



Research Advisory

Hewitt

Canadian Research Group

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Highlights

The 2009 federal Budget contains funding relief for pension plan sponsors, assistance for workers, and efforts to stimulate the economy through infrastructure spending.

The Hewitt Research Advisory is a regular Hewitt newsletter designed to provide a detailed overview of specific legislative and regulatory developments in Canada relating to human resources.

If you have questions or comments, please reply to this message or contact INFOCAN@hewitt.com.

Federal Budget 2009 – An Abrupt Change in Direction

To help Canada weather a severe recession and to honour its international commitments to stimulate the global economy, federal Budget 2009 contains billions of dollars of spending and will result in a deficit in excess of \$80 billion within five years. Infrastructure spending features prominently in this scheme, as does reform of securities regulation in Canada. Specific relief is also provided for pension plan sponsors, seniors, unemployed workers, and taxpayers generally.

Federally Regulated Private Pension Plans

On January 9, 2009, the Government released a consultation document on the legislative and regulatory framework for federally regulated pension plans. Given the importance of these issues, the Government will accelerate its timeline so that consultations will be completed within 90 days. Originally, the process was to be completed by the summer.

The Office of the Superintendent of Financial Institutions (OSFI) will increase the 110 per cent policy limit on asset value smoothing. To assist OSFI in providing this additional solvency funding relief, the Government will take action to improve pension plan member protection by making the amount of any deferral of funding that results from the use of an asset value in excess of 110 per cent subject to a deemed trust.

Hewitt Comment: OSFI regulates federally registered pension plans (typically those for individuals in federal employment, e.g. financial institutions, transportation, etc.). The November 2008 Economic Statement proposed a number of measures to provide funding relief, such as extending the amortization period for funding solvency deficiencies from five to 10 years subject to

employee consent. Budget 2009 includes those measures while providing additional relief.

Currently, OSFI permits the use of a smoothed asset value to stabilize market value fluctuations over a period of up to five years for solvency and going concern funding purposes. OSFI currently does not permit the use of a smoothed asset value that exceeds 110 per cent of the actual market value. The federal Budget eliminates this restriction. For plan sponsors that are facing significant increases in pension plan deficits, the change may result in a material decrease in company contributions.

Some measure of protection is also afforded to plan members through the introduction of a deemed trust on the reduction in funding resulting from the use of an asset value in excess of 110 per cent of market value. This deemed trust ensures that the amount of contributions deferred would not form part of the company's property available to creditors upon a subsequent bankruptcy.

Federally Regulated Retirement Savings

Last November, in recognition of the impact of deteriorated market conditions on retirement savings, the Government proposed to reduce the required minimum withdrawal amount for Registered Retirement Income Funds (RRIFs) by 25 per cent for 2008. RRIF holders who had already withdrawn more than the reduced 2008 minimum amount would have been permitted to re-contribute the excess to their RRIFs, until the later of March 1, 2009 and 30 days after enactment. Re-contributions would also have been deductible for the 2008 taxation year, and similar rules would have applied to those receiving variable benefit payments under a money purchase Registered Pension Plan. In Budget 2009, the Government reiterated this proposal.

Budget 2009 proposes to allow, upon the final distribution of property from a deceased annuitant's Registered Retirement Savings Plan (RRSP) or RRIF, the amount of post-death decreases in value of the RRSP or RRIF to be carried back and deducted against the year-of-death RRSP/RRIF income inclusion. This measure will apply in respect of deceased annuitants' RRSPs or RRIFs where the final distribution from the RRSP or RRIF occurs after 2008.

***Hewitt Comment:** Currently, the fair market value investments held in an RRSP or RRIF at the time of the annuitant's death is included in his or her income for the year of death. This Budget provision will allow for losses after the date of death to be deducted against the year of death RRSP or RRIF income inclusion. This may reduce taxable income on a deceased's terminal return.*

Financial Literacy

In the spring of 2009, the Government will establish an independent task force to make recommendations on a cohesive national strategy on financial literacy. The task force will include representatives of the business and education sectors, volunteer organizations and academics, and will be supported by a federal secretariat. The collaboration of the provinces, private sector and community organizations will be sought to ensure a positive outcome.

***Hewitt Comment:** By announcing a task force to make recommendations on a cohesive national strategy on financial literacy, Canada joins other developed nations (US, UK, Australia, and other OECD and EU countries) in recognizing the importance of improving financial literacy. The issue is gaining prominence as the number and complexity of financial products and instruments increases, and as organizations shift responsibility for important financial decisions to employees.*

Personal Tax Relief

Effective January 1, 2009:

- The basic personal amount will be increased to \$10,320 from \$9,600 in 2008;
- The top of the first personal income tax bracket will be increased to \$40,726 from \$37,885 in 2008, allowing more income to be taxed at the lowest 15-per-cent rate, rather than the 22-per-cent rate; and
- The top of the second personal income tax bracket will be increased to \$81,452 from \$75,769 in 2008, allowing more income to be taxed at the 22-per-cent rate, rather than the 26-per-cent rate.

Normal indexation will apply to the new basic personal amount and bracket thresholds for future years.

TFSA Insurability

The Government is proposing to designate Tax-free Savings Accounts (TFSAs) as a separate category of deposits insurable by the Canada Deposit Insurance Corporation (CDIC), in a manner similar to the treatment provided RRSPs and RRIFs.

