Submission to the House of Commons Standing Committee on Finance

Portfolio Management Association of Canada
August 2014

Attention: Christine Lafrance
Clerk of the Standing Committee on Finance
Tel: 613-992-9753
E-mail: FINA@parl.gc.ca

Re: House of Commons Standing Committee on Finance – Pre-Budget Consultations

The Portfolio Management Association of Canada is pleased to submit comments on recommended priorities for the **Federal 2015 Budget**.

As background, the Portfolio Management Association of Canada ("PMAC") represents over 180 investment management firms from across Canada. Our Members invest the assets of individual Canadians who are saving for retirement and the assets of both traditional defined benefit pension plans and defined contribution pension plans. Many of Canada's largest pension plans and small employer pension plans hire our members to manage all or portions of their investment portfolios. In addition, individual Canadians who seek professional management of their savings, become clients of our members who set up custom portfolios for individuals based on their retirement goals, risk profile and financial objectives. Our members are from across Canada and manage retirement savings for Canadians in every province and territory. PMAC was established in 1952 and its members manage in excess of $900 billion assets (excluding publicly offered mutual fund assets). Our mission is to advocate the highest standards of unbiased portfolio management in the interest of the investors served by Members. This mission guides our advocacy objectives and focuses our government relations efforts on goals which ultimately benefit all Canadians.

We express our support for all of the themes identified for the 2014 pre-budget consultations. The focus of our comments will be on improving Canada's taxation and regulatory regimes.

We have 4 specific recommendations all focused on improving Canada's taxation and regulatory regimes and the end impact this will have on Canadians along with enhancing economic growth in Canada.

- **Continued Progress on the Cooperative Capital Markets Regulator**
- **Taxation Fairness for Canadian Investors**
- **Pension Innovation and Harmonization**
- **Financial Literacy and Investor Education**

Each of these is addressed in more detail below.

1) Continued Progress on the Cooperative Capital Markets Regulator

PMAC commends the Federal government and its provincial partners on its progress and commitment towards creating the Cooperative Capital Markets Regulator (CCMR).
We believe the creation of a CCMR is a major improvement to the securities regulatory regime in Canada and addresses the interests of Canada's investors and capital market participants. The CCMR is a major boost for investor protection and economic efficiency

that benefits all Canadians. PMAC has long advocated for a single common regulator and have consistently stated that the existing fragmented system is out of step with global standards and does not serve Canadian investors well. We urge the Federal government to continue working with the other provinces that are not yet participating to recognize it is in the best of all Canadians that they join as well.

2) Taxation Fairness for Canadian Investors

PMAC is focused on various tax advocacy initiatives that we believe are critical to improving Canada's taxation policy on investments and retirement savings. See below a summary of these initiatives and our key recommendations.

New Trust Loss Restriction Rules in Federal 2013 Budget. One of PMAC's key advocacy priorities this past year has been to advocate to the Federal government the impact of the trust loss restriction rules on investment funds and the end impact of these rules on Canadian unitholders.[1] We believe the broad scope of these rules and the negative impact they have on Canadians' investment managers and investors of these vehicles have been overlooked by the Department of Finance. The trust loss restriction rules impact fund activities that are neither tax motivated, nor abusive from a tax policy perspective.

Canadians are allocating billions of dollars toward saving for retirement in investment vehicles like registered plans (i.e. registered retirement savings plan (RRSP), tax-free savings account (TFSA) as well as other types of investment vehicles).[2] Many investors hold units in trusts that are registered investments or qualified investments in various savings vehicles such as RPPs, RRIFs, RRSPs, RESPs, and RDSPs. In many situations, it will not be possible to predict or control the occurrence of a trust loss restriction event and the resulting deemed taxation year end, which will negatively impact investors.

The application of the trust lost restriction rules to funds formed as trusts results in an unfair outcome for funds, fund managers and their investors where there is no intended tax abuse. Given the market turbulence in the last several years, investors are looking for trust in the industry and confidence in investments and in Canadian capital markets. The impact of these rules to investment funds will cause uncertainty, unease and will unnecessarily erode investor savings.

We recommend that investment funds be exempt from the application of the trust loss restriction rules. It is our view that the rules are not intended to catch ordinary course fund activities where there may be a shift in beneficial ownership and fund activity will be unduly compromised given the breadth and broad scope of the trust loss restriction rules.

Negative Implications of 150 Unit Holder Rule for Mutual Fund Trust Status. We believe the current threshold is too high and results in unfair and unintended tax

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[1] The trust loss restriction rules were announced in the 2013 Federal Budget and extend the application of the acquisition of control rules as they currently apply to corporations, to now also apply to trusts, including investment funds formed as trusts. A trust loss restriction event is triggered whenever a person becomes a majority-interest beneficiary as defined in the ITA. The objective of the trust loss restriction rules is to prevent arm's length loss trading transactions that have been developed and that purport to enable one taxpayer to access the unused losses of another.

[2] See Statistics Canada. Total contributions to registered retirement savings plans (RRSPs) amounted to $35.7 billion in 2012, up 3.8% from 2011. **$73.9 billion** — value of tax-free savings accounts in Canada as of June 2012 (up from $54.4 billion the year earlier), according to data from consulting firm Investor Economics.

consequences on retirement savings.[3] In addition, the rule limits new fund innovation, and reduces opportunities for Canadians and non-residents to invest in new funds which meet their needs. Lowering the 150 unit holder would ensure the development of, for example, new pooled funds. We recommend that the 150 unit holder rule to qualify for "mutual fund trust" status be modified to provide a "look through" for pension plans and group RRSPs such that each participant in the pension/group RRSP is counted as 1 unit holder, regardless if they invest in fund directly or via an insurance segregated fund.

