FTR Now

Federal Budget 2011

Date: March 24, 2011

The Minister of Finance, the Honourable James M. Flaherty, tabled the Government of Canada's 2011 Budget "A Low-Tax Plan for Jobs and Growth" in the House of Commons on March 22, 2011.

In this *FTR Now* we review the key aspects of the Budget that are of most interest to employers and human resources professionals. At the time of publication, the leaders of the opposition parties have each announced that they will not support the Budget in its current form and the Government has announced that it will not be proposing further amendments. Accordingly, the following proposals are not likely to come into effect unless pursued by a future Government after what appears is likely to be a spring 2011 election.

Key items of interest include:

- Elimination of the mandatory retirement age for federally regulated employers;
- New rules for individual pension plans and RRSPs;
- The announced review of employee profit sharing plans
- Restrictions on increases to employment insurance (EI) premiums and other EI measures for employers; and
- A new tax credit for Volunteer Firefighters;

The Budget also included confirmation that the federal and provincial finance ministers are working to implement the new defined contribution pooled registered pension plan initiative announced in December 2010. This initiative is expected to provide Canadians with a new retirement savings option for those not participating in employer-sponsored pension plans. Modest enhancements to the Canada Pension Plan were also indicated as a priority to be discussed at the next meeting of Canada's finance ministers.

The Budget would also commit $3 million per year to financial literacy initiatives to help Canadians make more informed retirement savings choices. This education initiative is expected to have an affect on member engagement particularly for those who participate in defined contribution pension plans and group RRSPs.

The following is a more detailed summary of the key Budget announcements:

ELIMINATION OF THE MANDATORY RETIREMENT AGE FOR FEDERALLY REGULATED EMPLOYERS

One of the most significant changes proposed in the Budget are amendments to the *Canadian Human Rights Act* and the *Canada Labour Code* to prohibit federally regulated employers from setting a mandatory retirement age, unless there is a *bona fide* occupational requirement. The Budget proposes to review other acts to further this objective but does not indicate the specific amendments that would be made to the legislation or when the amendments would become effective.

While the proposal permits mandatory retirement in circumstances in which age is a *bona fide* occupational requirement, recent jurisprudence in the federal tribunals and courts in the context of federally regulated pilots suggests this may be a difficult standard to meet.

Our experience in advising employers following the elimination of mandatory retirement under Ontario's *Human Rights Code* is that the elimination of mandatory retirement gives rise to a multitude of significant practical and legal issues for employers.

Affected employers, both unionized and non-unionized, will want to review the terms and provisions of any collective agreements, employment contracts, pension plans, disability, insurance and other benefit plans to determine what distinctions are being made on the basis of "retirement age" to ensure that distinctions contained in those agreements comply with the proposed amendments.

Even those workplaces that no longer have mandatory retirement policies in place may be affected. Benefit plans and programs, such as long-term disability and life insurance, which typically incorporate age-based distinctions, will have to be reviewed in light of the amendments.

A Benefit Regulation under the *Canadian Human Rights Act* currently establishes a number of specific exemptions relating to an employee's participation in certain pension and benefit plans, the provisions contained in pension and benefit plans, and contributions to those plans. The Budget does not address whether these exemptions will remain in force.

The inclusion of this proposed change in the Budget is a clear indication that mandatory retirement will likely be eliminated in the future and would be re-tabled in the event that the Budget is not passed. We will closely monitor this change and provide further reports in future *FTR Now*s if, or when, the amendments are formally introduced.

INDIVIDUAL PENSION PLANS AND OTHER REGISTERED PLANS

The Budget contains a number of proposed changes to individual pension plans ("IPPs"), registered retirement savings plans ("RRSPs"), registered disability savings plans, and registered educational savings plans. The majority of changes are intended to enhance tax fairness by closing perceived loopholes or reducing unfair advantages. While most of the changes will primarily affect individual end-users of such plans, we have highlighted those proposed changes of note to employers and plan sponsors or administrators.

IPP

Under current rules, although an IPP member must commence a pension by the end of the year he or she attains age 71, the member may be able to minimize his or her retirement income paid from the IPP to defer taxation on retirement savings well beyond what is permissible for other registered pension plan members or registered retirement income fund (“RRIF”) annuitants The Budget proposes that members of IPPs upon reaching age 72 be required to receive a minimum level of pension income from the IPP equal to the amount that would be required to be paid from the IPP to the member if the member’s share of the IPP assets were held in a RRIF of which the member was the annuitant.

In addition to the imposition of these minimum withdrawals, the Budget also proposes to implement a restriction on the purchase of past service under IPPs by requiring either that the member’s existing RRSP assets or defined contribution account balances fund the purchase or that the member’s accumulated RRSP contribution room is reduced before new deductible contributions in relation to the past service may be made.

These new rules will apply to IPPs with three or fewer members where at least one is related to the sponsoring employer.

RRSP – ANTI-AVOIDANCE RULES

Of note for employers who sponsor Group RRSPs, the Budget proposes restrictions and associated penalties where an RRSP holds “prohibited investments” and changes to the rules in regard to RRSPs holding “non-qualified investments”, as those terms are defined under the *Income Tax Act*. The Budget imposes a tax equal to 50% of the fair market value of any prohibited investment or non-qualified investment held in an RRSP. This tax may be refunded if the investment is disposed of within specified time limits. The Budget proposes to replace the current rules imposing penalty tax on holding of a non-qualified RRSP investment with the 50% tax described above. However, investment income earned on a non-qualified investment in an RRSP will remain taxable to the RRSP.

