
March 22, 2011 Federal Budget Update **Proposed Changes to Individual Pension Plans (IPPs)**

The Federal Budget tabled on March 22, 2011 proposed the following two changes to IPPs which could under certain circumstances significantly reduce the tax advantages of future new IPPs. IPPs are superior pension schemes for executives, business owners and incorporated professionals that offer greater contributions, deductibility of investment costs, considerable past service contributions at implementation and significant additional contributions after commencement of pension by the employer.

The two budget IPP proposals are as follows:

1. Annual minimum amounts will be required to be withdrawn from IPPs, similar to current minimum withdrawal requirements from Registered Retirement Income Funds (RRIFs), once a plan member attains the age of 72; and
2. Contributions made to an IPP that relate to past years of employment will be required to be funded first out of a plan member's existing Registered Retirement Savings Plan (RRSP) assets or by reducing the individual's accumulated RRSP contribution room before new deductible contributions in relation to the past service may be made.

Proposed IPP Rule #1 would require the payout of IPP assets that are significantly more than the pension amount as defined under an IPP and would lead to substantial risks of not having adequate benefit security on the promised pension. Proposed IPP Rule #2 would penalize individuals who have accumulated a significant amount of personal RRSP funds. The available IPP past service funding room under the existing rules would be reduced by the amount of personal RRSP funds the individual has that are in excess of the required transfer amount to meet past service eligibility.

The references in the Budget Papers to the proposed changes are unusual in the sense that they do not include draft amendments to the Income Tax Act, the normal procedure for changes of this kind. In view of this, we do not know the detail of how these proposals might be implemented. According to informed sources, however, Rule #1 would apply to all IPPs whereas Rule #2 would apply only to new IPPs implemented after the Budget Day.

We feel that these two proposed new rules are extremely unfair and discriminatory. We along with many other actuarial consulting firms have made a joint-submission to the Honourable James M. Flaherty and the Honourable Ted Menzies at Finance to request that these proposed IPP changes in the budget be withdrawn and rescinded. For a full copy of our joint-submission, please click [here](#).

Our recommendations to individuals who wish to establish new IPPs are as follows:

1. If your personal RRSP funds are insufficient to meet the required transfer amount for recognition of your full past service, the proposed IPP past service rule has no impact on your situation. It is recommended that you proceed with plan implementation.
2. If your personal RRSP funds are slightly more than the required transfer amount and less than the past service contribution amount available, i.e. your situation is similar to the example below:
 - a. The qualifying transfer amount from the RRSP is \$400,000 and the past service pension value is \$600,000, hence past service funding room is \$200,000 (\$600,000 less \$400,000). The individual has a current balance of \$420,000 in personal RRSP funds.
 - b. Under existing rules, \$400,000 would be transferred from the personal RRSP to the new IPP leaving behind a remaining balance of \$20,000 in the RRSP. The employer would be able to make a past service contribution of \$200,000.
 - c. Under the proposed new rules, the full \$420,000 personal RSP balance would be transferred to the new IPP. The employer would only be able to contribute \$180,000 (\$600,000 less \$420,000)

We recommend that you proceed with IPP implementation as follows:

- I. We will specify in the plan documentation that the required transfer amount and the employer past service funding would depend on whether the proposed IPP past service rule in the budget would eventually get passed into the tax legislation.

- II. The member would transfer in the full \$420,000. If the proposed IPP past service rules in the budget eventually get passed, the full \$420,000 would be part of the defined benefit provision. In the event that the proposed IPP past service rules in the budget do not get passed, the \$400,000 required transfer would be part of the defined benefit provision and the excess \$20,000 will be treated as Additional Voluntary Contributions (AVC's) – similar to RRSP funds kept inside an IPP.
 - III. The employer would only make past service contributions in the amount of \$180,000 (i.e. assuming that the budget proposal would get passed). In the event that the budget proposal does not get passed, the employer would then contribute the remaining \$20,000.
3. If your personal RRSP funds are way more than both the required transfer amount under existing rules and the past service contribution amount available such that there is not a meaningful amount of past service contribution room under the proposed new rule, our recommendation would be to put things on hold pending the eventual outcome of the federal election and the budget.

We will keep you posted with updated information on these proposed IPP changes in the March 22, 2011 federal budget as soon as they become available.

If you wish to obtain an IPP Quote to determine the past service funding opportunities, please use our IPP On-Line Quoting System at:

<http://www.westcoast-actuaries.com/OnlineQuotingSystem/>

Should you have any questions or require further information or clarification, please contact us at (604) 730-1898 or IPP@WAIInc.ca. Our professional staff would be pleased to assist you.