Taxation on Investment Management Services. GST / HST is a consumption tax. In our view, building retirement savings is the direct opposite of consumption and, accordingly, we fundamentally disagree with the idea that Canadians should pay a tax on services designed to help them build retirement savings. We recommend that the Federal Government agree with the provincial governments to adopt the policy positions taken elsewhere in the world and exempt consumption taxes on investment management services generally (i.e. on savings) or in the alternative, to work with the provincial governments to remove or mitigate the additional and uneven provincial portion of HST immediately.

***Expansion of Designated Stock Exchange*.** Designation status in Canada is very important for Registered Retirement Savings Plan ("RRSP") investors, as securities listed on designated stock exchanges are eligible to be held in an RRSP. Securities listed on designated stock exchanges are also eligible investments for other popular investment vehicles such as Deferred Profit Sharing Plans and Tax-Free Savings Accounts (TFSAs). The Department of Finance's approach of using a prescribed list and application process to designate stock exchanges (DSE) is not effective in today's ever changing global economy and fast evolving investment environment. The addition of more exchanges on the DSE would provide Canadian investors with the opportunity to further diversify their investment portfolios and maximize the investment returns in their tax deferred accounts. In our view, the current limited list of 40 exchanges does not allow for proper risk diversification or optimum asset allocation. We recommend that a new and more robust framework be developed in order to reflect the evolving definition of emerging markets and allow for proper risk diversification in the asset allocation of Canadian retirement savings. The current DSE list effectively limits Canadians from investing their retirement savings in many companies listed on well respected, regulated and established exchanges in various parts of the world. We urge the Federal government to expand the DSE list with additional foreign exchanges in emerging markets.

3) Pension Innovation and Harmonization

PMAC is a strong advocate of pension innovation and believe that Canadians should have access to retirement savings options. Over the last few years, we have supported two new retirement savings vehicles: Pooled Registered Pension Plans (PRPPs) and Target Benefit Plans (TBPs). We commend the Government for its commitment to ensuring a secure retirement for Canadians and moving towards pension savings options that allow alternatives to current plans.

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[3] For example, if a Canadian had RRSPs in a fund that had 150 or more unit holders, it would be a qualified investment. If however, the fund dropped below the 150 level, the fund would no longer be a qualified investment for a Canadian's RRSP. This would also trigger a host of detrimental tax consequences including a 1% penalty tax per month to the RRSP annuitant on the book value of their investment in the fund simply due to the arbitrary event of dropping below 150 unit holders; before this drop, it was a qualified investment.

We believe the TBP Framework provides a workable alternative to current plan options (defined benefit (DB) and defined contribution (DC) plans) and provides a more long term sustainable option for retirement savings. The flexibility and hybrid nature of the TBP Framework may prove attractive to employers who are moving away from the risks of DB plans. The balanced responsibility of risk between employers and employees is an attractive model as the TBP's shared risk model provides a workable solution to the issues and costs associated with both DC and DB plans. We are also supportive of PRPPs and believe that PRPPs will increase the retirement savings options available to all Canadians and address the growing aging population in Canada.

Correspondingly, we believe that with pension innovation, harmonization of pension options should be a policy priority to ensure equal access to retirement savings options. We also strongly urge the Government to consider funding flexibility as a necessary priority with Canada's longer mortality rates.[4]

Finally, we encourage the Government to implement the modernization of the pension investment rules contained in the federal *Pension Benefits Standards Regulations* that was first proposed in 2009.

4) Financial Literacy and Investor Education

PMAC commends the Federal government on the appointment of Jane Rooney as Canada's first Financial Literacy Leader on April 15, 2014. We believe in a national strategy for financial literacy and investor education for Canadians. The focus of Ms. Rooney's mandate is coordinating and collaborating activities with stakeholders to strengthen the financial literacy of Canadians; we believe the Canadian investment community has an important role to play in this mandate and associations such as ours can provide key input on various issues facing Canadian investors. We urge the Federal government to also focus its efforts on the financial literacy of seniors and other vulnerable sectors of the Canadian population. We are pleased that the first phase of the National Strategy for Financial Literacy will focus on seniors.

We have stated in other consultations with regulators that Canadian investors would benefit from more education and clarity around the availability of investment advice services. We believe the current myriad of investment professional/registration titles and corresponding designations cause immense confusion among investing Canadians and must be clarified so as to ensure investors understand what services they are receiving from investment professionals and those who are actually operating under a fiduciary duty when providing investment advice. More investor education in this area would ensure that these roles are properly understood by investors. In this regard, PMAC has taken an active role in ensuring the profession of portfolio management in Canada's investment industry is better understood.

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[4] See "Mortality Projections of Public Pension Plans in Canada and its financial implications", available at: http://www.osfi-bsif.gc.ca/Eng/oca-bac/sp-ds/Pages/jcm20140110.aspx

We would be please to answer any questions in connection with this submission and would be happy to present our submission to the House of Commons Standing Committee on Finance.

Sincerely,

K.A. Walmsley

Scott Mahaffy

Katie Walmsley
President, PMAC

Scott Mahaffy
Vice President & Senior Counsel
MFS Investment Management Canada Limited