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ADMINISTRATION OF LIFE INCOME FUNDS

In Department of Finance News Release No. 2008-037, dated May 8, 2008, the Minister of Finance announced that changes to the Pension Benefits Standards Regulations, 1985, regarding the administration of Life Income Funds ("LIFs"), are now in effect. These changes, which increase the flexibility to withdraw funds, were proposed in the 2008 federal Budget. The Overview from the Backgrounder and the accompanying Questions and Answers are reproduced below.

The Regulations set out the necessary forms that must be completed. Further information on LIFs and locked-in RRSPs is available on the Office of the Superintendent of Financial Institutions Website at www.osfi-bsif.gc.ca.

Further information on pensions can be found in the Employer Pension Plans section of PAYSOURCE at ¶60,200 *et seq.*

Overview

The Government has amended the federal Pension Benefits Standards Regulations, 1985, following through on the commitment made in Budget 2008 to increase the choices available to holders of federally regulated Life Income Funds (LIFs) with regard to unlocking their funds. Moreover, in the interest of reducing the administrative burden upon some of the individuals that the changes are intended to benefit, regulatory changes have also been made with respect to locked-in Registered Retirement Savings Plans (locked-in RRSPs). These amendments are effective May 8, 2008.

Inside

The three new options, which are now available, are as follows:

1. One-Time 50 Per Cent Unlocking: Individuals 55 or older will be entitled to a one-time conversion of up to 50 per cent of LIF holdings into an unlocked tax-deferred savings vehicle.

2. Small Balance Unlocking: Individuals 55 or older with small total holdings in federally regulated locked-in funds of up to $22,450 will be able to wind up their LIFs or convert them to an unlocked tax-deferred savings vehicle.

3. Financial Hardship Unlocking: Individuals facing financial hardship (that is, low income, or high disability or medical-related costs) will be entitled to withdraw up to $22,450 per calendar year.

With the coming into force of these regulations, those with existing contracts will be able to unlock their funds as soon as their financial intermediary can make the necessary amendments.

Individuals who do not wish to use this new flexibility, however, are under no obligation to purchase a new contract. These changes will not affect their existing LIF contracts or locked-in RRSP contracts.

For individuals who do not currently have a LIF or locked-in RRSP but are in the process of establishing such funds, transitional provisions will allow for a six-month adjustment period during which LIF and locked-in RRSP contracts will be permitted to be drafted under the old rules. After this six-month period, financial intermediaries will be required to include new provisions as set forth in the amended regulations into all new contracts related to LIFs and locked-in RRSPs.

Further, the regulatory changes also set forth the terms and conditions for two new types of contracts – Restricted Life Income Funds (RLIFs) and Restricted Locked-in Savings Plans (RLSPs) – that will be permitted under the new regulatory environment.

Under the new regulatory regime, extraordinary withdrawals in circumstances of reduced life expectancy or permanent departure from Canada will be retained for LIFs and locked-in RRSPs, and further will be extended to RLIFs and RLSPs.

Financial institutions and interested individuals should also be aware of the attestations, consents, and forms that will be required under the regulations in order for individuals to avail themselves of the new options for unlocking funds: these will be contained in a new annex to the Pension Benefits Standards Regulations, 1985, contained in Schedule V to those Regulations.

Pension plan administrators should be aware of the changes to the terms of prescribed savings plans to which pension benefit credits may be transferred, and of the new option for transferring pension benefit credits to an RLIF that will be made available. Plan administrators should also be aware of the changes to the form that a member is required to provide to a plan administrator prior to the transfer out of the pension plan of a pension benefit credit of a member or survivor (Form 3 of Schedule I of the Pension Benefits Standards Regulations, 1985).

* * *

Questions and Answers

When do these changes take effect?

The changes take effect immediately. However, financial intermediaries may need some time to update their systems in order to offer these new options.

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Anyone with an existing locked-in RRSP or LIF will have to purchase a new contract to take advantage of this new flexibility.

