

## QUFA INFOSHEET

# Pension Options if You Continue Working Beyond 65

By the Pension Working Group, QUFA

This *QUFA Infosheet* is primarily for the information of QUFA Members who shortly will be approaching their so-called Normal Retirement Date (NRD). For faculty, the NRD is usually the 30 June following your 65th birthday. Mandatory retirement at age 65 was abolished at Queen's in 2005, and a number of faculty now continue working beyond what previously would have been their NRD.

As you approach age 65, you will receive a letter from Queen's Human Resources asking whether you intend to work beyond your NRD and, if so, what you plan to do regarding your pension. The following article describes your available pension options and highlights some possible factors to consider in choosing between them.

### What Are the Options?

Active members of the pension plan who remain in the service of the University past their NRD have the following options available to them:

#### ***a) Continue to Make Pension Contributions***

You may continue to contribute to the plan and accrue service during the period of the postponed retirement. Canada Revenue Agency (CRA) rules require that the pension must be taken no later than the year you turn age 71.

#### ***b) Cease Making Pension Contributions but Defer Taking the Pension***

You may cease to contribute to the plan and defer the commencement of your pension until their postponed retirement date. CRA rules require that the pension must be taken no later than the year you turn age 71.

#### ***c) Start Taking the Pension***

You may commence your pension as of your NRD, in which case you would cease making further contributions and accruing further benefits under the plan. You would then be receiving both salary and pension.

#### ***d) Transfer the Cash Value of Your Pension Out of the Plan***

Under any of the three scenarios above, and at the time you would otherwise take your pension, rather than receive a Queen's pension, you can elect to leave the plan and withdraw the cash value of your pension. The cash value is the greater of your actual account balance or the commuted value of the corresponding defined benefit (there will

be more information on this option and commuted values later in this article).

#### **How Will Your Pension Be Calculated if You Elect Option a) or b)?**

*If you go out on a Money Purchase Pension (MPP):*

Under both options a) and b), the Money Purchase Pension (MPP) payable at your eventual postponed retirement date will be determined as the amount of pension that can be provided by your then money purchase account balance, based on the actuarial assumptions in effect at that time. This calculation will reflect the fact that the you will be commencing a pension at an age later than 65 (i.e., if Professor X and Professor Y aged 65 and 68 respectively retire in the same year with the same account balance, Professor Y will receive a higher MPP than Professor X).

*If you go out on the Minimum Guarantee Pension (MGP):*

Under Option a), the MGP is calculated in the same manner as if you had retired at your NRD. However, the calculation would take into account and reflect your service and earnings in the period since your NRD and hence be higher than the MGP you would have received had you taken it at age 65.

Under option b), the MGP will be determined as the actuarial equivalent of the pension that would have been payable at the NRD. This means that the pension will be higher than if you had

taken it at your NRD, to reflect the fact that you are taking it at a later date. The amount of the adjustment is dependent on interest rates in effect at the time you actually retire.

### Which Option Should I Choose?

*There is no definitive answer to this question.* Much depends on your own specific circumstances and your assessment of what is likely to happen in the period between your NRD and the time you actually commence taking your pension (e.g., your expectation with regard to future financial market returns, annual salary increases, etc.).

One important consideration is whether, based on your recent annual pension statements, you expect to go out with a MPP or a MGP. Bearing this in mind, the following are some of factors you may wish to consider.

#### With Regard to Option a):

- Your Money Purchase Account will have continued to accrue additional contributions (from both your own contributions and the employer's contributions). As long as the QPP enjoys positive annual investment returns, you will have a larger money purchase account balance when you retire. Assuming that you do go out on a MPP, your starting pension will be higher due to:
  - the larger account balance that you will have accrued, and
  - the fact that by beginning the pension at a later age, actuarially you will be taking the pension for a shorter period.
- Remember that, as a result of changes to the QPP agreed to during the 2011 round of collective

bargaining, at the time you take the pension there will be a charge against your money purchase account balance to fund the pension non-reduction provision of the plan. This charge is to be phased in three steps: after 1 September 2012, the charge is 1.5% of your money purchase account balance; after 1 September 2013, it is 3.0%; and after 1 September 2014, it is 4.5%. This charge will reduce the money purchase account balance on which your starting pension will be calculated.

- If you continue to make contributions and go out on a MGP, you will have a larger pension than if you take it at your NRD because you will have accrued more years of service in the plan and, presumably, your final average salary will be higher (these are the two key variables that determine the value of your initial MGP). However, note the first point below under option b).

