Locked-In RSPs And Your Options

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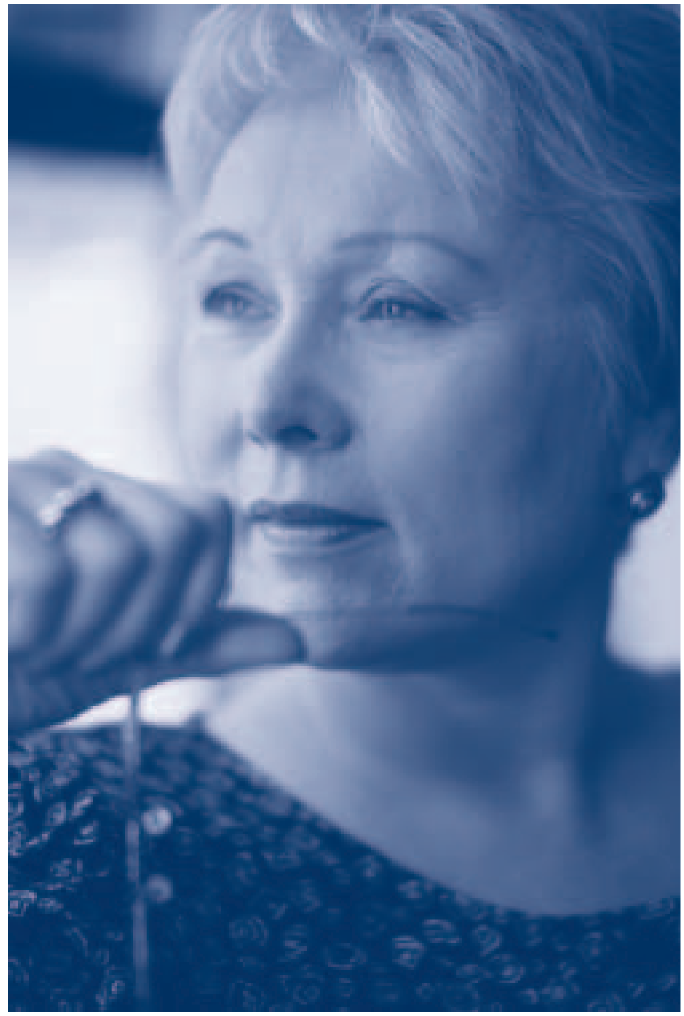
1 › Introduction

For most individuals, their employer pensions represent the single most significant retirement asset, the cornerstone of their retirement.

Quite often however, individuals are presented with an opportunity to take their employer pensions in the form of a lump sum payment. This publication has been written to explain why this is possible and to discuss the various issues surrounding the “locking-in” of commuted pension plans.

The “locking-in” rules set forth in this publication are based on the federal tax and pension law and the provincial pension law in effect as of the date of this publication. (June 2005)

2 › Locked-in RSPs and LIRAs



A locked-in RSP or locked-in retirement account (LIRA) is created when the commuted (lump sum) value of the employer and employee's vested contributions plus interest are transferred from a Registered Pension Plan (RPP) to an RSP.

The locked-in RSP and the LIRA have virtually identical attributes. No contributions can be made to these accounts.

British Columbia and Nova Scotia continue to use the term locked-in RSP. However, the provinces of Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick and Newfoundland & Labrador have adopted LIRAs to designate the account into which assets are transferred from pension plans.

The province of Prince Edward Island does not yet have any legislation in force that deals with locked-in accounts. Therefore PEI residents should refer to their specific pension plan documentation.

The options to receive income out of a locked-in RSP/LIRA are as follows:

1. Purchase a life annuity at any time before the end of the year in which an individual reaches the age of 69*.

2. Transfer the funds to a Life Income Fund (LIF) at any time before the end of the year in which an individual reaches the age of 69*.

3. In Alberta, Manitoba, Ontario and Newfoundland & Labrador transfer the funds to a Locked-In Retirement Income Fund (LRIF) at any time before the end of the year in which an individual reaches the age of 69*.

