRSPs achieve retirement incomes comparable to participants in public sector DB plans. As a first step, contribution limits should be increased to 20% of earned income and the maximum dollar limits should continue to be indexed. Further increases in these limits should be a priority for future fiscal policy.

b) The current two year 100% vesting rule should be replaced by gradual vesting over a 3-year period from the date of plan enrolment, with 1/3 at the end of the first year, 2/3 at the end of the second year and full vesting at the end of the third year (the employees contributions are, of course, fully vested from the beginning). This would provide employers with a greater incentive to establish a pension plan. The employee would also have a greater incentive to remain with the company over a longer period, while at the same time, providing some compensation to employees who leave the company before the three-year period. With this approach, employees always receive their money plus a share of the employer's money at termination of employment. Non-vested forfeitures should only be used to offset an employer's current service contributions.

c) While it is recognized that the tax assisted private retirement planning system in Canada results in significant deferrals, ultimately the tax will be paid. Accordingly, administration rule amendments such as: a reduction or change in minimum withdrawal rates; a longer window for deferral, i.e. to age 75 and the ability to defer tax for prescribed pension amounts while still actively employed (ie voluntary private and public pension rollovers) would create larger pools of capital for the individual to supplement their retirement income at a later date, and for governments to ultimately tax.

d) Contributions to retirement savings plans should be determined on a life-time average basis in order to not penalize those individuals with fluctuating incomes and individuals whose income increases rapidly later in their working lives. This would allow any earned income in excess of the contribution limit in a year to be carried back or forward to create additional contribution room for years where earned income was below the limit. Any taxable withdrawals from an RRSP or CAP Plan in a year would create future RRSP contribution room. This would allow individuals with career interruptions to make up for years with little or no income by permitting extra contributions in subsequent years of high earnings.

   For DC plans, employees and employers should be allowed to make past service contributions based on prior year's earnings up to the limit of the individual's unused RRSP contribution room.

   This would also allow individuals to draw down their pension savings to finance other needs (as is currently allowed with RRSPs) without permanently impairing their ability to save for retirement.

e) The age limit for contributions to retirement savings plans should be increased from age 71 to 75, implemented over a 4-year phase in period given the fact that people are living longer and continuing to work post-retirement.

f) The required withdrawal of amounts upon retirement from locked-in retirement accounts should be lowered to reflect the fact that interest rates are low, Canadians are continuing to work post-retirement and are living longer.

2. This paper describes a number of possible options for increasing retirement savings in Canada. What do you feel are the merits of the various options? Do you have particular concerns with any of these options?

(i) Expansion of the existing Canada Pension Plan (CPP)

Advocis does not, at this time, support expansion of the CPP as a way to improve retirement income adequacy for future Canadian retirees.

Advocis urges the government to allow private sector pension reforms to be implemented and given a chance to succeed prior to giving serious consideration to changes to Pillar 2 (CPP) of the retirement income system.

In addition, the Federal Government and many provinces' deficit situations and the existing tax burden for employees and employers does not support the imposition of an additional tax burden on employers or employees that would be required to expand the CPP.

(ii) Creation of a voluntary defined contribution supplement to the CPP

Advocis believes that governments should implement reforms to the existing private sector pension and retirement savings system (Pillar 3) before implementing any new retirement savings structure. Such reforms could include allowing employers to auto-enroll employees in a CAP Plan, with the ability of the employee to opt out, should they choose to do so.

Advocis is not in favour of a government legislated supplemental pension plan as described in the consultation paper that does not allow for a level playing field with the private sector and that may crowd out existing retirement savings options for consumers and employees.

The costs to set up and run the plan will be significant for taxpayers, including those who do not wish to participate in such a plan. Such costs should not be incurred at this time before allowing reforms to the existing system being implemented.

(iii) Modernization of pension standards to improve flexibility in pension plan design

The modernization of pension standards legislation so that complexities and costs to employers are reduced as well as harmonizing the legislation between provinces, will encourage more employers to offer a pension plan to their employees. This will likely increase pension coverage.

