

# What are the Financial Implications of a Job Loss?

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**WHEN YOU LOSE YOUR JOB, one of your first concerns is, naturally, your financial health. Deal with this concern right away, so you can go on to conduct a successful work search.**

***Please Note:*** Although we make every effort to provide accurate and current information, the following is provided as a general guideline regarding some important financial matters connected with loss of employment. Speak with your PWL Advisor prior to making any decisions.

### **Getting organized financially:**

Sit down with your Partner and make sure you have a clear picture of your current financial situation. If you do not already have a means for keeping track of your finances, you may find the attached worksheets helpful:

- Net Worth
  - Inventory of Personal Registered Retirement Savings Plans
  - Income and Expense Worksheet
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- If you don't have a budget, this may be a good time to start one.
  - If possible, postpone large expenditures. Also, cut back on everyday spending.
  - Set aside funds to cover upcoming expenses you can't postpone.
  - Set aside an entertainment fund, so you can have a well-deserved break as a reward for your work search efforts.
  - If you anticipate being unable to meet any regular payments (e.g. life insurance premiums, mortgage, car loan, etc.), inform creditors of your circumstances before falling into arrears. Partial payments or a hold on payments can frequently be arranged.

### TAX SHELTERING SEVERANCE PAYMENTS

#### Retiring Allowances

An amount that can be identified as a payment received from your former employer “in respect of loss of office or employment” is considered a retiring allowance. Employers often refer to such payments as severance pay or termination pay. This type of income is reported on a T4A slip for income tax purposes, and may be eligible for a special RRSP contribution. Rules governing such special contributions can be complex and only a brief summary can be provided here.

#### DETERMINING YOUR “ELIGIBLE RETIRING ALLOWANCE” LIMIT

Your “eligible” limit is determined by a combination of your years of service and your status under your former employer’s pension plan.

The following calculation applies to everyone, regardless of pension plan status:

- \$2,000 per year or part year of service up to and including 1995. Service after 1995 cannot be counted in determining your eligible amount since the tax rules changed in 1995.

In addition, the following rules apply if you were a member of your former employer’s pension plan:

- If you are entitled to receive only your own contributions plus interest from the plan, you can shelter an **additional** \$1,500 for each year of service up to and including 1988.
- If the employer has contributed to the pension plan, and you are entitled to the associated benefits, calculation of the amount eligible for contribution to an RRSP becomes more complicated. It is necessary to determine the years of service prior to January 1, 1989, to which the employer’s contributions apply. For any years to which employer’s contributions **do not** apply, an **additional**

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\$1,500 per year is eligible for the special RRSP contribution. For any years to which employer's contributions do apply, no additional amount is eligible.

If you were **not** a member of a pension plan, an **additional** \$1,500 per year of service up to and including 1988 will apply (thus bringing the total for years prior to 1989 to \$3,500, with years from 1989 to 1995 remaining at \$2,000.)

The maximum amount for this special contribution is the lesser of the total retiring allowance and the amount determined under the applicable formula.

The attached "Severance Calculations for RRSP Rollover" worksheet can be used as a guide, although you are advised to obtain assistance to determine the exact "eligible amount" which applies in your situation, particularly if you are entitled to benefit from your employer's pension plan contributions.

Please note that:

- These are special contributions that must be made to your own RRSP and cannot be contributed to a spousal plan.
- Your eligibility to make the standard annual RRSP contribution is **not affected** by these special contributions.
- Funds other than the severance pay (such as vacation pay, wages in lieu of notice, or salary continuation payments) are **not eligible** for a rollover into an RRSP under the retiring allowance provisions. These are treated as employment income (reported on a T4 slip at tax time).

### **TRANSFERRING “ELIGIBLE RETIRING ALLOWANCES” TO YOUR RRSP**

Once your “eligible amount” has been determined, it can be contributed to an RRSP at any time up to the 60th day of the year following payment. However, a direct transfer from your former employer to your RRSP avoids the requirement for withholding tax, giving you immediate tax savings. (Note that the ability to make this special RRSP contribution is available only for the year of receipt of the retiring allowance. It does not carry forward to future years, as is the case of your regular unused RRSP contribution room.)

A direct transfer of funds to your RRSP can be arranged by providing your former employer with a letter of direction, which includes the following details (this was formerly accomplished via a TD2 form which is now obsolete):

- a) RRSP account number
- b) Financial Institution
- c) Address of Financial Institution
- d) Your account representative’s name and phone number, if applicable
- e) Amount

This should ensure proper credit of the funds to your account.

