



Pension Plan Options when you terminate your Employment

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This article covers the four most common pension options that are available when you terminate employment, and suggests ways you can choose the best option for your situation more easily.

Understanding your alternatives

Whether you are retiring, starting a new job or taking time off, leaving an employer can often be an emotional time. Financial concerns and the need to make some important decisions, such as what to do with your pension, may add to your stress level, at least in the short term.

If you have been a member of a pension plan for many years, the benefits that you have earned in the plan could likely be the largest source of income you will receive in retirement. Deciding what to do with this income involves many variables and can be quite confusing. And, once you make a decision, it is often irreversible.

Because of this, it is essential you get the advice you need from someone who is familiar and experienced with analyzing this type of decision. A financial advisor can help you make the most appropriate choice for your specific circumstances. Advisors also have access to a wide range of information and sophisticated forecasting tools and calculators that can help you analyze your options. Working with your advisor and pension and benefits representative or human resources specialist, you will be better able to select the option that is best for you and your family.

Which choices you have, when you will receive the money, how much money you will receive and how your spouse and other dependants may be affected will all depend on your specific pension plan as well as the applicable legislation that governs the benefits you have accumulated. Since many of these details depend on whether your pension plan is governed by federal or provincial legislation, this report will focus on the general options that are common to most jurisdictions.

What happens when you terminate your employment?

Prior to or shortly after you have terminated employment, your employer should send you a written summary outlining your company pension plan options. You will be required to select one of the options by a specific deadline. Sometimes you may not have very much time to make your decision. And if you don't act before the deadline, your employer may consider that you have chosen one of the options by default, which may or may not be the best one for you. This is why it's so important to get the guidance you need to help you make the best decision quickly.

Reviewing your options

Speaking with your pension and benefits representative is the best way to find out about the specific options available to you when you terminate employment. The choices will vary significantly from plan to plan, but generally include the following:

OPTION 1: REMAIN IN THE PENSION PLAN

You may be able to stay in the company pension plan, but stop contributing to it. This option may be available for both defined benefit and defined contribution pension plans.

If you are a member of a defined benefit pension plan, the benefits you've earned as a result of your accumulated service up to the time of your termination will be paid to you on a monthly basis for your lifetime, beginning at an agreed-upon age. If you decide to take this option, you may still have several decisions to make.

Depending on your age at the time you stop working, you may have the choice of beginning your pension benefits immediately or deferring the benefits until a later date. If you defer your pension, you will generally receive a higher monthly amount than you would if you took your pension immediately.

If you do not require pension income immediately because you have a new or alternate source of income, you may want to consider receiving it at a later date if you are given the choice. If you have not yet reached the age at which the plan allows you to receive benefits, you may be able to choose the future date that your deferred pension will begin under this option.

If you have a spouse (as defined in your plan), they will be entitled to receive survivor benefits following your death, usually at a reduced level, for the remainder of their lifetime. Your employer may provide you with the option to select enhanced survivor benefits for your spouse — but there's a cost. Typically, if you opt for enhanced survivor benefits, the initial amount of your pension benefits will be lower.

If you decide to remain in the pension plan, choosing the appropriate level of survivor benefits (if the choice is available) will be a critical decision. The age, health and life expectancy of you and your spouse should be considered carefully. Also, the degree to which your spouse and any other dependants may need to rely on this income to meet their expenses is an important consideration.

If you decide to remain in the pension plan, you should be aware that many defined benefit plans are designed to provide a higher level of benefits from the time that payments begin until the age at which certain government benefits, such as the Canada or Quebec Pension Plan (CPP/QPP) and Old Age Security (OAS) are scheduled to start (usually age 65), and a reduced level of benefits afterwards. Pension plans that are designed this way are referred to as being “integrated” with CPP/QPP or OAS. Knowing how your plan is designed will help you make the right choices about when and how to draw on your other sources of retirement income.