4. In Saskatchewan, transfer the funds to a Prescribed Retirement Income Fund (PRIF) at any time before the end of the year in which an individual reaches the age of 69*.

** Most provinces have a minimum age restriction on the conversion to an annuity, LIF, LRIF, or PRIF. See Figure 5 on page 9 for details.*

3 › Life Income Fund (LIF)

The LIF is similar to a RIF (Retirement Income Fund), to the extent that an individual must receive at least the annual minimum payment from a LIF. However, it differs in that there is also a maximum payment allowed. The minimum LIF payment calculation is identical to the minimum RIF calculation. See **Figure 1** for details of this calculation.

The maximum payment percentage is an actuarial calculation based on a person's age and an interest rate factor known as the CANSIM rate. As the CANSIM rate is reset every year (in November) the maximum payments will fluctuate to the extent that future payouts can only be approximated. **Figure 2** (next page) provides the LIF minimum and maximum payment rates in effect for 2005.

The LIF differs from a RIF in one other significant way. The LIF requires conversion to a life annuity by the end of the year in which the individual turns age 80 versus the RIF, which can continue throughout the individual's lifetime. Note that this mandatory conversion is not required in B.C., Manitoba, Quebec, Nova Scotia or New Brunswick; however, the New Brunswick LIF assets must be exhausted by age 90. At the time of printing this publication, Federal pension legislation is being amended to remove the requirement for locked-in federal plans to be converted to an annuity at the age of 80.

FIGURE 1

HOW LIF PAYMENTS ARE CALCULATED

Minimum Payment

$$\text{Minimum Annual Payment} = \text{Plan Balance at December 31 of previous year} \times \frac{1}{90 - \text{age at December 31 of previous year}}$$

Note: The provinces of British Columbia, Alberta, Manitoba, Ontario, Quebec, Newfoundland & Labrador and Nova Scotia as well as Federal registered plans allow the younger spouse's age to be used in the calculation of the minimum LIF payment. The province of New Brunswick does not.

The above formula applies until the planholder reaches age 71. At age 71 the new minimum payment schedule for RIFs will take effect (See Figure 2 for actual percentages).

Maximum Payment

Maximum Annual Payment = Plan Balance at December 31 of previous year X Actuarial Calculation based on client's age at December 31 of previous year*

* The actuarial calculation is determined using an average government bond yield (called a CANSIM rate) which changes each year. Therefore the maximum percentage will vary from year to year. See Figure 2 (next page) for actual 2005 LIF maximum percentages. The maximum LIF payment in B.C. is the greater of this actuarial calculation or the previous year's investment return.

The maximum payment available in the first year of the plan is prorated based on the months remaining in the current year, with any part month being equal to a full month. No proration is required in the first year for a B.C., Manitoba, New Brunswick, Nova Scotia, or Quebec LIF.