These proposals could affect employers who sponsor Group RRSPs, particularly if the employer is responsible for the selection of the slate of investment options for the RRSP. Although “prohibited investments” are unlikely to arise in a Group RRSP context, employers will wish to review the terms of their service provider and investment management agreements to ensure that these providers undertake to ensure that there are no prohibited or non-qualified investments available under the Group RRSP and that these agreements indemnify the employer from any liability in the event that any issues arise with respect to prohibited or non-qualified investments.

REVIEW OF EMPLOYEE PROFIT SHARING PLANS ANNOUNCED

The Budget includes a statement by the Government expressing concern regarding the improper use of employee profit sharing plans (“EPSPs”). The Government has announced that it will review the existing rules for EPSPs to determine whether technical improvements are required and will undertake consultations. Employers who provide EPSPs for their employees may wish to provide input in the consultations as any changes that are implemented may affect existing EPSPs.

RESTRICTIONS ON INCREASES TO EMPLOYMENT INSURANCE PREMIUMS AND OTHER EI MEASURES FOR EMPLOYERS

LIMITING EI PREMIUM RATE INCREASES

The Canada Employment Insurance Financing Board (“CEIFB”) was established by the 2008 Budget to set EI premium rates on a cost-recovery basis, subject to a 15 cent limit on annual increases. The 2011 Budget confirms a measure announced in September 2010 that the Government has placed a further limit on the amount by which the CEIFB can increase EI premiums. For 2011, this maximum is limited to 5 cents per $100 of insurable earnings. For subsequent years, the maximum increase permitted is 10 cents per $100 of insurable earnings. The CEIFB will otherwise remain responsible for setting premium rates and managing the cash reserve.

The Government also announced consultations about how the EI rate-setting process can be improved to ensure stable and predictable rates going forward. A consultation paper on this topic is expected in the near future.

TEMPORARY HIRING CREDIT FOR SMALL BUSINESS

The Budget provides a temporary hiring credit for small businesses. The credit provides of up to $1,000 against increases in 2011 EI premiums over 2010 EI premiums. This one-time credit is only available to small businesses whose total EI premiums were at or below $10,000 in 2010.

EXPANDED EI BENEFITS UNDER WORK-SHARING AGREEMENTS

The Work Sharing Program (WSP) is a program designed to help employers and employees avoid temporary layoffs by providing income support to employees who work a temporarily reduced work week. The Budget extends the WSP by up to an additional 16 weeks for active or recently terminated work-sharing agreements up to October 2011.

TAX CREDIT FOR VOLUNTEER FIREFIGHTERS

The Budget proposes a non-refundable tax credit for volunteer firefighters for 2011 and future tax years. For 2011 the tax credit would be $450. This credit will be available to volunteer firefighters who perform at least 200 hours of service for their communities during a year. Volunteer service for a fire department will be ineligible if the firefighter also provides firefighting services, other than as a volunteer, to that fire department. In addition to the payor's obligation to report remuneration, the fire chief or a delegate will be required to certify the number of eligible volunteer firefighting service hours performed by persons claiming this tax credit.

Eligible volunteer firefighters who currently receive honoraria in respect of their duties as volunteer firefighters will be able to choose between claiming the new tax credit and continuing to be entitled to the existing tax exemption of up to $1,000 for honoraria.

OTHER MEASURES

EMPLOYEES AFFECTED BY CORPORATE INSOLVENCY

The Budget contains two changes that will affect employees in the context of corporate insolvencies and restructurings.

- Expanding The Wage Earner Protection Program (WEPP)

The WEPP reimburses eligible employees for unpaid wages (including vacation pay, severance pay and termination pay) when their employer declares bankruptcy or becomes subject to a receivership under the *Bankruptcy and Insolvency Act*. WEPP currently covers unpaid wages earned in the six months preceding the employer bankruptcy or receivership.

Budget 2011 announced that the coverage period will be increased. The proposed changes seem to be directed at extending WEPP coverage to employees whose employer undertakes an extended *Companies' Creditors Arrangement Act* restructuring period (i.e., beyond six months) prior to a bankruptcy or receivership.

The proposed WEPP changes do not affect employers.

- Taxation of Lump Sum Payments in Lieu of Health and Dental Coverage

Current Canada Revenue Agency (CRA) policy provides that lump sum payments made by employers to former employees and retirees in lieu of their right to ongoing health and/or dental coverage (i.e., retiree benefits) are not "income" to former employees and retirees for tax purposes.

Budget 2011 announced that CRA will clarify that the current rules will continue to apply to lump sum payments made by *insolvent* employers to former employees and retirees in relation to insolvencies *arising before 2012*. This announcement contains little detail but *prima facie* suggests that the current preferential tax treatment provided former employees and retirees who receive lump sum settlements/buy-outs of health and/or dental coverage may be limited to only insolvent employers in conjunction with insolvencies occurring before 2012.

FUNDING FOR LABOUR CANADA'S PREVENTIVE MEDIATION PROGRAM

The Budget announced an expansion to the delivery of the Preventive Mediation Program which is intended to assist in labour relations at the federal level. The program offers a number of workshop services and facilitation services to workplaces aimed at improving constructive relationships between employers and unions.

CONCLUSION

In addition to the items described above, there are a number of other Budget measures that are of general interest to Canadians, such as the enhanced Guarantee Income Supplement for Seniors, the Children's Art Tax Credit, an extension to the program designed to assist older workers in seeking employment, and the further extension of a number of employment insurance benefit improvement pilot projects.

For more information on this Budget and its implications to your workplace, please contact your regular Hicks Morley Lawyer.