After you have calculated the eligible amount, any remaining retiring allowance will be paid directly to you. This type of payment will not be subject to CPP or EI premium deductions. The following income tax withholding rates will apply:

amounts less than \$5,000	10%
amounts from \$5,000 to \$15,000	20%
amounts in excess of \$15,000	30%

It is important to note that the rates above are withholding rates only and are not necessarily the total amount of tax that will apply. Any balance will usually be payable on April 30 of the year following receipt of the funds, when you file your income tax return.

### USING YOUR UNUSED RRSP DEDUCTION ROOM

If you have accumulated RRSP deduction room, as reported on your annual Notice of Assessment from CRA, your termination income may provide a source of funds to use this deduction limit.

You can direct your employer to make a direct payment to your RRSP by providing the same details as itemized above. (Note that a waiver letter is no longer required by CRA, although your former employer may ask for a copy of the statement of your RRSP contribution limit as shown on your Notice of Assessment.)

When using your unused contribution limit, you should note that the source of funds for the contribution is not limited to a retiring allowance payment – it can be from pay in lieu of notice, vacation pay, non-eligible retiring allowance amounts, bonus payments, etc. This type of contribution can be made to a plan in your own name or to a spousal plan.

When deciding how much of your unused contribution limit to utilize, bear in mind that the room is not replenished if you must make a withdrawal from the RRSP to make ends meet through your transition.

### OTHER RRSP CONSIDERATIONS

In order to maintain as much flexibility as possible through your transition period, consider holding any transferred RRSP funds in very liquid investments, such as savings accounts or money market mutual funds. If it becomes necessary to withdraw from the RRSP to cover living expenses, you will have ready access to your funds. Once you are through the transition and settled into the next step on your career path (give it at least three months), develop a long-term investment strategy for the RRSP funds.

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If you withdraw money from your RRSP, the amount withdrawn will be taxable in the year of receipt. The financial institution holding your RRSP must withhold tax when money is withdrawn from an RRSP.

The withholding rates are:

for amounts up to \$5,000	10%
for amounts from \$5,001 to \$15,000	20%
for amounts in excess of \$15,000	30%

The total amount of tax payable on your withdrawals will depend on your total taxable income for the year, with any amount in excess of the withholding rate payable at the time of filing your tax return.

You should also check with your RRSP issuer (bank, trust company, life insurance company, broker, etc.) to determine what fees may be charged for withdrawal of funds. If making withdrawals, be sure to allow sufficient time to process your request.

### **PENSION ADJUSTMENT REVERSAL (PAR)**

If you have been a member of a registered pension plan (RPP), you have had an annual Pension Adjustment (PA) which has reduced the amount of RRSP contribution available to you each year. In the case of a defined benefit pension plan, the PA is based on the assumption that benefits under the pension plan will continue until retirement age, and is not adjusted for the age of the employee. The result is that PA's tend to be under-estimated for younger employees and over-estimated for older employees.

The Pension Adjustment Reversal (PAR) was introduced for terminations occurring after December 31, 1996. The purpose of the PAR is to restore lost RRSP deduction room to a pension plan member who terminates from the plan and who is either not vested in post-1989 RPP benefits or who elects to receive a lump-sum settlement of post-1989 RPP benefits.

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In the case of a defined benefit pension plan, the PAR will be equal to the sum of the PA's reported on T4's since 1990, less the commuted value of the pension benefit earned since 1990.

In the case of defined contribution pension plans, where the employer contributions have not vested (the employee does not yet own the employer contributions), the PAR will equal the amount of the employer's contributions which are forfeited.

Additional information can be found on the CRA Web site at <http://www.cra-arc.gc.ca/>

## EMPLOYMENT BENEFITS

### ...Pension

With the termination of employment, if you have been a member of an employer-sponsored defined benefit pension plan, you may have options regarding your pension benefits.

These options generally include:

- a) leaving your accrued benefits with the employer's plan, or
- b) transferring the "commuted value" to a Locked-in Retirement Account (LIRA).

With a transfer to a LIRA, you assume the investment responsibility for your pension funds. The locking-in features restrict the timing of access to an income stream and the amounts that can be withdrawn on an annual basis. Since the funds originated from a pension plan, the LIRA must provide a retirement income for your lifetime. (It is important to note that "locking-in" in this context does not refer to the type of investment vehicle used — the investment options for LIRA's are the same as for regular RRSP's.)

If you opt to transfer your "commuted value" to a LIRA, the transfer is done directly and the transaction is not reported on your income tax return. The paperwork includes the completion of form T2151 and a Locking-in Agreement between the pension plan and the issuer of the

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LIRA (your bank, trust company, broker, etc.). Any Pension Adjustment Reversal is reported after the transfer is completed.