FIGURE 2

YEAR 2005 LIF MINIMUM AND MAXIMUM PAYMENTS

Age at December 31 of previous year (2004)	Minimum Payment	Maximum Payment (1)	Maximum Payment (2)(3)	Maximum Payment (4)	Maximum Payment (5)
55	2.86%	6.51%	6.40%	6.51%	5.90%
56	2.94%	6.57%	6.50%	6.57%	5.96%
57	3.03%	6.63%	6.50%	6.63%	6.02%
58	3.13%	6.70%	6.60%	6.70%	6.09%
59	3.23%	6.77%	6.70%	6.77%	6.16%
60	3.33%	6.85%	6.70%	6.85%	6.24%
61	3.45%	6.94%	6.80%	6.94%	6.33%
62	3.57%	7.04%	6.90%	7.04%	6.42%
63	3.70%	7.14%	7.00%	7.14%	6.52%
64	3.85%	7.26%	7.10%	7.26%	6.63%
65	4.00%	7.38%	7.20%	7.38%	6.75%
66	4.17%	7.52%	7.30%	7.52%	6.89%
67	4.35%	7.67%	7.40%	7.67%	7.04%
68	4.55%	7.83%	7.60%	7.83%	7.20%
69	4.76%	8.02%	7.70%	8.02%	7.39%
70	5.00%	8.22%	7.90%	8.22%	7.59%
71	7.38%	8.45%	8.10%	8.45%	7.82%
72	7.48%	8.71%	8.30%	8.71%	8.08%
73	7.59%	9.00%	8.50%	9.00%	8.38%
74	7.71%	9.34%	8.80%	9.34%	8.72%
75	7.85%	9.71%	9.10%	9.71%	9.11%
76	7.99%	10.15%	9.40%	10.15%	9.55%
77	8.15%	10.66%	9.80%	10.66%	10.07%
78	8.33%	11.25%	10.30%	11.25%	10.68%
79	8.53%	11.96%	10.80%	11.96%	11.40%
80	8.75%	N/A	11.50%	12.82%	N/A
81	8.99%	N/A	12.10%	13.87%	N/A
82	9.27%	N/A	12.90%	15.19%	N/A
83	9.58%	N/A	13.80%	16.90%	N/A
84	9.93%	N/A	14.80%	19.19%	N/A
85	10.33%	N/A	16.00%	22.40%	N/A
86	10.79%	N/A	17.30%	27.23%	N/A
87	11.33%	N/A	18.90%	35.29%	N/A
88	11.96%	N/A	20.00%	51.46%	N/A
89	12.71%	N/A	20.00%	100.00%	N/A

(1) The maximum LIF payment for all jurisdictions except B.C. Manitoba, Quebec, Nova Scotia, New Brunswick and Federal.
(2) The maximum LIF payment for Manitoba, Quebec and Nova Scotia
(3) The maximum LIF payment for B.C. is the greater of the percentage in the above column or the previous year's investment return.
(4) The maximum LIF payment for New Brunswick
(5) The maximum LIF payment for Federal

4 › Locked-In Retirement Income Fund (LRIF)

Available in Alberta, Manitoba, Ontario and Newfoundland & Labrador

An LRIF is similar to a LIF to the extent that both allow the individual access to their locked-in funds within defined minimum and maximum levels (see **Figure 3**).

However, a key difference between a LIF and LRIF is that an LRIF can continue throughout an individual's lifetime (i.e. there is no requirement to convert the remaining funds to a life annuity at age 80).

Also, the maximum payment calculation for an LRIF is significantly different than for LIF accounts. As explained in **Figure 3**, the LRIF maximum payment will be the greatest of four amounts. This amount is generally equal to the investment growth earned in the account in the previous year. The investment growth is defined as the value of the LRIF at the end of the previous year less the value of the LRIF at the beginning of the previous year (adjusted for account transfers) plus withdrawals made in the previous year.

An individual using an LRIF can convert to a life annuity at any time. Note that an individual cannot convert from the life annuity option to either an LIF or LRIF.

It is possible for an individual to convert directly from a LIF to an LRIF and vice versa.

FIGURE 3

HOW LRIF PAYMENTS ARE CALCULATED

Minimum Payment

$$\text{Minimum Annual Payment} = \text{Plan balance at December 31 of previous year} \times \frac{1}{90 - \text{Age at December 31 of previous year}}$$

Note: The provinces of Alberta, Manitoba, Ontario, and Newfoundland & Labrador will allow the younger spouse's age to be used in the calculation of the minimum LRIF payment.

The above formula applies until the planholder reaches age 71. At age 71 the new minimum payment schedule for RIFs will take effect (See Figure 2 for actual percentages).

There is no minimum payment in the year the plan is established.

