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TAX & ESTATE PLANNING

Locked-in plans: types of plans and unlocking options

December 28, 2023

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Picking up from last month's blog post, let's continue our look at locked-in plans. As with Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs), locked-in plans consist of pre and post-retirement plans. Specific rules relate to unlocking amounts from these plans.

Pre-retirement locked-in plans

Pre-retirement locked-in plans are considered RRSPs for federal income tax purposes. From a practical standpoint, they are essentially RRSPs with additional restrictions placed on access to the funds contained within the plans. Pre-retirement locked-in plans have various names, including Locked-in Retirement Savings Plans (LRSPs), Restricted Locked-in Savings Plans (RLSPs) and Locked-in Retirement Accounts (LIRAs), depending on the applicable legislation. Currently, all LRSPs and RLSPs are subject to federal pension legislation. Pre-retirement locked-in plans subject to the legislation of any of the provinces are called LIRAs.

While RRSP annuitants can withdraw funds at any time without limit, funds from LRSPs, RLSPs and LIRAs are accessible under limited circumstances. If the plan holder of a pre-retirement locked-in plan wants to make a withdrawal, they must either be the required age to transfer funds to an allowable post-retirement plan or become eligible to access one of the unlocking options described in the applicable pension legislation.

Post-retirement locked-in plans

Similar to RRSPs, all pre-retirement locked-in plans must collapse and convert to a maturity option by the end of the year the plan holder turns age 71. The earliest age at which a pre-retirement locked-in plan can be converted to a maturity option varies by pension legislation, with some having no age requirement at all. Four types of post-retirement locked-in plans are available, depending on pension legislation: Life Income Funds (LIFs), Restricted Life Income Funds (RLIFs), Locked-in Retirement Income Funds (LRIFs) and Prescribed Registered Retirement Income Funds (PRIFs).

Post-retirement locked-in plans are considered RRIFs for federal income tax purposes. The comparison of post-retirement locked-in plans to RRIFs is similar to that of pre-retirement locked-in plans to RRSPs: they are RRIF accounts subject to additional rules and restrictions. As with RRIFs, there is no mandatory minimum withdrawal amount from post-retirement locked-in plans in the year they are created. In every subsequent year, a prescribed minimum amount based on the plan holder's age must be withdrawn. Unlike RRIFs, however, post-retirement locked-in plans are subject to an annual maximum withdrawal limit in each year, including the year the plan is created. The governing pension legislation of the locked-in plan dictates the formula for calculating the annual maximum.

Unlocking options

Access to funds exceeding the annual maximum amount from a locked-in plan is generally restricted. If additional funds are needed, a plan holder may be able to exercise one of the available unlocking options if they meet all the requirements and conditions under the pension legislation governing the locked-in plan. This often includes a requirement to obtain the written consent of the plan holder's spouse or common-law partner. Some jurisdictions have comparable unlocking categories to one another, but each jurisdiction's exact requirements to exercise any given option often differs.

Some unlocking options may have tax consequences for the plan holder; plan holders are strongly encouraged to speak to a financial professional before making any important financial decisions. We highlight some options that may enable unlocking below, but these are not permitted uniformly across the provinces and territories of Canada. Please contact us to confirm unlocking eligibility in your specific case.

Temporary income

In general, this unlocking option allows an eligible plan holder who has reached the early retirement age (usually age 55) but has not yet reached the normal retirement age (usually age 65) to withdraw an extra amount exceeding the annual maximum withdrawal limit while preserving their Canada Pension Plan (CPP) pension until the plan holder reaches the age at which they can receive an unreduced CPP pension.

Financial hardship

When a plan holder is in a dire position of financial need, they can complete the applicable application along with other required documentation to unlock an extra amount exceeding the annual maximum withdrawal limit. The regulator usually creates a new application for each year. In general, the plan holder must meet all the criteria outlined in the pension legislation governing the locked-in plan, such as not exceeding a specific annual income threshold amount, experiencing residential eviction, being in arrears on mortgage payments, or facing medical expenditures that a Canadian registered physician has already approved.

Shortened life expectancy

In general, an eligible plan holder who has been diagnosed with a terminal illness may unlock their entire locked-in plan, provided that the Canadian registered physician of the plan holder is willing to complete a certification stating that the plan holder's life expectancy has decreased considerably or, as some legislation requires, is less than two years.

50% unlocking

An eligible plan holder may unlock up to 50% of the locked-in plan once in their lifetime. In general, the plan holder must meet the age requirement (usually age 55) and the unlocked funds can be transferred to an RRSP or RRIF on a tax-deferred basis. Some jurisdictions allow direct redemptions in cash. If the plan holder decides not to unlock the entire 50%, there is no opportunity to unlock the remaining eligible portion later.

Non-residency

In general, an eligible plan holder who has ceased to be a Canadian resident for more than two years may complete and file Form NR73: *Determination of Residency Status (Leaving Canada)* with the Canada Revenue Agency (CRA) to obtain a CRA letter declaring the plan holder is a non-resident for the purposes of the *Income Tax Act*. In addition, some legislation requires the plan holder to complete an application provided by the applicable regulator.

Small amount

When the balance of the locked-in plan is too small for potential growth or to provide a reasonable incremental retirement income, as determined by the governing pension legislation, an eligible plan holder may unlock the entire plan balance. In general, the plan holder must meet the age requirement and the balance of the locked-in plan must be below a specified threshold amount.

One-time transfer of three times the maximum

For New Brunswick locked-in plans only, an eligible plan holder can make a one-time transfer of three times the LIF's annual maximum amount to a RRIF. The amount transferrable under this option is tax deferred. The transfer amount cannot exceed 25% of the LIF's value and the unlocking request must be approved by the New Brunswick regulator.

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