In some cases, there may be excess funds beyond the locked-in amount. Be sure you understand your options for handling these amounts. Things to watch for include:

- a) ability to transfer to a normal RRSP on a direct transfer basis, with no impact on your regular RRSP deduction room;
- b) ability to transfer to a normal RRSP on a direct transfer basis, with a requirement that the deduction for tax purposes is limited to your available deduction room;
- c) taking excess funds in cash, in which case they will be taxable and could impact on the timing of your EI benefits. Watch also for income tax withheld when the funds are received, and the additional amount which may be payable when your tax return is filed.

The Pension Adjustment Reversal (PAR) discussed previously should also be taken into account when considering your options regarding the pension plan.

## OTHER BENEFITS

Be sure to understand how your other group benefits will be impacted by your termination. Some things to watch for:

### ...Long Term Disability

often cannot be continued beyond your last day at work. In some cases, personal coverage may be available, but application must be made within 30 days of termination of group coverage.

### ...Life Insurance

“Conversion” to a personal policy may be available, again with application being required within a defined time frame. This conversion may be possible without providing medical evidence of

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insurability; therefore it is a critical issue for anyone with health problems that would restrict their ability to purchase life insurance.

Be sure to check with your former employer to find out exactly when your coverage ceases under your various plans. You can then make the necessary arrangements to obtain private coverage for benefits you wish to continue on a personal basis, or until you are covered under your new employer's plan. (Bear in mind that there could be a waiting period before new benefits commence.)

### ...Employment Insurance Benefits

*Cautionary note:* Your eligibility for EI benefits can only be determined by filing a claim. You are advised to register at the HRDC (Human Resources Development Canada) nearest to your residence as soon as possible after your last regular day of work.

Information on EI benefits is available at the following Web site:  
[www.hrdc-drhc.gc.ca/ae-ei/employment\\_insurance.stml](http://www.hrdc-drhc.gc.ca/ae-ei/employment_insurance.stml).

# Net Worth

As of \_\_\_\_\_

<b>Current Assets</b>	<b>Self</b>	<b>Partner</b>	<b>Total</b>
Cash, in Bank			
Canada Savings Bonds			
Bonds			
Term Deposits			
Stocks			
Life Insurance (Cash Surrender Value)			
Tax Refund			
Other			
Other			

**Total Current Assets**

<b>Fixed Assets</b>	<b>Self</b>	<b>Partner</b>	<b>Total</b>
Residence			
Other Property			
RRSP's			
Pension Plan			
Personal Effects			
Tax Shelters			
Art; Jewelry; Antiques			
Other			

**Total Fixed Assets**

*(Current Assets plus Fixed Assets)* **Total Assets**

<b>Liabilities</b>	<b>Self</b>	<b>Partner</b>	<b>Total</b>
Mortgage			
Loans (Financial Institution)			
Credit Cards			
Income Tax			
Other			
Other			

**Total Liabilities**

*(Total Assets less Total Liabilities)* **Net Worth**



# Income and Expenses Worksheet

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
BANK BALANCE												

**INCOME**

Salary												
Vacation Pay												
Severance Payments												
Retirement Income												
Partner's Work Income												
EI Payments												
Investment Income												
- Interest												
- Dividends												
- Annuities												
Rental Income												
Other Income												

**TOTAL MONTHLY INCOME**

**EXPENSES**

Mortgage or Rent Payments												
Property Taxes												
Home Repair / Maintenance												
Utilities - Heat												
- Water												
- Electricity												
- Telephone												
- Cable TV												
Furnishings & Appliances												
Food												
Clothing												
Insurance - Life												
- Property												
- Car												
Car - Gas & Parking												
- Repair & Maintenance												
Job Search Expenses												
Medical & Dental Expenses												
Loan Payments												
Credit Card Payments												
RRSP Contributions												
Alimony / Maintenance												
Child Care Expenses												
Education Fees & Costs												
Vacation & Holidays												
Recreation												
Entertainment												
Gifts & Charities												
Books & Subscriptions												
Personal Grooming												
Other Expenses												

**TOTAL EXPENSES**

**NET CASH FLOW** (total income less expenses)

BANK BALANCE												
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# Severance Calculations for RRSP Rollover

Calculation	Years	Amount	Total
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**A. Basic Rollover**

Enter the number of full or part years of service up to and including December 31, 1995

		x \$2000 =	
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*(Please Note - Select either B or C Below)*

**B. Additional Rollover if NOT a member of a pension plan**

Enter the number of full or part years of service up to and including December 31, 1988

		x \$1500 =	
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**C. Additional Rollover if A MEMBER of a pension plan**

Enter the number of full or part years of service up to and including December 31, 1988

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Subtract the number of years vested pensionable service

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Remaining years or part years of service

		x \$1500 =	
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**D. If Pension Plan Fully Vested**

Nil	Nil
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**Total of Calculation A plus B or C**

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