Those who do not wish to use this new flexibility are under no obligation to purchase a new contract.

A six-month transition period will ensure an orderly transition to the new regime.

Who can unlock funds?

Anyone 55 and older; or anyone facing financial hardship from two sources:

(1) Low income

(2) High medical costs or disability-related costs relative to income.

When can I unlock my funds?

With the coming into force of these regulations, those with existing contracts will be able to unlock their funds as soon as their financial intermediary can make the necessary amendments.

How much can I unlock?

In the year they turn 55, or afterward, people will be allowed to transfer 50 per cent of their funds into a tax-deferred vehicle. In addition, people whose total locked-in holdings are below the minimum threshold – $22,450 in 2008 – or who face financial hardship will also be able to unlock funds.

Where can I obtain the forms required to unlock the funds in my Life Income Fund?

These forms will become available from financial intermediaries that offer LIFs and locked-in RRSPs. If you currently have a LIF or locked-in RRSP, the necessary forms can be obtained from the financial intermediary that holds your LIF or locked-in RRSP contract.

Financial intermediaries and other interested parties can also obtain copies of the necessary forms, which are included as Annexes to the Pension Benefit Standards Regulations, 1985 in Schedule V, Forms 1, 2, and 3.

Why can't I take advantage of these changes without purchasing a new locked-in fund?

The terms and conditions for the unlocking of funds held in federally regulated locked-in RRSPs and LIFs are set down in contracts between the offering institutions and the individuals that hold them. The federal government's role is to provide certain standard rules governing the withdrawal of funds.

The new rules require that all new contracts contain new flexibility options to unlock the funds under certain conditions. However, the federal government will not intervene to change existing contracts signed before the new rules took effect. Therefore, people with LIFs or locked-in RRSP contracts who wish to unlock them should contact their financial intermediary to purchase a new, more flexible contract.

Those who do not wish to use this new flexibility are under no obligation to purchase a new contract.

Will these changes affect provincially regulated pensions?

These changes will only affect those funds that are regulated federally.

Will these changes affect the pensions of those who were or are employed by the Government of Canada?

These measures only affect those individuals who have transferred their pension credits out of their pension plan.

However, the Treasury Board Secretariat is responsible for matters relating to pensions for federal government employees. Therefore, questions about the application of these amendments to federal government employees should be directed to the Treasury Board Secretariat.

Do funds become taxable if they are unlocked?

Yes, but only if they are withdrawn.

Withdrawals from all tax-deferred vehicles are taxable under the *Income Tax Act* or other legislation. People should seek professional advice about their tax implications before making such withdrawals.

Direct transfers of funds from one tax-deferred vehicle to another are not taxable under the *Income Tax Act*.

An example of this would be unlocking funds from an RLIF and placing the proceeds into an RRSP.

Does unlocking funds affect the protection these funds receive from creditors?

Yes, regardless of whether they are withdrawn or not.

Funds that are unlocked – even if they are only transferred to an unlocked tax-deferred vehicle such as an RRSP or RRIF – will lose the protection from creditors provided to locked-in funds.

Has anything been done to protect the interests of the spouses or common-law partners of individuals?

Yes. Those who wish to unlock funds will be required to provide an attestation of assent to this transfer from a spouse or common-law partner. If they do not have a spouse or common-law partner, they must provide an attestation to this effect.

Can I take my pension credits out of my pension, put them in an RLIF, and unlock half the value?

The new rules do not affect a plan member's ability to transfer pension benefit credits out of the plan. The right to do so under certain circumstances is set out in federal pension legislation and may also be permitted by the terms of the pension plan. Where a member has the ability to transfer a pension benefit credit out of the plan, the new rules do permit the pension benefit credit to be transferred into an RLIF, from which half of the value can be unlocked.

What is YMPE? How do I find it out in the future?

The YMPE (Yearly Maximum Pensionable Earnings) is the maximum amount of earnings on which contributions to the Canada Pension Plan (CPP) are based. (Editor's Note: For the current year's YMPE see the CPP/QPP section at ¶30,355).

