

Information from the National Post today as an example of the possibilities.

RRSP Can Be Used For Pension Plan Buyback

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Question I am a retired federal public servant and I am buying back some 11 years of past service.

I have about \$85,000 in a self-directed RRSP administered by a brokerage firm. I just turned 64.

What I would like to find out is whether I can use funds in my RRSP to cover the buyback, either on a monthly basis or in a lump sum, and also whether I could start doing this now or when I have to start drawing down on the RRSP?

Answer Pension plans can be divided into two basic groups: defined contribution plans and defined benefit plans. Defined contribution plans are the simplest. They define the amount you and your employer can deposit into the plan. Just like an RRSP, the ultimate retirement income that you can expect from a defined contribution plan is not defined. It is completely dependent on the rate of return on the money invested.

Federal government employees belong to a defined benefit pension plan. With this type of pension plan, the employer guarantees the amount of retirement income based on a formula such as years of service times 2% of the average wage over the last five years of employment. Using this formula, an employee with 35 years of service would be entitled to a pension of 70% of their average salary over the last five years.

A member of a defined benefit pension plan who has fewer years of service will receive a smaller pension. To assist employees who find themselves with reduced pensions because they don't have enough years of service, pension plans may allow the employee to "buy back" years of service by putting money into the pension. The money can come in the form of lump-sum or instalment contributions from the employee's non-registered savings, or by a direct transfer from another registered plan, such as an RRSP.

You should check with your pension plan administrator to make sure that the option to transfer from an RRSP to your pension plan is still available. In certain situations, there is a limited time period during which you can elect to transfer money from your RRSP after which you are limited to making non-registered contributions. When buying back pensionable service using a transfer from your RRSP, this would be done as a lump-sum direct transfer rather than by instalments. Assuming you are allowed to transfer money from your RRSP to your pension plan, you do not have to wait until the RRSP is converted into a RRIF.

When making the decision to buy back years of service, a number of pros and cons should be considered. On the pro side, a defined benefit pension plan with an employer like the federal government provides great financial security. It is guaranteed to pay an income each year until

you pass away. There is no chance of outliving your money, and you are not responsible for making investment decisions regarding the capital that is funding the pension. Also, money in your registered pension plan is probably creditor-proof while savings in your RRSP or non-registered portfolio might be attached by a creditor in the event of financial difficulty. Finally, some pension plans have ancillary health benefits that may only be available to members with more than a certain number of years of service. Buying back service to qualify for these benefits may be an excellent investment.

There are also some factors that favour not buying back pensionable service.

Once the money is put into the pension plan, there may be limited benefits to your surviving spouse and estate. While money in an RRSP rolls over tax-free to a surviving spouse and pays out on an after-tax basis to other beneficiaries, many defined benefit pension plans cut the income to a surviving spouse in half and give nothing to the estate once the surviving spouse is gone.

Before buying back pensionable service, you should always have a competent advisor calculate what rate of return you would need to achieve on an alternative investment to match the increased benefits you are receiving from the pension. On the off-chance that an alternative investment would only need to provide a very modest return to beat the pension, then buying back pensionable service might not be the right choice.

To get information on the Public Service Superannuation Plan call toll-free at 800-561-7930 or visit the Web site at www.pwgscc.gc.ca. Or, you can provide your financial advisor with written authorization to speak with your pension plan administrator directly.

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