Income

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The Critical 10

First year of retirement

Can I consider commuting my pension?

Many employers in Canada still offer, as part of the benefit package, some form of pension plan or defined contribution plan retirement saving vehicles. While still working you generally do not have access to these defined assets. When you retire, your pension plan may give you the choice to receive monthly payments or to “commute your pension” and take these accumulated funds in a lump sum.

Commuting your pension does not give you immediate access to all the funds accumulated at one time. Your pension provider has an obligation to ensure that you will have funds available throughout your retirement. An investment firm that receives commuted funds takes over that obligation and only allows those funds to be deposited into a locked in retirement account (LIRA). These funds can then be transferred to either a Life Income Fund (LIF) or a Locked Retirement Income Fund (LRIF). Money can be drawn from these funds according to federally regulated schedule each year. At age 65, the most you can draw from your locked in plan is 8.22% of the balance. This increases as you age to 57.46% at age 83 and 100% at age 84.

The LIF or LRIF can best be considered a restricted form of the traditional RRIF. The rules of these plans will be directed by the statutes of your pension plan. We will discuss federally administered plans and plans administered by Alberta organizations. There are a few similarities with these plans.

- Automatic beneficiary of these plans is your spouse.
- At death, funds may transfer to a spouse’s locked in plan (Federal plans) or to a RRSP (Alberta plans). Upon death of the second spouse, assets are paid out to the named beneficiaries or the estate.
- Upon a marriage breakdown or separation agreement, up to 50% of assets may be divided to the former spouse.
- An annuitant, who becomes a non-resident after 2 years and has written proof of non-resident status, can withdraw the balance of locked in plans.
- Both Alberta and Federal plans allow one time transfer of LIRA assets to the RRSP when converting to a LIF or LRIF.

While it is very appealing to collect pension cheques from your former employer during retirement, there may be a couple circumstances when you may wish to commute your pension and manage the funds yourself.

- **Performance** — Pension plan assets are managed in a very conservative manner. A high degree of fixed income and low management fees are associated with most pension plans. You may be able to grow your commuted value higher by increasing exposure to equity markets. You should be aware that you are exposing yourself to market volatility with this strategy and should be comfortable assuming more risk.

- **Portability** — Your locked in account is regulated by the type of pension plan it came from (Federal or Alberta) but the plan travels with you regardless of where you live. Taking control of your pension assets may be advisable if you are concerned about the health of the organization granting you the pension benefits.

- **The estate** — most pension plans provide ongoing benefits for surviving spouses, but the benefits end upon the death of the second spouse. If you wish to use pension funds as part of your family legacy, you may wish to consider commuting your plan.

Over the years, federal and provincial rules for locked in plans have become more accommodating. Alberta recently announced unlocking flexibility for financial hardship or for small balances. Alberta also increased the LIF maximum age calculation from 85 to 90 to account for an aging demographic. Consultation with your financial advisors about the best way to invest commuted pension funds should include a review of your overall asset allocation and your disposition to risk. Consideration of your retirement income needs and a schedule to draw down funds should also be discussed. This may be a good point in time to review your financial plan or create a new financial blueprint for your retirement years.