Tax memo

Canadian tax updates

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Pooled Registered Pension Plans (PRPPs)—Tax rules introduced

Outlines income tax rules for Pooled Registered Pension Plans (PRPPs).

January 18, 2012

On December 14, 2011, the Department of Finance released income tax legislative proposals for Pooled Registered Pension Plans (PRPPs)–voluntary savings plans aimed at individuals who do not have access to employer-sponsored pension plans, notably employees of smaller employers and the self-employed. The Department of Finance has requested comments on these proposals by February 14, 2012.

The proposals will apply to both federally and provincially regulated PRPPs. They will come into force at the same time as the *Pooled Registered Pension Plans Act*[1] – the federal legislation implementing PRPPs, which was introduced on November 17, 2011, and is discussed in our *Tax memo* "Pooled Registered Pension Plans: A new retirement savings vehicle" at **www.pwc.com/ca/taxmemo**.

Overview

The tax rules for PRPPs are meant to complement the existing Registered Pension Plan (RPP) and Registered Retirement Savings Plan (RRSP) framework, and are to operate in a manner similar to multi-employer money purchase RPPs.

Like RRSPs, PRPPs will be available from financial institutions, which will administer them. However, PRPPs are intended to allow more people to benefit from the lower investment management costs that result from membership in a larger, pooled pension plan. A single and separate account must be maintained for each PRPP member.

The key features of a PRPP are:

- **Members** – Individuals can have a PRPP regardless of employment status.
- **Employers** – Employers are not required to contribute to the PRPP of an employee, but may do so.
- **Contributions** – PRPP contributions made by the member and the employer are deductible, within limits.
- **Contribution limits** – Combined contributions to a PRPP and RRSP by the member and the employer cannot exceed the individual's RRSP deduction limit.
- **Investment income** – Earnings within a PRPP, as well as contributions made to the PRPP, are tax-sheltered until paid out of the PRPP.

1. Bill C-25, *An Act relating to pooled registered pension plans and making related amendments to other Acts.*

- **Payments** – Payments of non-locked in funds are taxable to the member.
- **Transfers** – The transfer rules for defined contribution RPPs generally apply to PRPPs.

Contributions

PRPP contribution rates will be set by the administrator. Contributions will be subject to applicable federal or provincial locking-in rules.

Contributions can be made by the individual member, whether employed or self-employed, and an employer. However, no contributions (other than certain transfers) can be made after the year the member turns 71.

Employees can contribute even if their employer is not involved with the PRPP. If the employer is involved with the PRPP, the employee is not required to become a member.

The total of the individual's and employer's contributions to a PRPP for a year are linked to the individual's available RRSP contribution limit for that year, which includes any unused amounts from previous years. Contributions exceeding this limit may result in a penalty tax to the individual (see **Over-contributions** below).

Contributions made in a year, by the individual and the employer, reduce the individual's RRSP contribution room for that year and future years. Employer contributions made in the year also reduce the individual's ability to make deductible PRPP contributions in that year and later years.

Neither employee nor employer contributions are subject to reporting of pension adjustments (unlike RPPs).

Individual contributions

To claim a deduction in a calendar year, individuals must make PRPP contributions no later than 60 days after the calendar year end (i.e., March 1, but February 29 for leap years; adjusted for deadlines that fall on weekends), paralleling the RRSP contribution deadlines.

An individual's contributions to a PRPP are treated as RRSP contributions for the purpose of determining the deductibility of total PRPP and RRSP contributions for the year.

Individuals can claim a deduction for certain transfers to a PRPP, including transfers of retiring allowances and withdrawals under the Home Buyers' Plan or the Lifelong Learning Plan, within specified limits.

Employer contributions

Employers can contribute to an employee's PRPP, but are not required to do so. Employer contributions are excluded from salaried compensation and are therefore not taxable to the employee. For example, employer contributions will not be subject to Canada pension plan (CPP)/Quebec pension plan (QPP) or Employment insurance (EI) withholdings. Employer contributions must vest immediately and indefeasibly.