A national approach involving both the federal and provincial governments in harmonizing efforts would likely lessen regulatory compliance costs and burdens for participants who operate in more than one province. Advocis urges governments to give serious consideration to harmonizing regulations, particularly with respect to locking-in rules, between provinces and federally to reduce complexities and costs for employers and employees.

Reducing barriers will improve pension coverage but incentives so as to encourage employers to offer these plans are also required. Otherwise, increased pension coverage will not be as great as it otherwise could be. Governments should explore tax incentives for small and medium sized businesses that choose to offer pension plans to their employees.

Employers should themselves be recognized for their sponsorship of pensions. Employers who are well-versed on the issues associated with retirement planning tend to be more interested and we would suggest more inclined to offer benefits to employees.

(iv) Tax Reforms – Changes to the Income Tax Act (Canada)

Advocis recommends various tax reforms which are set out in the answer to Question 1 (above).

3. **Do you think that additional *mandatory* measures are required to ensure adequate retirement savings in Canada? Do you think this would be better accomplished thorugh expanded CPP coverage, through mandatory enrolment in a new supplementary plan, or a combination?**

Advocis strongly believes that Canadians should have the choice of how they accumulate savings for their retirement and that government should not implement reforms that substantially alter the balance between the current three pillars of the retirement income system and would mandate how Canadians save.

Private sector reforms should first be given a chance to be successfully implemented before potentially costly reforms are made to the second pillar of the income system or government legislated supplemental plans are introduced.

Advocis is not in favour of a government legislated supplemental pension plan as described in the consultation paper that does not allow for a level playing field with the private sector and that may crowd out existing retirement savings options for consumers and employees.

The costs to set up and run the plan will be significant for the taxpayers of those provinces who join, including those who do not wish to participate in such a plan. Such costs should not be incurred at this time before allowing reforms to the existing system being implemented.

Advocis does not, at this time, support expansion of the CPP as a way to improve retirement income adequacy for future Canadian retirees. The Federal Government and many provinces' deficit situations and the existing tax burden for employees and employers does not support the imposition of an additional tax burden on employers or employees that would be required to expand the CPP.

5. **Employers play a critical role in Canada's retirement income system. However, the proportion of Canadian workers with employer-sponsored registered pension plans has been steadily declining for many years. How do you think these options would affect employers' participation in, and support for, the retirement income system?**

Governments should reduce barriers and provide incentives so that more Canadian will save for their retirement through private sector employer sponsored CAP plans.

Advocis believes that the reforms we are suggesting will provide Canadians with flexibility and choice with respect to private savings options as more employers will offer their employees the ability to save through a pension plan (including a CAP Plan). Advocis' recommended reforms would likely increase employers' participation in the third pillar of the retirement income system.

Advocis strongly supports reforms to the regime for CAP Plans, as these plans are the best type of pension plan for small and medium sized enterprises. There has been an increase in the percentage of DC Plans and other CAP plans and most of the substantial loss of membership in DB Plans has occurred because of plan conversions[2].

7. **Do you have any other ideas for measures that would help to improve Canada's retirement income system?**

In addition to the suggested reforms set out in question 1, above, Advocis also recommends the following changes to the OAS and GIS:

- Guaranteed Income Supplement (GIS) recipients should be permitted to claim non-refundable tax credits that eliminate the personal income tax that they would otherwise pay. This would reduce their effective marginal tax rate to 50% - the basic GIS claw-back. This reform would resolve the serious disincentive to saving through RRSPs or DC Plans that currently exists given the high post-retirement effective marginal tax rates.

- The Old Age Security (OAS) claw-back of 15% should be reduced to 10.5 percent, if not abolished. The OAS claw-back creates a dramatic ballooning of marginal and effective tax rates post-retirement. The OAS claw-back is a major deterrent for middle income working Canadians to continue to contribute to society through their work after age 65 and has an adverse incentive effect for retirement savings for some individuals.

We appreciate the opportunity to provide our comments to the government as it considers reforms to the retirement income system.

Yours sincerely,

Greg Pollock
President and CEO

Terry Zavitz, CFP, CLU, RHU, GBA, EPC
Chair, National Board of Directors

[2] Gunderson and Wilson at page 2-5.