You may need to make some other decisions as well if you decide to remain a member of the pension plan. Your advisor, together with your pension and benefits representative or human resources specialist, can help you work through these important decisions.

OPTION 2: PURCHASE AN ANNUITY

You may be able to instruct your employer to transfer the value of your pension to an insurance company to buy an immediate or deferred annuity. The annuity will pay you a set income beginning at the age set out in the annuity contract.

Annuity contracts produce a predictable, recurring income stream. These contracts are available with many different features and benefits. The level of benefits to a surviving spouse may be customized.

The annuity option is similar to Option 1 in that it pays a regular monthly payment. Note that once you have decided to purchase an annuity, the decision cannot be reversed. So, you should carefully evaluate the pros and cons of this alternative before you buy.

OPTION 3: TRANSFER YOUR PENSION VALUE TO A LIRA OR LOCKED-IN RSP

A third option is to transfer the commuted value of your pension to a locked-in RSP or a locked-in retirement account (LIRA). This allows you to invest the money yourself and decide when you want to begin withdrawing it, subject to age restrictions and annual minimum and maximum amounts.

Note that in order to receive income, you will need to convert your LIRA/locked-in RSP to a life income fund (LIF) or annuity; or in some provinces an additional option is a locked-in retirement income fund (LRIF) or prescribed retirement income fund (PRIF). Detailed information on these types of plans is available in our publication *Locked-in RSPs and Your Options*.

By taking control of your pension money, you can choose from a wide range of investments and design a portfolio that is customized to your specific objectives in terms of producing income, offering growth and providing liquidity to make the payments that you need in retirement.

Managing your pension money yourself gives you more flexibility than remaining in the pension plan or purchasing an annuity:

- Withdrawals may begin as early as the age your pension would have started, if needed.

- You can begin to withdraw funds and then stop the withdrawals at a later date, if you no longer need the income, by transferring the funds back into a locked-in RSP/LIRA (provided that it is not yet the end of the year in which you turn 71).
- If you do not need the income, you are not required to withdraw funds until the year in which you turn 72. This allows the funds to continue to grow, tax-sheltered, until they are needed.
- You may decide to withdraw more or less in any given year, as the funds are needed, subject to a maximum and minimum in any given year.
- By deciding how much to withdraw in any given year, you have greater control over your level of taxable income. In some cases, you may be able to control your eligibility for certain income-tested government benefits such as OAS or the guaranteed income supplement (GIS).
- Some strategies are available to “unlock” certain amounts of money held in a locked-in plan and transfer them to a regular registered plan where withdrawals are not restricted.
- You can, at any time, choose to use part of your locked-in funds to purchase an annuity contract, if appropriate. Note that this option might produce a pension adjustment reversal (PAR), which could increase your RRSP deduction room.

The Income Tax Act limits how much pension money you can transfer to a locked-in RSP or LIRA, so you may not be able to contribute all the money from the pension to this type of account. If the value of your pension exceeds the amount that can be transferred, the balance that you are owed will generally be payable to you in a lump sum and taxed in the year it is paid.

While receiving a taxable amount may appear to be a drawback, this option may have certain benefits:

- In many cases a lump sum of money is needed for immediate uses such as repaying debt before you retire or funding a large expense, purchase or other project.
- If you have unused RRSP deduction room, you may be able to make a large contribution to your individual plan or spousal plan, where appropriate. This could defer the taxation of part or all of the lump sum that you receive.

OPTION 4: TRANSFER THE VALUE OF YOUR PENSION TO A PENSION PLAN OF A NEW EMPLOYER

In some cases, if you are not retiring, you may be able to transfer the vested amount of your pension into a new employer's pension plan. If a new employer provides you with the option to participate in a defined benefit pension plan, this transfer will involve exchanging some or all of the value of your pension for a certain number of years of "pensionable service" in the new plan. Note that this is possible only if your new employer is willing to accept the transfer.