Maximum Payment

Maximum Annual Payment = **Greatest** of the following amounts (1, 2, 3 or 4)

1. the value of the LRIF at the beginning of the year less the net amount transferred in.
2. the investment growth in the immediately previous year, based on the change in market value.
3. if the payment is being made in the calendar year in which the LRIF was established or in the immediately following year, the maximum payment equals 6% of the LRIF value at the beginning of the year.
4. the minimum payment

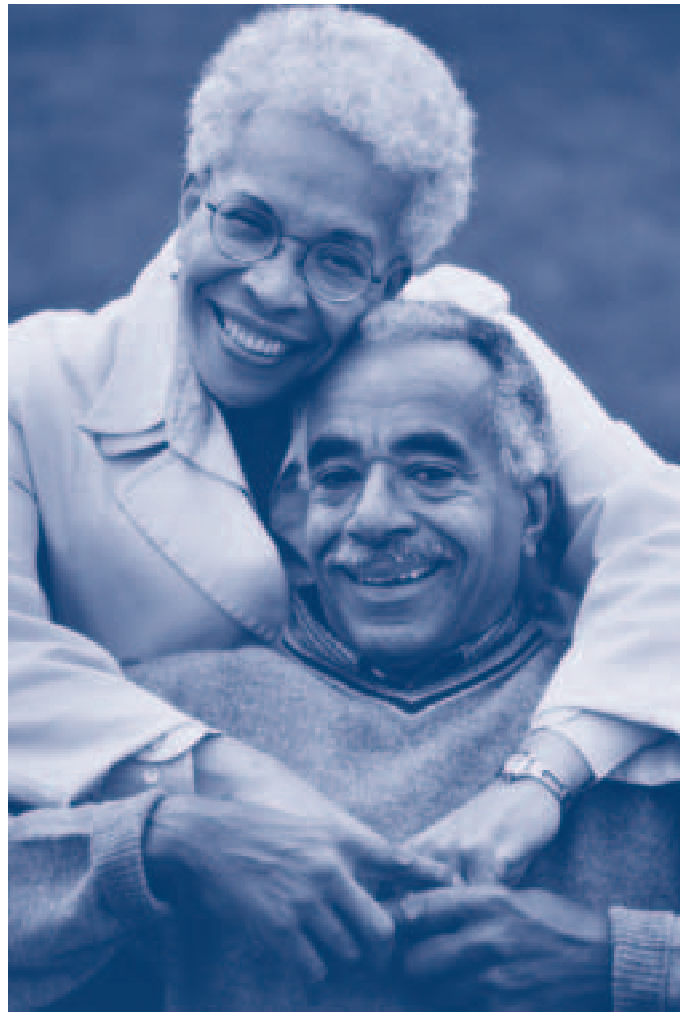
In other words, the maximum in the first two years of the plan will normally equal 6% of the plan balance at the beginning of the year. After the first two years of the plan, the maximum will normally be equal to the investment growth earned in the previous year.

The maximum payment available in the first year of the plan is prorated based on the months remaining in the current year, with any part month being equal to a full month. No proration is required in the first year for a Manitoba LRIF.

5 › Prescribed Retirement Income Fund (PRIF)

Available only in Saskatchewan

In addition to the life annuity, effective April 2002, locked-in accounts under Saskatchewan pension legislation have another income option called a Prescribed Retirement Income Fund (PRIF). Only those annuitants who are at least age 55 (or the early retirement age established by the plan where the money originated) are eligible for the PRIF.



The main advantage of the PRIF compared to the LIF and LRIF is that the PRIF has no maximum withdrawal limits. However, minimum withdrawals are still required, which are identical to the LIF and LRIF.

The following are other features of the PRIF:

- Consent forms to permit the transfer to a PRIF must be signed by a spouse or a common-law partner if applicable;
- A spouse or common-law partner must still be a beneficiary of a PRIF unless they waive their designated beneficiary status;
- No requirement to purchase an annuity at age 80 with a PRIF;
- Those annuitants who currently have a LIF or LRIF under Saskatchewan legislation can transfer to a PRIF on a tax-deferred basis.

6 › Determining which options apply to you

The available maturity options for your locked-in funds will generally depend on the province in which you worked when the pension benefits were earned. For example, if you worked in the province of Saskatchewan, but have retired in the province of British Columbia, then your locked-in funds will be subject to Saskatchewan pension legislation.

Individuals with Federal Pensions will generally be governed by the Canada Pension Benefits Standards Act (PBSA) regardless of the province they worked in. Information in this publication related to Federal pensions assumes the member's pension is governed by the PBSA.