#### With Regard to Option b):

- If you anticipate that, in all likelihood, you will go out on the MGP, you may decide it would be better to take Option b) rather than continue to contribute to the plan (i.e., Option a)). Why?
  - If you stop making contributions but defer taking the pension until you retire, you will get an actuarially increased pension at the later retirement date. The amount of the increase is dependent on the interest rates in effect at the time (as an example, given the interest rates then in effect, if you had retired in November 2011 at age 68,

your deferred MGP would have been 117% of the MGP you would have received at 65).

- In addition to the actuarial increase to the age 65 MGP, during the deferral period and up to age 71, you could contribute up to the maximum allowable annual amount to an RRSP (the maximum RRSP deduction limit for 2013 is \$24,270), which would add to your overall retirement savings: you will no longer be making contributions to the Queen's Pension Plan, which will free up cash for you to redirect to the RRSP.

#### With Regard to Option c):

- Income tax considerations. You will be drawing both your salary and a pension, which probably will result in a significant amount of income tax to be paid. If you have a spouse, CRA rules allow you to split your pension income with your spouse for income tax purposes. Depending on your spouse's income, this could enable you to offset some of the income tax that you would otherwise have to pay.
- Since you are continuing to draw a salary and no longer making contributions to the QPP, you will be able to contribute up to the maximum allowable annual amount to an RRSP (currently \$23,820) until age 71 and, hence, provide more savings for your eventual retirement. Since RRSP contributions are tax-deductible, this will also help to offset some income tax.

#### *With Regard to Option d):*

Earlier, we mentioned that, rather than stay in the plan and receive a Queen's pension, you can elect, at the time you would otherwise take your pension, to leave the plan and withdraw the cash value of your pension. This is also one of the options available to people who either retire early or leave Queen's to take up an appointment elsewhere.

If you withdraw from the plan, then you will receive the *greater* of:

- Your money purchase account balance (with no charge applied to it for the non-reduction provision, since you will not be taking a Queen's pension); or
- The commuted value of the minimum guarantee pension. The commuted value is determined by an actuarial formula such that it is sufficient, at then current interest rates, to fund a pension equal to your MG pension, assuming an average life expectancy. Because interest rates are currently at very low levels, the commuted value of minimum guarantee pension may well exceed the value of your money purchase account.

CRA rules allow you to transfer a significant part of the cash value to a tax-sheltered vehicle (e.g., a locked-in retirement account (LIRA)), so that it is taxable only when eventually paid out to you. As with all retirement savings options, payments must begin no later than the year you turn age 71, in this case, from a Registered Retirement Income Fund (RRIF) or equivalent. The balance that is excluded from the tax-sheltered transfer must be taken in cash and is taxed at source.

There are clearly risks and downsides involved in withdrawing the cash value (CV) of your pension:

- First and most obviously, the retirement income you actually receive from your LIRA/RRIF will depend on the performance of the investments which you choose. Hence, your retirement income could be less than you expected, and less than you would have received if you had remained in the Queen's plan. On the other hand, and, depending on your skill as an investor and the investment advice you receive, it could be higher.
- Should you choose, on the other hand, to guarantee your retirement income by using the cash value to purchase an annuity from an insurance company, the annual annuity payments are unlikely to be greater than the Queen's pension you would have received had you remained in the plan.
- If you do not purchase an annuity, you risk running out of money should you live longer than the average (whereas the pension plan, like an annuity, provides you with "insurance" against longevity by providing a pension for life).
- The Queen's pension plan provides for future indexing of pension payments when the fund return (averaged over the prior six years) exceeds 6%. Given the non-reduction guarantee, your Queen's pension will not be reduced even when annual fund returns fall below 6% or even below 0%. While indexed annuities are available in the market, they are very costly, and most people opt for non-indexed annuities.
- One instance where taking the cash value might well be a preferred option is if you do not have a spouse and have a shortened life expectancy due to an existing

medical condition. In this case, if you have taken the cash value, there could be a significant amount of money left to the beneficiaries of your estate.

One possible attraction of taking the cash value, for those who are going out on an MG pension and who have confidence in their investment ability, is that, at present, the commuted value of MG pensions are very high and may well exceed the value of your money purchase account. This is because interest rates are at historically low levels. However, those same low interest rates mean that bond interest rates, GIC rates, and the annual annuity payments that your lump-sum cash value will buy are also low.

In summary, it is very unwise to consider withdrawing the cash value of your pension without very careful consideration, including a realistic assessment of your own investment ability, and before securing reliable financial advice from a disinterested party (not an investment manager eager to administer your pension savings for a fee).

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**QUFA staff can be reached at [qufa@queensu.ca](mailto:qufa@queensu.ca).**