Can I combine both a 50 per cent unlocking with a small balance extraordinary withdrawal?

Yes.

I have two LIFs. Can I unlock them separately?

Yes, provided all other legislative and regulatory requirements are met.

Can financial intermediaries charge penalties for unlocking early?

Institutions may, at their own discretion, charge transfer fees for LIFs and other such products. Individuals should consult the financial institution that holds their Life Income Fund or locked-in RRSP contract.

Hot News Items

2008 Budget Season Ends

The 2008 Budget season is now over. With this Report the final 2008 Budget has been delivered: Northwest Territories. Highlights of all the Budgets relating to payroll are reproduced below and in the Budgets & New Developments section of PAYSOURCE. All previous 2007 budgets are located at ¶180,162 and ¶180,164.

Northwest Territories

The 2008 Northwest Territories Budget of May 22, 2008, presented by Finance Minister Floyd Roland, contained no new tax increases/decreases affecting payroll.

British Columbia Introduces Reservists Leave

British Columbia will protect the jobs of reservists while they are on active service with the Canadian Forces, Labour and Citizens' Services Minister Olga Ilich recently announced.

British Columbia will join the federal government, New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario, Prince Edward Island, Manitoba and Saskatchewan, which have already amended their respective employment standards legislation to protect reservists' jobs.

Amendments to the *Employment Standards Act* will provide job protection for reservists who temporarily leave their civilian employment in order to serve with the reserve forces.

The unpaid leave would apply to reservists deployed for overseas missions, including pre- and post-deployment duties related to the operation, or domestic emergencies. During those periods, reservists are paid by the Canadian Forces. Employers will not be required to continue benefit and pension contributions while the employee is on leave.

The new provisions apply to all employers covered by the *Employment Standards Act*.

The amendments are contained in Bill 43, *Miscellaneous Statutes Amendment Act (No. 2)*, 2008, which received first reading April 30, 2008 and second reading May 15, 2008. The progress of the Bill will be noted in future Reports.

Newfoundland and Labrador Reservists Leave

Bill 1, *An Act to Amend the Labour Standards Act to Provide for Leave for Reservists*, previously summarized in the April issue of *PaySource*, No. 154, will become law when Bill 1 receives Royal Assent at the end of the current spring legislature.

Newfoundland and Labrador now joins the federal government, New Brunswick, Nova Scotia, Ontario, Prince Edward Island, Manitoba and Saskatchewan, which have already amended their respective employment standards legislation to protect reservists' jobs.

Amendments to the current legislation allow reservists to be away on unpaid leave for the period of service which includes training and any period of time for treatment, recovery or rehabilitation in respect of a physical or mental health problem that results from service. In order to meet eligibility requirements, the applicant must have at least six months of employment with his or her employer and provide the employer with 60 days' notice of intention to take leave. The notice must give the date on which the leave will begin and the anticipated date on which his or her service will end. In addition, documentation from the Canadian Forces and from the employee requiring leave must be provided upon the request of the employer.

Reservists are also entitled to reinstatement in the position they held prior to the leave or in an equivalent position. However, unless the employer and the employee otherwise agree, the period of reservists leave does not count towards seniority/length of service and, therefore, also does not count with respect to accrual of vacation entitlement, required notice of termination etc. The period of employment following leave is, however, considered to be continuous with the period worked before the leave.

The new Newfoundland and Labrador Reservists Leave has been incorporated into the employment standards section of PAYSOURCE at ¶5930.

Need To Know

CRA Questionnaire – Parking as a Taxable Benefit

The CRA Web site has been revised to provide a questionnaire to help you determine if an employer-provided parking spot is a taxable benefit to the employee: www.cra-arc.gc.ca/tax/business/topics/payroll/benefits/automobile/parking-e.html.

British Columbia Farm Worker Protection

During Farm Safety Week in British Columbia, the government introduced legislation to improve farm worker protection.

