Stephen Frank
President and CEO

May 3, 2022

Mr. Shawn Porter
Assistant Deputy Minister, Tax Legislation
Department of Finance Canada

Ms. Kathleen Wrye
Acting Director Pensions Policy
Financial Sector Policy Branch
Department of Finance Canada

Dear Mr. Porter and Ms. Wrye,

Re. Expanding the scope of the VPLA's to enable more Canadians to access retirement income security

I am writing on behalf of the Canadian Life and Health Insurance Association (CLHIA) to request the scope of the Variable Payment Life Annuities (VPLAs) enacted into the *Income Tax Act & Regulations* (ITA) effective January 1, 2020, be expanded so that all or most of the over 500,000 Canadians retiring each year have access to this innovative decumulation solution.

About the CLHIA

The CLHIA is a voluntary association whose member companies account for 99 per cent of Canada's life and health insurance business. These insurers provide financial security products including life insurance, annuities (RRSPs, RRIFs and pensions) and supplementary health insurance to over 29 million Canadians. They hold nearly $ 1 trillion in invested assets in Canada and employ more than 157,000 Canadians.

The CLHIA commends the Federal government for enabling both Advanced Life Deferred Annuities (ALDAs) and VPLAs in 2021. These initiatives have the potential to provide Canadians the means to achieve retirement income security. However, we believe that minor but important changes to the ITA are required to ensure that many more Canadians can access VPLAs.

VPLAs as enacted can only assist few thousand Canadians, if that, each year

While the VPLA legislation, as enacted, will enable members of Defined Contribution (DC) and Pooled Registered Pension Plans (PRPPs) to access VPLAs, only members of very large money purchase pension plans, with at least 10,000 plus members, can make the VPLA solution operationally feasible. This is because benefits payable from a VPLA are dependent on the pooling of both investment and longevity risks across cohorts of retirees. While there are currently over 11,000 DC plans operating in Canada with over $94 billion in retirement assets, we estimate that only a handful of Canadian DC plans have the scale to enable the "within plan" VPLA solution, as currently enacted.

While the government also enabled VPLAs within the PRPPs, PRPPS are not very prevalent and the accumulations within PRRPs are small and lack the necessary scale. As of June 30, 2021, there were assets of approximately $350 million in PRPPs with less than 105,000 members.

A successful accumulation/decumulation arrangement is very much dependent on pooling and scale. For example, the Australian Q Super partners operate with nearly 60,000 employers providing secure and cost-efficient retirement income to over 600,000 members across the country.

Data shows that over 88% of private sector employees work for employers with less than 500 employees[1]. Even if these employers were offering DC pension plans or PRPPS, they are not large enough to offer the "within plan VPLA" solution as currently enacted (See Appendix #2 for an analysis on the importance of scale to avoid income volatility). We believe the intent of the VPLA rules was not to exclude the millions of Canadians who work for employers without the necessary scale to offer a "within plan VPLA". Thousands of Canadians within these pension plans retire each year, and it is imperative that these Canadians have the opportunity to have a VPLA solution to manage their retirement income.

Further, statistics show only about 1 in 3 Canadians have access to a workplace pension plan (a DB, DC or PRPP). Even these Canadians need to top up their workplace pension plan with contributions to a group or individual RRSPs (and TFSAs). Given this, access to VPLAs must also include the many millions of Canadians saving for their retirement entirely or in part through group and or individual RRSPs (including RRIFs and LIFs and TFSAs). In 2020, assets in these vehicles totaled approximately $1,600 billion in RRSPs and $422 billion in TFSAs (See Appendix #1 for sources of Canadian retirement accumulations). This is a considerable quantum of retirement accumulations outside the scope of VPLAs as currently enacted. The flexibility of acquiring a single VPLA that can source funds from pension plans (DC or PRPP) as well as individual, or group, RRSPs and TFSA will provide retirees with one-stop solution and ease the client experience.[2]

[1] 2020 Innovation, Science and Economic Development Canada, Small Business Branch, Research and Analysis Directorate, page 17.

[2] While subparagraph 146(3)(b)(iii) provides for a variable annuity payment to increase or decrease in line with value of a specified group of assets, it is unclear if this also allows for variability due to both investment and longevity risk.

Such potential large case pooling maximizes stable income in retirement for Canadians choosing to acquire a VPLA. A lack of adequate pooling, by design, contributes to increased investment and mortality risk which can trigger more frequent income adjustments to the VPLA benefits. Expanding the scope of VPLAs to all registered retirement funds will allow maximum access to VPLAs and enhanced retirement security.
While the VPLA as a retirement solution has the potential to help all or most of the 500,000 Canadians set to retire each year, "the within plan VPLAs" as enacted can only assist a few thousand Canadians, if that, each year as previously noted.

