Submission

on the

2018 Federal Budget

to the

House of Commons Standing Committee on Finance

by the

Canadian Life and Health Insurance Association

Canadian Life and Health Insurance Association
79 Wellington St. West, Suite 2300
P.O. Box 99, TD South Tower
Toronto, Ontario M5K1G8
416-777-2221 www.clhia.ca

canadienne des compagnies d'assurances de personnes
79, rue Wellington Ouest, bureau 2300
CP 99, TD South Tower
Toronto (Ontario) M5K 1G8
416-777-2221 www.accap.ca

Toronto • Montréal • Ottawa

EXECUTIVE SUMMARY

The Canadian Life and Health Insurance Association (the "CLHIA") is pleased to provide its recommendations for the upcoming 2018 Federal Budget. Our recommendations align with the Government's priorities ***to support the middle class, create jobs and set the right conditions for long-term prosperity for Canadians.***

Canada's life and health insurers play a key role in Canada's economy. We protect over 75% of Canadians through a wide variety of life, health and annuity products. The industry paid over $84 billion (more than $1.6 billion a week) in benefits in 2015, with over 90% paid to living policyholders. Almost 150,000 Canadians work within the sector (as employees or independent agents). The industry is a major investor in Canada with more than $760 billion in assets, nearly 90% of which comprise long-term investments, providing an important source of stable capital for the federal and provincial governments and businesses. Canadian life insurers contributed over $2 billion in corporate, capital, sales and other taxes to the federal government for the 2015 calendar year. Canada's life insurers have a long record of operating in international markets, with over $67 billion (or 42%) of their premiums coming from outside Canada.

In this submission, we recommend the following four initiatives that align with the Government's key priorities for the 2018 budget*:*

1. ***Encourage private sector investment in infrastructure***

2. ***Enhance retirement income security***

3. ***Reduce or eliminate capital tax on financial institutions***

4. ***Further international trade and tax competitiveness***

Our recommendations are sustainable, prudent and will help drive prosperity for all Canadians.

1. ENCOURAGING PRIVATE SECTOR INVESTMENT IN INFRASTRUCTURE

The CLHIA commends the Government focus on providing much needed long-term support for public infrastructure. Effective long-term investments will benefit Canadian productivity and competitiveness and help drive economic growth. As part of this effort, the CLHIA is supportive of the creation of the government's new Canada Infrastructure Bank.

With over $690 billion in long-term investments, Canada's life and health insurance industry is already a significant investor in Canada's economy. Canadian life and health insurers have invested over $40 billion in domestic infrastructure and have a strong desire and capacity to invest more. In addition the diversity within Canada's life and health insurance industry - both in terms of scale and regional vs national focus - means insurers are ready and able to invest in smaller, local, projects (e.g. $50 million), which large pension funds would not consider.

Canada's life and health insurers are ready to be a key partner with government to get infrastructure projects built across the country. ***We recommend the Infrastructure Bank work with the private sector to expand our strong, existing, role in infrastructure investment in Canada. To this end, we encourage predictable and transparent government policies and regulations that are designed to encourage private investors, including Canadian life and health insurers.***

As part of the Government's infrastructure efforts, public-private partnerships (P3s) can play an important role in stimulating long-term investments without imposing the burden of development and start-up costs on governments. P3s are also an attractive long-term investment for the life insurance industry to match our long-term liabilities. By implementing more infrastructure projects as P3s, governments can employ the private sector's expertise on governance and execution to deliver projects on time and within budget.

The bulk of Canada's $400 billion infrastructure deficit is at the smaller municipal government and First Nations' level. Active collaboration between all levels of government and the private sector to develop a comprehensive long-term plan to fund and facilitate identified needs at the local level will help speed projects to market and reduce the infrastructure deficit. ***We recommend the federal government support P3 partnerships through the Building Canada Fund and collaborate with private-sector stakeholders to develop new ways to bundle small projects together to make them attractive investments.***

2. ENHANCING RETIREMENT INCOME SECURITY

Increasingly large numbers of Canadians are expected to enter retirement without the security of retirement income from defined benefit pension plans. Old Age Security and the Canada/Quebec Pension Plan will be the primary sources of secure, guaranteed, income payable for life for these Canadian workers during retirement. While the recently adopted expansion of CPP will ultimately improve guaranteed lifetime income payments to retirees, the effects of that change will not be realized for decades. For many Canadian retirees, there is an increasing need to convert some or all of the savings accumulated in their defined contribution pensions, RRSPs, RRIFs, PRPPs, and TFSAs into guaranteed lifetime income streams. Below are some options that can be considered by the federal government to enhance retirement security:

a) Annuities payable for life are the most effective way to provide such guaranteed incomes. But requiring Canadians to wait until retirement to choose such income options exposes them to significant "interest rate" risk, since the income that can be provided from an annuity depends on market rates when they make that choice. One way to minimize this risk and increase retirement incomes is to allow gradual annuity purchases prior to the cusp of retirement, even though income payments from those annuities will not start until retirement or later. Unfortunately, such "laddering" of “deferred annuity” purchases over several years appears to conflict with current tax and pension law (although such purchases were permitted prior to 1980, and are still permitted in some pension plans).