Amendments made by the Bill to the *Employment Standards Act* that prohibit farm producers from hiring farm labour contractors who are not licensed, and that provide for the cancellation or suspension of a farm labour contractor's licence for safety violations, came into force on Royal Assent. Other amendments, which require contractors to pay for alternative transportation of affected employees when an unsafe farm labour contractor's vehicle is taken off the road following a roadside check, will come into force by Regulation.

The provisions of the Bill that will improve the timeliness of decision-making with respect to applications and complaints to the Labour Relations Board, and will make an administrative change to the *Workers Compensation Act*, will also come into force by Regulation.

The amendments are contained in Bill 13, the *Labour and Citizen's Services Statutes Amendment Act, 2008*, which was previously summarized in the April issue of PAYSOURCE, No. 154.

Bill 13 received first reading March 13, 2008, second reading April 1, 2008, third reading April 7, 2008, and Royal Assent May 1, 2008.

Lastly, the Bill will make changes to the *Freedom of Information and Protection of Privacy Act* to make it a more potent piece of legislation.

Manitoba Child and Foreign Worker Protection Legislation Introduced

Manitoba has introduced legislation to better protect two vulnerable groups, children and youth in the modelling industry and foreign workers, from unscrupulous recruiters. Bill 22, the *Worker Recruitment and Protection Act*, would, if passed, repeal the *Employment Services Act*, which currently governs the activities of third-party placement agencies in Manitoba.

With respect to children and youth in the modelling and talent industry, the Bill proposes to decrease their vulnerability by:

- regulating the activities of talent and modelling agencies through licensing;
- ensuring that fees are not linked to the child's opportunity to find work; and
- instituting strict requirements for children being promoted by the industry, including child work permits.

With respect to foreign workers, the Bill would offer increased protections by:

- requiring all employers to register with the province before recruitment of foreign workers begins;
- regulating the activities of recruiters through licensing; and
- prohibiting recruiters from charging workers fees, either directly or indirectly, for recruitment.

The Director of Employment Standards would have the authority to refuse or revoke a licence, and to investigate and recover for workers or children money they have paid to be recruited or represented by an employment agency, a child talent agency, an employer, or a recruiter of foreign workers or child performers.

Bill 22 received first reading on April 7, 2008 and second reading May 22, 2008. The progress of the Bill will be noted in future Reports.

Recent Cases and Rulings

Dismissal of employee during probationary period justified

• • • **British Columbia** • • • Pekrul had worked with her former employer for a number of years, and eventually decided to look for a position with a greater challenge and opportunity to earn more. She wanted a new job where she could upgrade her skills, increase her salary, work without probation and have immediate benefits. She applied to Flexmaster, and was offered a position. Pekrul believed that she was offered the position without a probationary period, while Flexmaster believed she had been hired on a three-month probationary period. Pekrul accepted the offer, and resigned from her former employer. When she was terminated during the first three months on the job, Pekrul brought a wrongful dismissal complaint.

The complaint was dismissed. Clearly, Pekrul was not induced to leave her former employer, since she had actively been engaged in a job search for over six months when she accepted the job with Flexmaster. With respect to the probationary period, the Court accepted the evidence of the employer that it was a term of Pekrul's hire that there would be a three-month probationary period. During the short period of time when Pekrul was employed, there was a series of incidents that raised concerns about her suitability with the company, including smoking inside the building, attending a job interview for a different job, acting in a bossy and argumentative manner, and handling customers in an aggressive manner. Flexmaster reasonably and fairly considered Pekrul during her probationary period, and concluded that her assertive nature, her apparent inclination to pursue authority and control, her relationship with other employees, and a perceived tendency to "shade the truth" in pursuit of those goals made her unsuitable for the position within the employer's organization.

Pekrul v. Flexmaster Canada Limited, (B.C.S.C.), 2008 CLLC ¶210-016.

