THE INVESTMENT FUNDS INSTITUTE OF CANADA | L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

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August 5, 2016

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The Chair and Members
House of Commons Standing Committee on Finance
Sixth Floor, 131 Queen Street
House of Commons
Ottawa ON K1A 0A6

Dear Committee Members:

RE: **Pre-Budget Consultations – 2017 Federal Budget**

Thank you for the opportunity to present our recommendations for inclusion in the 2017 federal budget. As requested, our submission focusses on measures to increase the ability of Canadians to contribute to the country's economic growth: Tax relief for middle class Canadians through GST/HST reform and better access to Registered Education Savings Plans; support for retirement savings through reforms to registered savings plans, and measures to remove barriers experienced by Canadians with disabilities in accessing and using Registered Disability Savings Plans. Each proposal addresses issues that currently serve as barriers to the ability of Canadians to maximize their contributions to the country's economic growth by reducing their available income.

Supporting Economic Growth - Tax Relief for Middle Income Canadians through GST/HST Reform

Since the introduction of the GST in 1991, most financial services in Canada have been taxed under an exemption system. One notable exception to this rule is mutual funds, whose investors are fully taxed on the entire cost of "producing" a fund. This anomaly is the result of the way in which funds are structured, and of a failure by the 1991 architects of the GST to recognize and address the anomaly.

IFIC is asking that the federal government support Canadian savers by qualifying funds for a 100% rebate of the GST paid, consistent with how other financial services products are taxed. Should revenue considerations preclude this solution, a partial improvement would be to apply a pension-type rebate equivalent to 33% of the GST paid by investment funds.

Under Canada's GST exemption system, investors are not charged tax on the financial products and services they consume, and financial services providers cannot claim input tax credits on their taxable supplies. Since most financial products, such as GICs, are manufactured "in house", many of the production costs do not attract GST/HST and the charges to the end consumer include little GST/HST. However, the corporate structures used by most investment funds that enable pooling of investors' funds preclude full "in house" production.

The majority of investment funds in Canada are structured as trusts, with the authority to hire a management company to direct the fund's day-to-day affairs and hire other required services, such as a third-party custodian of the fund's assets. The unique structure for investment funds safeguards investors' assets, but this protection comes at an unseen price for the investor because, as suppliers of exempt services, investment funds are not entitled to recover the GST/HST paid to the fund manager. As a result, 100% of the GST/HST is a cost to fund investors, which reduces the net return on their investments. This amounts to a tax on savings for those investors who choose investment funds over other financial products in Canada.

A tax rebate provided to the investment fund would have the immediate effect of increasing an individual's accumulated savings and enhancing the savings returns, unlike other forms of tax reductions that are provided directly to an individual who may then choose to save or spend the money. This increase in accumulated funds would be reinvested in the capital markets, benefiting economic growth. In addition, a high proportion of investment fund savings are intended for retirement; therefore, the rebate will lead to higher retirement income levels, reducing dependency on public retirement income supplements such as OAS and the GIS.

Supporting Economic Growth – Increasing Education Savings

Canada's future economic growth will depend on a well-educated workforce. In order to increase education savings to help Canadians pay for post-secondary education, we recommend steps to improve awareness of available programs and improvements to several existing programs.

Improving Awareness of Existing Programs

A significant barrier to the use of existing programs is low awareness of the existence of RESPs and the availability of Canada Education Savings Grants and Canada Learning Bonds. We recommend the federal government budget include funding for a joint awareness campaign with common messaging and materials produced by the federal government that can be distributed through federal and provincial channels as well as providers, including advisors.

Removing Outdated Rules and Processes

Outdated rules may create disincentives for some Canadians to opening an RESP. We recommend the following rules be removed:

<u>Eliminate the 16/17 year old rule</u> which limits Canada Education Savings Grants for some older teenagers. It unfairly penalizes those who were unaware of the program or unable to participate due to financial circumstances. It also creates challenges for new Canadians who immigrate with teenagers. Any child under the age of 18 should be eligible for incentives.

Eliminate yearly maximums for CESG which punish families who were unable to save earlier in their children's lives. Families should be able to contribute up to the lifetime limit at any time before the child turns 18 and receive fully matched Canada Education Savings Grants.