b) In light of increasing life expectancies and currently low interest rates, it would make sense to permit some further flexibility beyond retirement, allowing consumers within tax-deferred plans to retain investment control and exposure to investment market growth to a later date. For instance, a holder of a RRIF might choose to purchase laddered annuities within that plan, to increase guaranteed lifetime income commencing at age 80 or later. As well, allowing consumers to use part of their tax-deferred savings prior to, for instance, age 65 to provide a guaranteed income starting at age 85 or later may provide significant longevity protection to individuals, and reduce the long-term cost of public income security programs.

c) While Tax Free Savings Accounts (TFSAs) are an important savings vehicle, they are primarily designed as liquid, short- to medium-term plans to allow Canadians access to their savings. But many Canadians are using TFSAs to supplement their retirement income. Some consumers may want to exchange TFSA liquidity and residual value on death for higher guaranteed lifetime incomes. Allowing Canadians to waive liquidity rights would permit life annuities to be held within TFSAs, efficiently meeting demand for guaranteed lifetime income. Such a waiver would not be needed until a holder elects a guaranteed income (at age 55 or later), preserving liquidity until that time.

These options would allow individuals within tax-advantaged savings and retirement plans to "lock in" guaranteed income streams at opportune times while adding no cost to the tax system, since those savings are already exempt from tax reporting until actually paid out of such plans.

We recommend the government review alternatives to allow Canadians to avoid undue risks from longevity and low investment yields and choose secure, guaranteed, lifetime incomes through the purchase of life annuities on a gradual basis, increase consumer flexibility for a range of guaranteed income options, and enhance the flexibility of TFSAs for retirees.

3. REDUCING OR ELIMINATING CAPITAL TAX ON FINANCIAL INSTITUTIONS

Internationally, governments continue to strengthen regulatory capital requirements of financial institutions (FIs) to protect consumers and prevent the need for costly taxpayer bail-outs. Canada is no exception. However, Canada is the only major country to also levy a tax on the very same regulatory capital held to protect consumers.

In 2015, life insurers paid over $270 million in federal capital taxes in addition to the income taxes paid on corporate profits. While the CLHIA has repeatedly advocated eliminating this tax, the introduction of a new regulatory capital framework in 2018 will further increase the capital tax burden of life insurers, making capital tax even more punitive than it is today.

Capital tax perversely increases life insurers' cost of capital both directly and indirectly, limiting their ability to strengthen capital levels, to underwrite additional risks, and to provide greater protection for Canadians. This contrasts with the Government's general policy to reduce the "hurdle rate" for new investments for manufacturers and other businesses by providing tax incentives such as accelerated capital cost allowance and other tax credits. Studies generally indicate that a 10% increase in the cost of capital leads to a 7% to 10% reduction in investment in the long run.

As the only nation in the G20 to impose such a tax, it is time for the Government to eliminate capital tax on Canadian financial institutions to encourage their competitiveness. If elimination is not possible in the short term, ***the CLHIA recommends that the capital tax rate be reduced immediately to ensure reasonable recoverability against corporate income tax***. Such clear Government action would send an unequivocal message that capital accumulation by FIs to protect consumers is encouraged and supported.

4. FURTHERING INTERNATIONAL TRADE AND TAX COMPETITIVENESS

Canadian life and health insurers are strongly supportive of the Government’s efforts to increase Canada’s trade through international agreements. Implementation of the Comprehensive Economic and Trade Agreement (CETA) with the European Union will set Canada apart from its peers as a country with an ambitious trade agenda. We look forward to working closely with the Government as it enters negotiations to modernize the North American Free Trade Agreement (NAFTA). We encourage the Government to continue to promote a progressive trade agenda globally.

International trade is also heavily influenced by regulatory and tax frameworks in the home and host jurisdictions. Canada has traditionally balanced immediate domestic objectives with furthering international trade, evidenced by the global success of Canadian multinationals, including life insurers. In this context, the industry is increasingly concerned by the OECD's initiatives regarding Base Erosion and Profit Shifting (BEPS) and the potential for harmful tax effects. It is important to ensure that any new regulatory or tax proposals do not result in any unintended consequences to global trade and, in particular, the Canadian economy.

Canada's life insurers strongly urge the Government to continue to focus on evidenced-based policy choices on the BEPS initiatives, after thorough consultation with stakeholders. Domestic measures should not disadvantage the tax competitiveness of Canadian multinationals in the global marketplace.