Dismissal not justified where distraught employee took leave without notice

• • • **Ontario** • • • Smith had worked for the Town of Ramara ("Ramara") for 18 years, most recently as a heavy equipment operator. At the end of May 2006, he and the other employees in the roads' department were told that overtime would be expected because of the amount of work to be done. Smith had separated in January 2005, and by May 2006 he was experiencing the stress of the loss of a family relationship, his farm, and a place to live. As a result, the overtime was an additional stress that he did not believe he could handle, so he asked for time off on vacation or stress leave. His supervisor agreed, which Smith believed meant that he could take the necessary time off, but his supervisor believed that he would still have to receive permission from the superintendent. Smith then unilaterally started taking time off based on his allotted vacation time, without informing anyone that he was going to be off work, or how long he would be off. Ramara viewed his prolonged period of absence from work as a fundamental breach of the employment contract, and justified termination. Smith brought a wrongful dismissal claim.

The claim was allowed. There was evidence that there was a high degree of flexibility at the workplace, since all of the employees had worked together for many years. In addition, it was clear that Smith would have been entitled to stress leave if he had communicated appropriately with Ramara. An employer is entitled to expect employees to show up for work unless vacation or leave time is arranged, and Smith did not communicate his intended vacation time. However, given the flexibility in the workplace, Smith's entitlement to vacation, the fact that others in the company knew his personal circumstances and how to contact him, his overwhelmed state of mind, his irrational reliance that it would all work out, and his long, unblemished employment record, the Court found that termination was not justified. Smith was awarded 12 months' reasonable notice for wrongful dismissal.

Smith v. Corporation of the Town of Ramara, (Ont. S.C.J.), 2008 CLLC ¶210-017.

Automobile Standby Charge – Inclusion of Management Expenses in Leasing Costs

The situation considered by the CRA involved the company ACO which provided automobile fleet management services to its clients whose remuneration policies involved the provision of automobiles to some of their employees. The agreement between ACO and a client allowed the eligible employee to select a particular automobile. The company would then purchase the vehicle and lease it back to the client who would become responsible for the vehicle during the term of the lease, at its maturity, and for the residual value of the vehicle. In addition to the lease of the vehicle as such, ACO would provide the following services to the client: (1) purchase of the vehicle at the dealer; (2) registration of the vehicle; (3) signature of documents and delivery of the vehicle to the employee; (4) preparation of monthly reports for all vehicles leased by the client; (5) follow-up on the return of the vehicles on or before maturity of the lease; (6) sale of vehicle at the end of the lease; and (7) annual calculation of the tax benefit of each employee. The CRA was asked if the management fees in respect of the services described in points (1) to (7) above (that would be invoiced separately from the lease charges by ACO to the client) would have to be taken into consideration to calculate element E of the formula to calculate the employee's reasonable standby charge contained in subsection 6(2) of the Act.

The CRA confirmed that, except for the management expense (7) concerning the annual calculation of the tax benefits of the client's employees, all the other management expenses would be considered a "lease cost" for the purpose of calculating element E of the formula used to calculate the employee's standby charge under subsection 6(2). Even if the question of whether the above management expenses were incurred for the purpose of leasing an automobile is a question of fact to be determined from a review of the leasing contract and the intrinsic purpose of the payment made by the client, the CRA considered that the lease costs included not only the costs related to the enjoyment of the automobile by the employee but also the other costs that are associated with the purchase, delivery, resale, etc., of said automobile. Subsection 6(2) of the Act clearly indicates that the lease costs would include the amounts that the employer (client) would be required to pay to the lessor (ACO), except for liability and collision insurance costs. For more details on the meaning of the expression "lease costs", see paragraph 13 of IT-63R5 and the section entitled "Calculating automobile benefits: Calculating a standby charge – Your leasing costs" in Chapter 2 of the CRA Guide T4130 "Employers' Guide – Taxable Benefits".

Technical Interpretation, Business and Partnerships Division, March 13, 2008, Document No. 2008-0270151E5.

