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# Tax News

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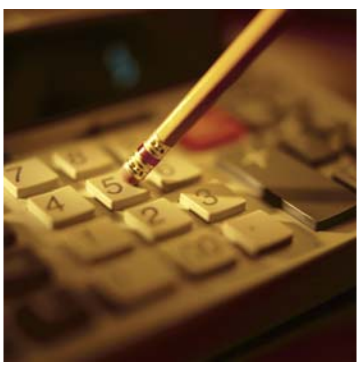
*Do you know the difference between severance pay and retiring allowance? What about tax deferral on transfers to RRSP's?*

*The following article deals with strategies for managing your severance package and provides some helpful tips on how to keep more of it in your pocket when you need it the most.*



## *Managing your severance package!*

***With the downturn of the economy, some who have lost their jobs, may have received large sums in severance and the uncertainty of what to do with it.***

Although receiving a large or modest severance package can help soften the blow of losing your employment, the sudden influx of cash can have serious tax consequences if not managed properly. In some cases, it might even be beneficial to negotiate with your employer and arrange to receive severance payments after January 1.

**Retiring Allowances:**
If severance is a one-time payment or a fixed amount payable over a short period with respect to loss of employment, or after retirement in recognition of long service (without continuation of employment benefits), it's considered a retiring allowance.

**Tax Deferral:**
Retiring allowances are fully taxable in the year received. However, a portion may be eligible for transfer to the recipient's RRSP, resulting in a deferral of tax on the amount transferred.

**Converting Group Health Insurance:**
Your life and health insurance benefits also need to be addressed rather quickly — often your group insurance can be converted into an individual policy without the need to provide medical evidence, but there might be only a short period of time to do so. Unless you are in excellent health, this could be your only chance to obtain sufficient insurance coverage at a standard rate.

**Severance packages and your RRSP:**
Retiring allowances can sometimes be transferred to your registered retirement savings plan (RRSP) without using up your existing contribution room.

Retiring allowance does *not* include superannuation, pension benefits, funds given in lieu of termination notice or amounts paid for unused vacation time.

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The amount eligible for transfer depends on the length of time you have been with the company. The amount is equal to $2,000 for each year or part year you worked with the company before 1996, plus another $1,500 for each year or part year you worked with the company before 1989, provided you did not earn (or have vested rights to) benefits in a registered pension plan or a deferred profit-sharing plan.

The amount of the retiring allowance eligible for transfer to your RRSP will be reported in box 26 of your T4A slip. Ineligible amounts will be shown in box 27.

If the severance you receive does not qualify under these rules — if you're leaving an employer you joined in 1997 or later, for example — the amount of severance that can be tucked away inside your RRSP will depend on the contribution room you have available.
If your RRSP is full, that amount might need to be reported as income.

If this is the case, it could make more sense to negotiate with your employer and arrange to receive this income in instalments over more than one year. This provides access to the lower marginal rates in the subsequent year, assuming that there are no other significant income sources in the year following termination. However, it also means you will not have access to the funds until that time.

**Your pension and other benefits**
Deciding whether to stay in your company pension plan (if you have one) or move your funds into a locked-in, self-directed retirement account requires that we do a calculation to determine which investment (your pension plan is an investment!) will generate better returns over time.

Thanks to recent pension regulation changes, locked-in accounts no longer need to be converted into a life annuity at age 80. This means pension payouts to a surviving spouse might not necessarily stop or be reduced when the pension plan member dies. Locked-in accounts might even be used to provide an inheritance to the member's family.

Finally, group life and health benefit plans can sometimes be converted into an individual policy without the need to provide medical evidence, but these things should not be left to fester. In some cases, there might be only a short period of time — usually 30 or 60 days — to make these arrangements. Unless you are in excellent health, this could be your only chance to obtain sufficient insurance coverage at a standard rate.



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