Please see **Figure 4** for a summary of the available maturity options.

Figure 5 outlines the differences in the maturity options available as well as when the maturity options can commence.

Upon marriage breakdown, locked-in plans can be transferred to the non-member spouse. However, the assets will remain locked-in for both the member and non-member spouse.

Figure 6 summarizes special withdrawals that can be made from locked-in plans. If an individual meets the criteria to unlock their locked-in plan then the amount that is unlocked will be fully taxable. To avoid this taxable amount, the amount unlocked can also be transferred on a tax-deferred basis to the annuitant's non-locked-in RSP or RIF.

Some provinces allow unlocking of their locked-in plans due to non-residency. See **Figure 6** for details. In order to unlock due to non-residency, the annuitant must supply proof that they have become a non-resident of Canada for income tax purposes. Written confirmation from the Canada Revenue Agency (CRA, formerly known as the Canada Customs & Revenue Agency) that the annuitant is a non-resident of Canada would generally serve as sufficient proof for this purpose. If the annuitant has a spouse, then a spousal waiver form must be signed by the annuitant's spouse in order to unlock the plan due to non-residency.

Note that since assets in a locked-in plan are governed by pension legislation, they are generally protected from creditors (other than an order for support payments). However, any withdrawals from a locked-in plan, including an unlocking of the plan, could then subject the assets to creditors.

At the date of this publication, Manitoba introduced and passed legislation to allow a one time transfer of up to 50% of the balance of LIF/LRIF to a creditor-protected RIF that is not locked-in (pending regulatory approval).

