



TAX &amp; ESTATE PLANNING

## Locked-in plans: understanding the basics

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This is a three-part series focused on locked-in plans. In this series, you'll learn the basics of these less-understood plans, explore pre-retirement and post-retirement plans and unlocking options, and get an overview of issues surrounding beneficiaries and creditors. Let's first understand the basics in this part.

### Locked-in plans: Part 1 of 3

The acronyms RRSP (Registered Retirement Savings Plan) and RRIF (Registered Retirement Income Fund) are so commonly used that the average Canadian recognizes them as readily as FYI (for your information) or ATM (automated teller machine). Further, many Canadians have some understanding of how RRSPs and RRIFs work. However, a closely related group of plans referred to as "locked-in plans" is far less well understood. The mention of those plan types – for example, LIF (Life Income Fund), LRSP (Locked-in Retirement Savings Plan) and LIRA (Locked-in Retirement Account) – is likely to elicit blank stares from most people.

Locked-in plans are a subset of RRSPs and RRIFs and are subject to additional rules under provincial or federal legislation. In general, the pension plan member's province of employment determines the applicable legislation governing the plan member's entitlement to survivor benefits, retirement benefits and employment termination benefits, as well as the minimum rights for eligibility to join the pension plan. For instance, if the member's province of employment is Ontario and the commuted value of the plan member's Registered Pension Plan (RPP) is transferred to a locked-in plan, that locked-in plan will be subject to rules outlined in Ontario's pension legislation.

The funds in locked-in plans can come from a commuted pension plan or from another locked-in plan governed by the same pension legislation. The purpose of locked-in plans is to provide tax-deferred savings vehicles for commuted pension proceeds while limiting access to ensure the funds are not depleted prematurely and increasing their opportunity for potential growth. Personal contributions to locked-in plans are prohibited. With certain exceptions, pension legislation typically prevents access to locked-in funds until the plan holder reaches a certain age dictated by the pension legislation governing the locked-in plan. Once plan members are able to access their locked-in plans, they receive funds from the post-retirement plans incrementally and are subject to an annual maximum withdrawal limit (discussed in the next blog post).

When a plan member leaves his or her employer or ceases to be a member of an RPP, the pension plan text dictates the portability options for accrued pension benefits. Eligible plan members may choose a deferred pension and receive pension payments at retirement, or they may transfer part or all of the commuted value to an appropriate locked-in plan on a tax-deferred basis. The exact amount transferrable from the RPP to a locked-in plan depends on the pension plan text and the governing legislation.

For plan members commuting a defined benefit pension plan, the federal tax regulations limit the amount that can be transferred from an RPP to a locked-in plan on a tax-deferred basis. The pension plan administrator performs a complex actuarial calculation to determine the maximum transfer amount. Any commuted value that exceeds the maximum transfer amount is generally payable to the plan member in cash and taxable in the year received. If the plan

holder has RRSP contribution room available, he or she can make an RRSP contribution in the same year he or she received the commutation payment or within the first 60 days of the following year to offset some of that income inclusion.

When commuting a defined contribution pension plan, the entire commuted value of the pension is transferrable to a locked-in plan on a tax-deferred basis.

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By Invesco Tax & Estate team

In the second post of this series, we explore the various types of locked-in plans and unlocking options

December 28, 2023