Employer-Provided Gifts and Awards

The CRA's policy regarding non-taxable gifts and awards provided to employees is discussed in Income Tax Technical News No. 22. It does not apply to cash or near-cash gifts, which are considered to result in a taxable employment benefit. Consistent with this, it is the CRA's view that "employees permitted to select a gift or award from a store or from a restaurant are essentially in the same position as employees receiving gift certificates".

It is also the CRA's view that a taxable benefit will arise from "employer-provided 'hospitality' functions, such as team building lunches, other motivational occasions, lunches/dinners or other similar functions that are in the nature of a 'thank you' from the employer for doing a good job or completing a job within a specified time frame except where the event is generally available to all employees in an employer's particular place of business".

Technical Interpretation, Business and Partnerships Division, March 13, 2008, Document No. 2007-0247981E5.

Distinctive Uniform – Shirt with Employer's Logo

As indicated in Interpretation Bulletin IT-470R: "An employee who is supplied with a distinctive uniform which is required to be worn while carrying out the duties of employment . . . is not regarded as receiving a taxable benefit".

It is the CRA's view that a shirt bearing an employer's logo can be considered a distinctive uniform. An employee would generally not be in receipt of a taxable benefit if the employer provides the employee with, or reimburses the employee with respect to, the cost of a shirt with the employer's logo that he or she is required to wear in the course of the individual's employment.

Technical Interpretation, Business and Partnerships Division, February 25, 2008, Document No. 2007-0237891E5.

Private Health Services Plans – Premiums Paid by an Employer for Retired Employees under the Basic Prescription Drug Insurance Plan

It is the view of the CRA that the premiums paid by an employer under the Basic Prescription Drug Insurance Plan in respect of individual insurance policies purchased for its retired employees would not constitute a taxable benefit by virtue of the exception under subparagraph 6(1)(*a*)(i) of the Act applicable to any private health services plan. The CRA relied on the definition of "private health services plan" included in subsection 248(1) and more specifically on the description of the coverage described in paragraph 4 of IT-339R2 to conclude that the Basic Prescription Drug Insurance Plan clearly qualified as a private health services plan. For more details on this topic, see also Technical Interpretation No. 2006-9721167. The CRA noted that the fact that the insured individuals were retirees, not employees, and that the portion of the premium paid by the employer in respect of the Basic Prescription Drug Insurance Plan was in respect of an individual, not a group plan, was not relevant in deciding whether the payment constituted a taxable benefit or not.

Technical Interpretation, Business and Partnerships Division, March 17, 2008, Document No. 2006-0216751E5.

Private Health Services Plan – Default Allocation under Flexible Benefit Program

In a situation the CRA was asked to comment on, an employee elects to take life insurance coverage under a flexible benefit program. The election is made before the beginning of the plan year and includes a stipulation that if the life insurance coverage is declined by the insurer, the flex credits that would have applied to the life insurance coverage will be added to the individual's health care spending account.

It is the CRA's view that the default allocation, in these circumstances, would not affect the status of the health care spending account as a private health services plan.

Technical Interpretation, Business and Partnerships Division, February 21, 2008, Document No. 2007-0227881E5.

Northern Residents Deduction – Nearest Designated City

As noted in Window on Canadian Tax, ¶8388, the determination of the "designated city that is nearest" for the purpose of Regulation 7304(2)(*c*) would be the "one reachable by means of public travel such as roads, highways, railways, ferries, etc. using the most reasonably direct route" (*Dianne M. Giannokopoulos v. The Queen*, 95 DTC 5477 (F.C.A.)).

In a situation the CRA was asked to comment on, the two nearest designated cities to Churchill Falls, under Regulation 7304(1)(*c*), are Moncton and St. John. There are no direct flights to either city. Travel to Moncton is via Goose Bay and Halifax. Travel to St. John is via Goose Bay and Deer Lake. In this situation, the total flight distance to St. John (via Goose Bay and Deer Lake) is the shortest route.

Technical Interpretation, Business and Partnerships Division, March 17, 2008, Document No. 2007-0239391E5.

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