Remove the requirement to verify proof of enrolment: Eliminate the requirement for paper-based verification of student enrollment. Education Assistance Plan withdrawals should be permitted based on a request by the client. The validity of the request can be verified by matching the T4A filed with Canada Revenue Agency by the provider with the matching T2220A (tuition tax receipt) from the school.

Remove the EAP Limit: Simplify and streamline the Education Assistance Plan by abolishing limits, such as the first 13 weeks rule that limits the amount of the payment during that period to $5000.00, and the formula for part-time studies.

Other Recommendations: Increase the RESP Contribution Limit and CESG Maximum:

The RESP contribution limit and Canada Education Savings Grant limit have not been increased since their inception in 1998. By comparison, average tuition fees in Canada have risen from $1,464 in 1990-91 to $6,348 in 2012-13. If the trend of unchanged grant amounts and continually increasing educational expenses continues, average Canadians will be discouraged from investing in higher education as the amounts they can save in their RESPs will be dwarfed by the educational expenses their children will face. The Canada Education Savings Grant lifetime grant maximum should be increased to $9000, and the $500 annual limit on the matching Canada Education Savings Grant should be removed, with a mechanism for regular ongoing review and adjustments for inflation and tuition increases.

Supporting Economic Growth – Facilitating Financial Security in Retirement

Group RRSPs are an accessible and efficient option within the retirement savings landscape - Canadians currently have more than $60 billion invested in group RRSPs. They fulfil many of the same goals as PRPPs – creating long-term savings through a workplace plan with minimal administration demands on employers, making them particularly appealing to smaller businesses. However, two related aspects of the current rules governing group RRSPs detract from their pension-like properties. Both can be addressed through minor rule changes, and one additional rule change would increase the likelihood of employee enrollment.

Locking in of employer contributions: In order for a workplace saving plan to be considered a pension plan by the Canada Revenue Agency, the employer contribution must be locked in; however, currently, there is no locking in ability for employer contributions to group RRSPs. The industry supports a change that would require employer contributions to group RRSPs to be locked-in, thereby encouraging adoption of group RRSPs by employers.

Exempting employer contributions from payroll tax: Because employer contributions are not locked-in, the Canada Revenue Agency treats employer contributions to group RRSPs as deferred income rather than as pension contributions. As a result, these contributions are fully subject to payroll tax, discouraging employers from offering an otherwise efficient workplace savings program. Locking in employer contributions and exempting the contributions from payroll tax would encourage adoption of group RRSPs by employers.

Auto-enrollment: Numerous studies in behavioural economics have identified auto-enrollment in retirement savings plans as a powerful way to increase employee participation. A change in the group RRSP rules to enable auto-enrollment similar to PRPPs would help the government attain its goal of getting more Canadians to save for retirement, while further strengthening group RRSPs as a desirable option for employers to offer to their employees.

Helping those with Disabilities Contribute to the Economy

Eligibility for the Registered Disability Savings Plan (RDSP) program is limited to a small portion of the population - an estimated 2 million people. However, based on statistics from Employment and Social Development Canada (ESDC), only 110,498 RDSP contracts were opened from the inception of the program to the third quarter of 2015. The most likely reason for this low take-up rate is the program’s complexity; it is easily the most complex of the existing registered programs to explain to clients and to administer.

A number of registration and eligibility issues pose barriers to firms that want to offer the program and to individuals who wish to set up plans. We recommend that the government work with the provinces, industry and other stakeholders to identify and eliminate some of these barriers. Some solutions we have identified include:

- Developing a link or document that an eligible beneficiary can present to his/her issuer of choice in order to confirm DTC eligibility.
- Improving communication with account holders regarding eligibility expiration dates.

- Clarifying rules on contractual competency and expanding the list of qualified family members who can act as account holders.
- Simplifying withholding tax provisions so that issuers can set up standard payment schedules for beneficiaries.
- Permitting more flexible and straightforward approaches to RDSP pay-outs
- Reducing the number of conditions required to administer a Specified Disability Savings Plan contract (for those who are medically determined to have a shortened life span)
- Removing the one account per beneficiary limitation to encourage access to the RDSP program.
- Increase awareness through collaboration with provincial governments and other stakeholders

By improving the financial security of Canadians with disabilities, the government will be contributing to better standards of living for these individuals, as well as increasing their ability to make meaningful contributions to Canada's economy.

We would be pleased to provide additional details on any of the above recommendations.
Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA

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