Changes to allow "standalone" VPLAs are needed to provide solutions to a greater number of Canadians

We believe, in addition to "within plan VPLAs", the ITA should enable "standalone VPLAs" that can be accessed by individuals or members of a group from an authorized annuity provider. A VPLA provider, such as a life insurer, will pool investment risk of participants' transferred assets from registered retirement plans (whether that be from DC, PRPP, DPSP, Group or individual RRSPs, RRIFs, LIFs or TFSAs) and their longevity risk to provide a reliable (but not guaranteed) source of retirement income. We expect a standalone VPLA will be subject to pension regulations, as well as regulatory controls by OSFI (Capital and Supervision) and provincial regulators for market conduct regulations.

A standalone VPLA could be available as an individual or group annuity product. Policyholders would be issued individual certificates with their rights limited to an interest in the VPLA pool, where income is adjustable based on the mortality and investment returns of the pool/group. We anticipate Canadians approaching retirement age may wish to access a VPLA while choosing to defer withdrawals up to the time they reach age 71. The investments held within the VPLA pool(s) may be arranged by cohort and/or investment risk.

Retirees face many uncertainties: volatile investment returns, increasing medical costs and above all, their individual life expectancy, and the fear of outliving their savings. These uncertainties and risks can force retirees to limit spending to the point of limiting or impeding their lifestyle. This is especially true for retirees without an adequate source of guaranteed income. With the ballooning segment of retirees in Canada, it makes economic sense to provide decumulation solutions that will enable retirees to spend and maintain an optimum lifestyle.

Appendix #3 includes some suggested relevant data in terms of accumulation and, at a high level, the changes that may be required to the ITA to extend the current "within plan VPLAs" to also include "stand alone VPLAs".

Conclusion

The CLHIA recommends the Federal government expand the scope of VPLAs to enable standalone VPLAs that can pool funds from across all registered retirement funds.

We urge the government to extend the VPLA solution to include “standalone” VPLAs as soon as possible to ensure fairness in terms of access to this innovative solution to all Canadians. The CLHIA and other stakeholders are ready to assist policy makers to flesh out the details and respond to any detailed questions. It is imperative that we improve upon the existing framework of retirement solutions to allow Canadians in and approaching retirement to obtain more secure lifetime income.

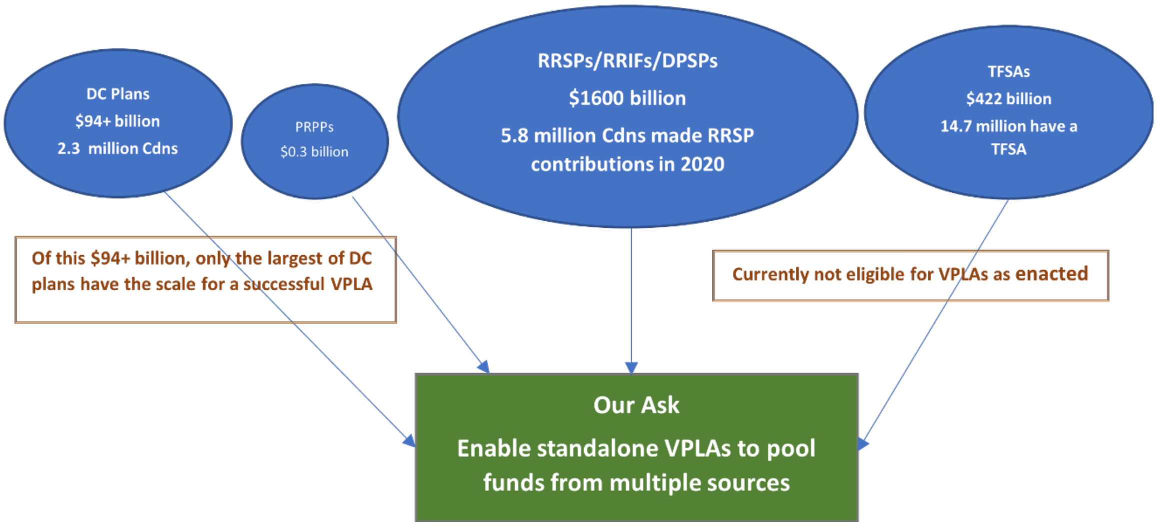
We would be pleased to meet to discuss any of our comments with you in further detail.