Immediate Action to Build Infrastructure

As promised in the fall, the Budget rolls out an array of specific infrastructure projects. The total commitment is about \$6 billion per year for the next two years. The projects are grouped into four categories: Provincial, Territorial, and Municipal Infrastructure; First Nations Infrastructure; Knowledge Infrastructure; and Federal Infrastructure. The largest single commitment is to a new \$4 billion Infrastructure Stimulus Fund that will cover up to 50 per cent of the total cost of projects that are currently awaiting funding and is intended to "get shovels in the ground quickly". In addition, there are other specific line-item infrastructure projects covered.

***Hewitt Comment:** The Budget contains details on the types of infrastructure projects that will be directly supported through the Government's fiscal stimulus. We expect these details, combined with the Government's continued support of public-private partnerships, to begin having an impact on the types of infrastructure investment opportunities that will be brought to market for consideration for inclusion in institutional investment portfolios.*

EI Reform and Other Labour Force Initiatives

The Government will freeze Employment Insurance (EI) premium rates at \$1.73 per \$100 of insurable earnings for both 2009 and 2010. This will represent their lowest level since 1982, and a projected \$4.5 billion stimulus relative to break-even rates.

In addition, Budget 2009 will support Canadian workers affected by the global economic downturn by, amongst others:

- increasing for two years all regular EI benefit entitlements to 50 weeks from 45 weeks;
- providing \$500 million over two years to extend EI income benefits for Canadians participating in longer-term training;
- extending work-sharing agreements by 14 weeks, to a maximum of 52 weeks, so more Canadians can continue working; and

- responding to skilled labour shortages with \$40 million a year to launch the \$2,000 Apprenticeship Completion Grant.

Hewitt Comment: *The extension of the maximum EI benefit period by five weeks applies only on termination of employment, not on sickness.*

The freezing of EI rates represents a departure from recent years, when employers and employees experienced a reduction in rates. However, Budget 2009 provides certainty that improvements to EI benefits introduced in this Budget will not result in higher rates over the next two years.

The enhancements to the work-sharing program provide employers greater flexibility in workforce management during the current economic downturn by extending the maximum period in which EI benefits supplement employee income.

While many observers had expected additional reform, such as the elimination of regional disparities in benefits coverage, this was not included in the Budget.

Other initiatives to assist workers include:

- more protection to workers by extending the Wage Earner Protection Program on an ongoing basis to also cover severance and termination pay, subject to the current maximum of four weeks of insurable earnings (currently the program covers wages only up to a prescribed limit);
- an additional \$87.5 million over three years to temporarily expand the Canada Graduate Scholarships program;
- an additional \$3.5 million over two years to offer 600 new graduate internships through the Industrial Research and Development Internship program;
- more than \$1 billion over five years for a Southern Ontario development agency to help workers, communities and businesses in this region;
- \$1 billion over two years for a Community Adjustment Fund that will help mitigate the short-term impacts of restructuring in communities in all regions; and
- an additional \$90 million over three years to extend the Targeted Initiative for Older Workers (TIOW) until March 2012.

Hewitt Comment: *While the coverage is limited, the Wage Earner Protection Program measure introduced in Budget 2009 may provide a small measure of protection to employees recently terminated and in receipt of severance payments. The other enumerated measures should enable workers to obtain appropriate training and alternative employment.*

Foreign Credential Recognition

Budget 2009 provides \$50 million over the next two years to support the Work of the Foreign Credential Referral Office and the Foreign Credential Recognition Program in the development of a common approach to foreign credential assessment. This measure will help ensure that immigrants are better integrated into the Canadian labour force.

A New Canadian Securities Regulator

On January 12, 2009, the Expert Panel on Securities Regulation released its Final Report and a draft Securities Act. The central recommendation is the establishment of a single securities regulator administering a single federal statute for all of Canada. With this federal Budget, the Government has

announced its intention to move quickly with like-minded provinces and territories to produce a transition plan within one year.

***Hewitt Comment:** The pace towards a much needed reform has been slow to date, and the Budget does not make it clear when a national regulator will be established, but there does appear to be a new sense of urgency. However, there remains considerable uncertainty as to which provinces or territories would be willing to cede jurisdiction in order to participate.*

Non-resident Trusts and Foreign Investment Entities

Outstanding proposals for non-resident trusts and foreign investment entities, first introduced in the 1999 Budget, apply in respect of arrangements under which Canadian residents seek to avoid Canadian tax through the use of foreign intermediaries under circumstances designed to circumvent the application of existing anti-avoidance rules. The Government supports the fundamental policy objective of ensuring that Canadian taxpayers should not be able to avoid paying their fair share of income tax through the use of foreign intermediaries, but will review the existing proposals before proceeding.

***Hewitt Comment:** Last year during Senate committee hearings, the government expressed willingness to exempt pension plans from the operation of these taxation provisions as urged by various pension advocacy groups.*

Improving Access to Credit

The government will provide up to \$200 billion through an Extraordinary Financing Framework to improve access to credit for consumers and allow businesses to obtain the financing needed to invest, grow and create new jobs.

Pay Equity

Legislation to modernize pay equity for federal public sector employees will be introduced. It will ensure that the employer and bargaining agents are jointly responsible and accountable for negotiating salaries that are fair and equitable to all employees.

Federal Public Sector Wages

The Government will legislate annual public sector wage increases of 2.3 per cent in 2007–08 and 1.5 per cent for the following three years.

Mandatory Electronic Filing

Taxpayers filing 50 or more returns (such as T4s for employment income) will be required to do so electronically. Previously, the limit was 500. This measure will apply in respect of information returns required to be filed after 2009. Penalties will be imposed for non-compliance.

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