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Beneficiary Robert Rabnett (left) with financial planner Blair MacLean. PAR restores RRSP room to those who leave pension plans.

Recipients of pension adjustment reversals have until month-end to contribute

The benefits of PARs

BY MICHAEL KANE

VANCOUVER • When Bob Rabnett's employer was swallowed up by a U.S. company, his pensionable job and six-figure salary also went south.

But Mr. Rabnett, 37, is not complaining. Instead, he's using his severance settlement to establish his own freight-forwarding business close to home in Vancouver. His former employer is one of his key customers. At the same time he is one of thousands of Canadians celebrating a windfall tax break from Ottawa.

In Mr. Rabnett's case, it's a cool $53,847 in additional contribution room for his registered retirement savings plan. That will cut his 1998 tax bill by about $30,000, says Blair MacLean, his financial planner.

Mr. Rabnett is one of an estimated 240,000 Canadians who have left pensionable jobs since 1996 and are the first beneficiaries of PAR – the pension adjustment reversal announced in the 1997 federal budget.

Pension administrators were required to report PARs on a new tax slip, the T10, by March 31. Unlike most Canadians, who faced a March 1 RRSP deadline, PAR recipients have until the end of this month to make RRSP contributions deductible from their 1998 taxes. They can also carry forward unused room to later years if they choose.

In a nutshell, PAR restores RRSP room to employees who terminate their membership in a defined benefit pension plan or deferred profit-sharing plan before retirement.

Defined benefit plans guarantee a set retirement income in advance and impose an offsetting reduction of annual RRSP contribution room called the pension adjustment.

The problem is that the pension adjustment, introduced in 1990 and reported on each year's T4, assumes the plan member has a Cadillac pension like the indexed one for public servants that provides 2% of final average earnings for each year of service. The pension adjustment is also calculated as if the member will put in a full career. If the pension is not allowed to grow to maturity, the commuted value of each year's contribution is far less than each year's lost RRSP room.

In Mr. Rabnett's case, 10 years in the pension plan at Harmac Pacific – absorbed last year by Oregon-based Pope & Talbot – netted a commuted value of only $26,716. That sum has been transferred to a locked-in RRSP that can't be touched before Rabnett reaches age 55.

Until PAR, pension plan members who were laid off, switched jobs, or terminated their plan for any reason, or who belonged to less generous plans, often ended up far worse off than if they had been contributing to an RRSP the annual maximum granted to individuals who don't have a pension plan.

PAR restores some of the reduced RRSP contribution room for employees who terminate their plan after Dec. 31, 1996, and may provide a convenient tax shelter for any severance pay.

Direct transfer of severance pay to a personal RRSP is limited to $2,000 for each year of service prior to 1996, plus an additional $1,500 for each year of service prior to 1989 for which the employee was not a member of a registered pension plan. Now some or all of the remaining severance can be tax-sheltered.

PAR is not perfect. Mr. Rabnett has forfeited the earnings that RRSP investments could have generated while he was in the pension plan but the commuted value of his pension is some compensation.

"He didn't get any growth but he got almost $27,000 out of the plan to compensate for growth," said Mr. MacLean, the president of B.C. Partners in Planning, of West Vancouver.

Mr. Rabnett, who is married, has one child, and recently bought a house, says severance is working out well.

"It's given me the opportunity to build my own business and still work with people I know. Financially I am better off, although it's too early to say how much better off. From a tax standpoint, being self-employed in Canada is more advantageous than being an employee. No two ways about it."

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