Yours sincerely,

Stephen Frank

Copy to: Andrew Donelle, Senior Director, Deferred Income Plans, Tax Legislation Division, Department of Finance

APPENDIX #1: SOURCES OF RETIREMENT ACCUMULATIONS IN CANADA



APPENDIX #2: IMPORTANCE OF SCALE TO AVOID INCOME VOLATILITY

The following table shows the expected variability in income payments caused by random longevity fluctuations for a given number of members in a VPLA. This would be independent of any additional volatility caused by investment return fluctuations.

Note that in order to have 1000 members in the VPLA option, it would require a pension plan to be much larger. For a pension plan of 10,000 lives, if in any given year 3% of members retire (approx. 1 in 33), and of those retiring, 25% elect the VPLA option, that would increase the members in the VPLA by 75 members, and it would take ~15[3] years to have 1000 lives. A pension plan with 1000 lives would take 15 years to get to 100 lives in the VPLA.

Number of Lives in VPLA	Income Volatility at 20 years	Income Volatility at 30 years
10	+/- 25%	volatile
50	+/- 15%	+/- 30%
100	+/- 10%	+/- 25%
1000	+/- 4%	+/- 10%

Results:

- Isolates income volatility due to random mortality - significantly reduces with scale
- Investment earnings held constant
- Ignores operational cost efficiencies

[3] While 75 people per year would take 13.33 years to reach 1000 lives, due to expected mortality it would take ~15 years before there were 1000 annuitants in the VPLA.

APPENDIX #3: SUGGESTED ITA CHANGES TO ACCOMMODATE A STANDALONE VPLA

Registered funds used to acquire a standalone VPLA, as a product, continue to be tax-deferred

Subsection 146(16) of the ITA provides for the tax-deferred transfer of funds from an RRSP, prior to maturity, to specified plans. Recently, subsection 146(16) was amended to include transfers “to a licensed annuities provider to acquire an advanced life deferred annuity for the benefit of the transferor”. We propose an amendment to subsection 146(16) to provide for the tax-deferred transfer of funds from an RRSPs acquire a “standalone VPLA”.

Similar amendments would be required to accommodate all holders registered funds to acquire or participate in a “standalone VPLA”, including:

RRSP – 146(16)
RRIF – 146.3(14.1)(c)
DPSP – 147(19)(d)(v)
RPP (money purchase plan) – 147.3(1)(iv)
PRPP – 147.5(21)(c)(vi)

Taxation of standalone VPLA & charging provisions

The following provisions would be required under the ITA for the taxation of the standalone VPLA and payments out of the VPLA to members:
Definitions section - standalone VPLA (similar to definition of ALDA in subsection 146.5(1)), annuitant, and beneficiary

Variable payment life annuity means a contract for an annuity that meets the following conditions:

(a) it is issued by a licensed annuities provider,

(b) it specifies that it is intended to qualify as a variable payment life annuity under this Act,

(c) periodic annuity payments under the contract are payable
  (i) in equal amounts, or
  (ii) in amounts that are not equal only because the payments are adjusted in whole or in part to reflect

(1) increases or decreases in the mortality experience of the VPLA pool, or

(B) increases or decreases in the investment returns increases or decreases depending on the increase or decrease in the value of a specified group of assets constituting the assets of a separate and distinct account or fund maintained in respect of the VPLA pool, or (d) it does not provide for any payment under the contract except as specified in this definition.

Annuitant - means an individual who has acquired a contract for an annuity from a licensed annuities provider.

Beneficiary - under a contract for an annuity, means an individual who has a right under the contract to receive a payment after the death of the annuitant.

Charging provisions for payments out of the standalone VPLA (similar to definition of ALDA in subsection 146.5(2)-(7))

(2) Amounts (including amounts deemed to have been received under paragraph (3)(a)) received by a taxpayer in a taxation year under a variable payment life annuity shall be included in computing the income of the taxpayer for the taxation year.

(3) If an amendment made at any time to a contract, results in it no longer meeting the conditions in the definition variable payment life annuity in subsection (1), the following rules apply:

   (a) the annuitant under the contract immediately before that time is deemed to have received under the contract at that time an amount equal to the fair market value of their interest in the contract at that time; and

   (b) the annuitant is deemed to have acquired their interest in the contract at that time for an amount equal to the fair market value of the interest at that time.

(4) No tax is payable under this Part by a trust on the taxable income of the trust for a taxation year if, throughout the period in the year during which the trust was in existence, the trust was governed by a variable payment life annuity.