To claim a deduction in a taxation year, an employer must make PRPP contributions with respect to employee service provided in that year, no later than 120 days after the taxation year, paralleling the RPP contribution deadlines.

For employers, there is no minimum contribution. The maximum employer contribution equals the employee's RRSP dollar limit for the year (which excludes unused amounts from previous years) – unless the employee directs otherwise.

Over-contributions

Over-contributions to PRPPs are subject to the same penalty as those to RRSPs: 1% of the individual's month-end excess. However, this penalty does not apply to certain non-discretionary contributions made by the employer.

Investment income

The investment income earned in a PRPP must be allocated to the member's account annually (or more frequently). The earnings in, as well as contributions made to, the PRPP are tax-exempt until paid out of the PRPP. However, this exemption does not extend to income from a business carried on by a PRPP.

Investments

PRPPs need not conform to the RRSP "qualified investment" rules, but are subject to investment restrictions intended to prevent administrators from participating in arrangements that could be used:

- to circumvent PRPP contribution limits; or
- in the case of older individuals, to reduce the value of the PRPP accounts in order to avoid or lower required RPP payments in retirement.

In addition, PRPPs must take reasonable precautions to avoid:

- acquiring investments in which a member has a significant interest (more than 10% of a class of shares); and
- concentrating more than 10% of plan assets in one business or non-arm's length group.

Small PRPPs (generally, those with fewer than 10 unrelated employers participating) must also avoid holding investments in participating employers.

Payments and transfers

During the member's life

Funds within a PRPP generally will be covered by locking-in rules similar to those applicable to RPPs. Subject to these rules, in general, payments from a PRPP must be included in the individual's income, and are eligible for the pension tax credit and pension income splitting. Payments made to a non-resident will be subject to withholding tax.

The existing transfer rules for defined contribution RPPs (governing transfer between RPPs and between an RPP and an RRSP, a Registered Retirement Income Fund (RRIF) and certain other registered plans) generally will apply to PRPPs.

A PRPP must be wound up by the end of the year in which the member turns 71, at which time the options mirror those for defined contribution RPPs.

The PRPP funds can be:

- paid as a single, non-periodic payment;
- used to purchase a life annuity for the member; or
- paid as variable benefits (RRIF-type payments).

Upon the member's death

The general rule is that the funds in the PRPP are included in income for the deceased member's last taxation year. However, if the deceased had directed that the funds go to the individuals noted below, the transfer will be tax-deferred.

		Tax-deferred transfer?	
		Surviving spouse or common-law partner	**Infirm financially dependent child or grandchild**
Fund transfer options	Become successor member, assume ownership of PRPP	Yes	No
	Transfer to own RRSP, RRIF, PRPP or RPP	Yes	Yes
	Acquire a qualifying annuity	Yes	Yes
	Transfer to Registered Disability Savings Plan (RDSP), to the extent of available contribution room	No	Yes

GST/HST

New legislation is expected that will make PRPPs subject to the same treatment as RPPs with respect to the Goods and Services Tax (GST) and Harmonized Sales Tax (HST) rules under the *Excise Tax Act*.

PwC comments

PRPPs are intended to provide new retirement savings options that will be attractive to smaller employers and the self-employed. Employees whose employers choose to contribute will benefit from this additional funding to their tax-assisted retirement savings.

However, other employees and the self-employed will continue to be solely responsible for their retirement savings. Furthermore, they will be unable to save more on a tax-deferred basis than is currently the case. The limitation remains the individual's RRSP contribution room, but this limit will be shared by the individual's RRSPs and PRPPs.

For more help

For help understanding how the PRPP proposals apply to you, please contact your PwC adviser or any of the following:

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1. Member of PwC's Canadian National Tax Services (see **www.pwc.com/ca/cnts**).
2. A law firm affiliated with PwC (see **www.wilsonandpartners.ca**).

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