FIGURE 4

SUMMARY OF MATURITY OPTIONS

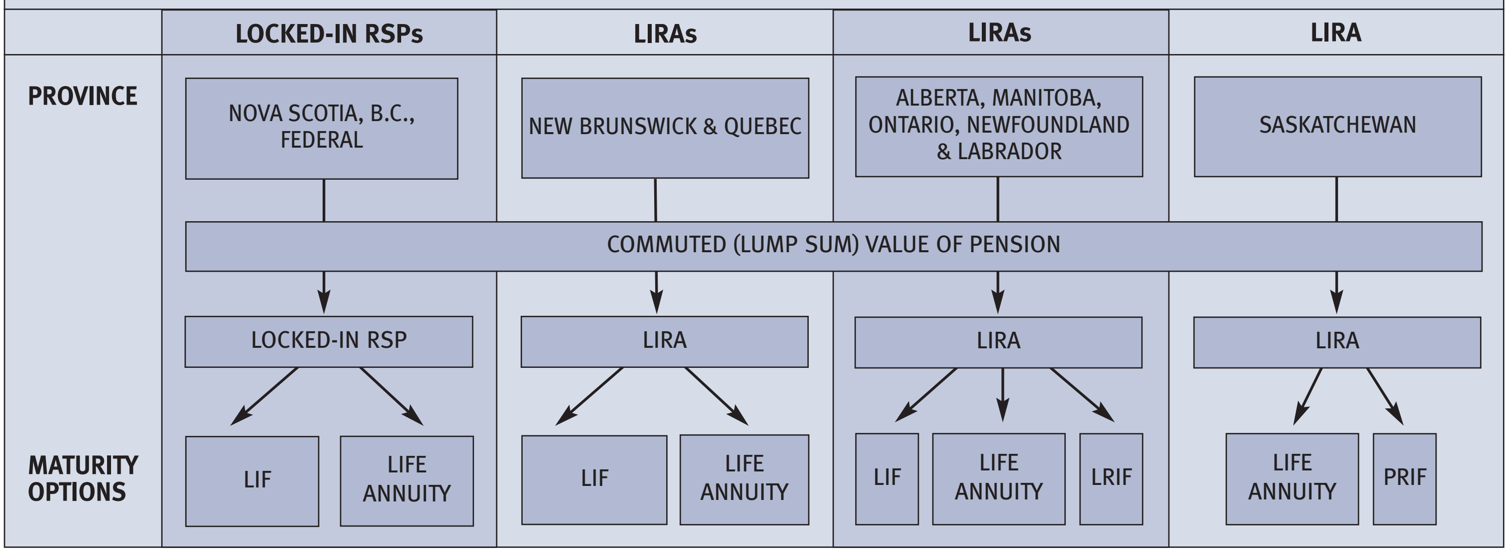


FIGURE 5

DETAILS BY PROVINCE FOR LOCKED-IN MATURITY OPTIONS

	Federal	British Columbia	Alberta	Sask.	Manitoba	Ontario	Quebec	Nova Scotia	New Brunswick	Nfld. & Labrador
Maturity Options:	LIF Life Annuity	LIF Life Annuity	LIF Life Annuity LRIF	Life Annuity PRIF	LIF Life Annuity LRIF	LIF Life Annuity LRIF	LIF Life Annuity	LIF Life Annuity	LIF Life Annuity	LIF Life Annuity LRIF
Age Limitation: • Initial LIF/LRIF/PRIF payment	Anytime	Age 55 (1)	Age 50 (1)	Age 55 (1)	Anytime	(2)	Anytime	(3)	Anytime	Age 55 (1)
• Initial annuity payment	Anytime	Age 55 (1)	Age 50 (1)	Age 55 (1)	Anytime	(2)	Anytime	(3)	Age 55	Age 55 (1)

(1) Subject to Registered Pension Plan providing for earlier payment if plan allows.
(2) Cannot begin earlier than the earliest date the Registered Pension Plan allows.
(3) Payments not to commence earlier than 10 years before the normal retirement date under the Registered Pension Plan.

FIGURE 6

DETAILS BY PROVINCE FOR SPECIAL WITHDRAWALS FROM LOCKED-IN PLANS

	Federal	British Columbia	Alberta	Saskatchewan
Early payout for shortened life expectancy	Yes – physician certificate and spousal consent	Yes – physician certificate and spousal waiver	Yes – physician certificate and spousal waiver	Yes – physician certificate and spousal waiver
Early payout for financial hardship	No	No	Yes – must apply directly to provincial government	No
Unlocking of small plan balances	No	Yes (1)	Yes (2)	Yes (3)
Unlocking due to non-residency	No	Yes – if non-resident for at least 2 years	Yes	No
Withdrawals in excess of maximum LIF/LRIF	No	No	No	Yes – by transferring to PRIF
Unlocking of LIRA or Locked-in RSP due to death of annuitant and transfer to spouse	No	No	No	Yes – by transferring to to a PRIF
Unlocking of LIF or LRIF due to death of annuitant and transfer to spouse	No	No	Yes	Yes

1) a) all ages and less than 20% of YMPE
   b) at least age 65 and less than 40% of YMPE

2) a) all ages and less than 20% of YMPE; OR
   b) at least age 65 and total locked in monies/pension plan total less than 40% of YMPE

3) a) LIRA only—all ages and less than 20% of YMPE and the owner has no other locked-in money

4) possible if certain conditions are met

5) at least age 55 and less than 40% of YMPE

6) at least age 65 and less than 40% of YMPE

7) at least age 65 and less than 40% of YMPE

8) a) at least age 65 and less than 40% of YMPE
   b) less than age 65 and less than 40% of YMPE divided by 1.06 for each year before age 65

9) a) all ages and less than 10% of YMPE; OR
   b) at least age 55 and less than 40% of YMPE

10) As of May 25, 2005, no amount may be paid out of a LIF or LRIF as temporary income. However, it is possible to transfer up to 50% of the balance of LIF/LRIF to a creditor-protected RIF that is not locked-in (pending regulatory approval).

