You've Lost Your Job – What's Next?

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The sudden loss of your job is an emotional, gut-wrenching experience, regardless of whether you are being terminated or offered some kind of early retirement package. Having someone say they chose you as part of an employee reduction program can be a crushing blow to your confidence and self-worth. One day you have an income, a purpose, a place to go. The next day you are faced with some kind of personal or financial crisis, empty dark days looming ahead of you and the only certainty you can face is an uncertain future.

Unfortunately it's at this time, in the middle of a personal crisis, that you must make some lifestyle and financial decisions that will affect your future long after your job has ended.

If you find yourself in this position, you will be faced with a myriad of financial decisions regarding your severance package. One of those options may include you being eligible for a retiring allowance.

What is a Retiring Allowance?

A retiring allowance is an amount you may receive if you are given an early retirement package, usually in recognition of long service. If your position is terminated, this is the portion that is considered termination pay, i.e. compensation for loss of employment, which is also based on your years of service.

The advantage of having these payments being classified as a retiring allowance is that they receive preferential tax treatment. There are special rollover rules where these monies can be transferred into your RRSP without affecting your RRSP deduction limit. This is also a great opportunity to significantly increase the value of your RRSP. If you do not wish to take advantage of this special rollover, you can choose to take your severance in cash. Keep in mind, when you do that, that amount is fully taxable and is included in your taxable income for the year.

What Other Payments Can be Classified as a Retiring Allowance?

Many employees who leave or retire early will receive pay for items such as bonuses, commission payments, accumulated overtime, and unused vacation credits. These monies are all considered to be employment income and do not qualify as a retiring allowance. However, for those of you who have unused sick leave credits, these monies do qualify as a retiring allowance.

What Can Be Transferred To An RRSP?

There are two parts of the retiring allowance that may be transferred to an RRSP.

The first amount is what is considered to be the *eligible amount*.

- The maximum amount of the eligible amount that can be transferred is $2,000 for each complete or partial year of service prior to 1996; and
- $1,500 for each year before 1989 where employer contributions to a pension plan or DPSP had not vested.

The second part would be referred to as the *non-eligible amount*, which is the remaining amount of the retiring allowance that does not qualify above. The remaining amount could be transferred to an RRSP provided you have the contribution room available.

Let's look at two scenarios here. Sarah and Dave both began working for a company back in 1982. Sarah's company had a pension plan; however, Dave's company did not have a pension plan. Recently, both of them were laid off and were a given a severance package.

	Sarah	Dave
	(Pension Plan)	(No Pension Plan)
Termination Pay	$65,000	$65,000
Step 1: Number of calendar years employed prior to 1996: 14 years x $2,000 = $28,000. While there are 29 years between 1983 and 2011, it is the number of years before 1996 that are relevant in this calculation.		
	$28,000	$28,000
Step 2: Prior to 1989, the number of calendar years employed when not a member of a vested pension plan or DPSP, Sarah has 0 years that she was in a pension. Dave qualifies for 7 years @ $1,500 per year (1982–1989) as he has no pension.		
	$0	$10,500
Total eligible for transfer to an RRSP as a retiring allowance	$28,000	$38,500

In our example, Sarah can transfer only $28,000 into an RRSP as a retiring allowance, while Dave can transfer $38,500 because he was never a member of a pension plan.

The *eligible* portion of a retiring allowance can only be transferred to a personal RRSP and cannot be transferred to a spouse or spousal RRSP.

The balance is the *non-eligible amount* which would have to be taken into income, just like salary or wages, and taxed accordingly. Or, if Sarah or Dave have unused RRSP contribution room, they can transfer this into their RSP or to a spousal RSP and take the offsetting deduction, thus avoiding immediate tax.

Tax Reporting

Starting in 2011 (for the 2010 tax year) retiring allowances will be reported on the T4 slip instead of the T4A slip. Your former employer is responsible for preparing the T4 slip which will indicate the *eligible* and *non-eligible* amounts of the retiring allowance. You, the employee, will then report the full amount of the retiring allowance from box 66 (*eligible* amount) and box 67 (*non-eligible* amount) of the T4 as "other income" on your personal income tax return. An RRSP contribution slip – sometimes referred to as a 60(j.1) receipt – would then be issued to you to claim an offsetting deduction for the *eligible* amount. If the *non-eligible* portion is used towards an RSP contribution, then you will receive an RRSP contribution receipt for the deduction.

For the portion that is not directly transferred to your RRSP and is taken as cash, your employer is required to withhold tax at source. So, for example:

- 10% (5% for Quebec) on amounts up to and including $5,000;
- 20% (10% for Quebec) on amounts over $5,000, up to and including $15,000; and
- 30% (15% for Quebec) on amounts over $15,000.

Recipients and employees may have to pay additional tax on these amounts when they file their tax returns.

In Summary

If you have been offered a severance package, take the time to understand it fully. You need to know how long any severance income will last, as well as the tax considerations if you do take it as a lump sum. Many packages may reduce or eliminate a major portion of your severance if you should find another job. This certainly reduces the incentive for one to return to the workforce any time soon.

Remember, you have many years experience in the workforce. People will pay for your wisdom. You do have a lot to offer. Many people use this time to reflect on their life and to plan for the future they deserve. Most importantly, "this too shall pass". Many of you will look back at this as a life-changing experience and wonder why you stayed at your previous employer for so long.

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