Making the best decision for you and your family

The following are the main considerations that are likely to influence your decision as to which option, or combination of options, is best for you and your family:

- Flexibility to access regular income and lump sums
- Benefits available to your surviving spouse or others upon death
- Investment management — degree of your involvement in making decisions
- Investment risk — impact of strong or weak investment performance on your retirement income
- Access to ancillary benefits that may be contingent on membership in the company pension plan

The table below summarizes the general implications of each of these considerations (except for potential access to ancillary benefits, which is discussed in the next section) for each of the four options outlined in this report.

The information in the table that deals with remaining in a pension plan applies to defined benefit pension plans, not defined contribution pension plans. The considerations for defined contribution pension plans are significantly different. If you belong to a defined contribution pension plan, please ask your advisor for guidance that's appropriate to your particular case.

	Flexibility	Survivor benefits and estate planning	Investment management and investment risk
Option 1 Leave pension with employer	<p>No ability to modify payments once they begin. Benefits are payable for life of annuitant.</p> <p>No ability to access lump sums from the pension plan.</p>	<p>Survivor generally receives a reduced monthly payment for the remainder of their lifetime.</p> <p>Enhanced protection may be available, at a cost, when initial choice is made.</p>	<p>All investment management decisions are made by pension plan administrator.</p> <p>Pension plan assumes risk associated with investment performance.</p>
Option 2 Purchase an annuity	<p>No ability to modify payments once they begin.</p> <p>No ability to access lump sums from annuity contract.</p>	<p>Details agreed to when annuity is selected. Various options are available to provide protection to surviving spouse and/or estate.</p>	<p>Insurance company assumes risk associated with investment performance.</p>
Option 3 Transfer to a LIRA/ locked-in RSP	<p>Flexible amount of income may be taken each year, subject to minimum and maximum amounts.</p> <p>Some flexibility to delay receipt of income and allow LIRA/locked-in RSP to grow in value, subject to age limits.</p> <p>Some flexibility to withdraw lump sums and/or “unlock” funds for increased availability at a later date.</p>	<p>Surviving spouse may receive 100% of remaining plan value on a tax-sheltered basis.</p> <p>After-tax proceeds, generally payable to estate or other beneficiaries if there is no surviving spouse.</p> <p>In some cases, surviving spouse may have increased access to lump sums if needed.</p>	<p>Annuitant may select desired degree of involvement and choose from wide range of investment solutions.</p> <p>Annuitant benefits from strong investment performance and assumes risk of weak investment performance.</p>
Option 4 Transfer to a new employer pension plan	<p>Options to be determined upon retirement or termination of membership in new plan.</p>	<p>As outlined in the terms of the new plan.</p>	<p>This is not a consideration until retirement or termination of plan membership if the new employer pension is a defined benefit plan.</p>

Continue to protect yourself and your family

In some cases, your employer may offer you ancillary benefits such as continued access to group health, dental and insurance plans on the condition that you remain a member of the company pension plan.

This is something that you should investigate and consider carefully. If you lose the coverage from your employer, you may qualify for benefits under your partner's employee group benefits; if you don't, you may want to replace the coverage to maintain the protection.

Check with your human resources department or pension and benefits representative to find out how long you will be covered under the company benefits plan. You might want to see if you can convert to personal coverage with the same insurance company, at your own expense, when your company coverage ends. This can be a cost-effective decision in the long run.

How do you choose?

When analyzing which pension option is best for you, essentially, what you are trying to determine is which option will provide you with the best cash flow throughout your retirement at a risk level that allows you to sleep at night. In many cases, you will also want to choose the option that will provide the largest benefit to your spouse or to your estate upon your death.

While it may seem difficult to know which is best for you and your family, we can explain your options and help you make an informed decision. If you are able to provide the relevant information, an advisor who is experienced with these matters will be pleased to prepare a customized analysis of your situation and make a recommendation based on all of the important considerations that are unique to your specific personal goals and circumstances.

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