Manitoba	Ontario	Quebec	Nova Scotia	New Brunswick	Nfld. & Labrador
Yes – physician certificate and spousal consent	Yes – physician certificate and spousal consent	LIRA yes – physician certificate and spousal consent physician certificate LIF – no	Yes but only if provided in pension plan – physician certificate and spousal consent	Yes – physician certificate and spousal waiver	Yes – physician certificate and spousal consent
No	Yes – must apply directly to provincial government	No	No	No	No
Yes (4)	Yes (5)	Yes (6)	Yes (7)	Yes (8)	Yes (9)
No, proposed legislation will permit	No	Yes – if non-resident for at least 2 years	No	Yes – cannot be Canadian citizen	No
Yes (10)	No	Yes (11)	Yes (12)	Yes (13)	Yes (14)
No	Yes	Yes	Yes	Yes	Yes
Yes	Yes	Yes	Yes	Yes	Yes

11) a) under age 54 then the additional temporary income can be withdrawn equal to 40% of YMPE less 75% of individual's income provided income from other sources does not exceed 40% of YMPE
b) at least age 54 and under age 65, additional temporary income can be withdrawn based on special Quebec tables; however, cannot be greater than 40% of YMPE
c) no additional temporary income if at least age 65

12) a) at least age 54 and under age 65, additional temporary income can be withdrawn based on special Nova Scotia tables; however, cannot be greater than 40% of YMPE
b) no additional temporary income if at least age 65

13) one lump sum lifetime withdrawal equal to 3 times maximum annual LIF % but no greater than 25%

14) must be under age 65; additional income can be withdrawn equal to 40% of YMPE less total pension income received from all employers/LIF/LRIF/life annuities

Note: YMPE is the Year's Maximum Pensionable Earnings and adjusted each year to reflect average Canadian wage levels. The YMPE for 2005 is $41,100.

7 › Choosing between a Life Annuity or LIF/LRIF

Both the life annuity and LIF/LRIF have advantages and disadvantages. The maturity option you choose to access your locked-in RSP or LIRA funds will depend upon a number of factors such as:

HOW MUCH ANNUAL INCOME WILL YOU REQUIRE?

If you will require a variable amount of annual income from your locked-in RSP or LIRA funds then you could consider the LIF/LRIF option to allow you some flexibility in the amount of income received in the year. For example, if you do not require additional income in the current year, you could receive the minimum payment leaving more funds within the LIF/LRIF to grow tax-deferred.

DO YOU WANT TO TAKE AN ACTIVE ROLE IN THE MANAGEMENT OF YOUR ASSETS?

An annuity will transfer the management and investment risk of your assets to the insurance company that you purchase the annuity from.

A self-directed LIF/LRIF will allow you to retain control of the investment of your funds and you will now have to accept the investment risk.

DO YOU WANT TO PRESERVE THIS ASSET FOR YOUR ESTATE?

Upon death, the full value of the LIF/LRIF will be payable directly to your beneficiary or estate. Taxes may be payable on this amount depending on who is the beneficiary of the LIF/LRIF funds. The estate benefit provided by an annuity will depend on whether a survivor benefit or guarantee period is purchased.

8 › Choosing between a LIF or LRIF

Both the LIF and LRIF will provide a certain amount of flexibility in the amount of annual income received. The main differences between these options are:

- the LIF must be converted to a life annuity by the end of the individual's 80th year (except in B.C., Manitoba, Quebec, Nova Scotia and New Brunswick. At the time of printing this publication, Federal pension legislation is being amended to remove the requirement for locked in federal plans to be converted to an annuity at the age of 80);
- once conversion to an LRIF has taken place, it can continue for life or can be commuted at any time to purchase an annuity;
- if the locked-in assets will be a major source of retirement income, then consider the LIF as the LIF can likely provide a more predictable maximum payment compared to LRIF maximums;
- maximum payments from the LIF will generally be higher than the maximum payment from the LRIF especially for a conservative investor over the age of 70; and
- unless converted to an annuity, the LIF can be converted to an LRIF anytime and vice versa.

9 › Summary

Since your locked-in funds can represent a significant retirement asset, it is important that you carefully consider the available maturity options. Remember to maintain your flexibility as circumstances are always changing and you will want to ensure that you can take advantage of opportunities as they arise.

Your advisor can assist you in determining which of the available maturity options is most appropriate for your circumstances.

For more information, speak with an Investment Advisor
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