McMaster University

Surplus Share Payment Options Guidebook

FEBRUARY 2002

For Inactive Plan Members

Key Terms

Canada Customs and Revenue Agency (CCRA) is the name adopted on November 1, 1999 by the department of the federal government formerly known as Revenue Canada.

Deferred pension means a pension to which an employee is entitled at the time the employee terminates employment before being eligible to retire. Payments begin at normal retirement age (usually age 65). A terminated employee who is owed a deferred pension may choose to begin it before normal retirement age, but usually there is a reduction in the annual pension to account for the early start date.

McMaster Salaried Pension Plan (MSPP) or the **Plan** means the *Contributory Pension Plan for Salaried Employees of McMaster University Including McMaster Divinity College 2000*, or any predecessor thereto.

Plan member means a member of the *MSPP*.

Registered retirement income fund (RRIF) is a tax-sheltered savings account to which money that would otherwise be in an *RRSP* must be transferred after age 69 and may be transferred at an earlier age. A certain minimum amount of money must be withdrawn from a RRIF each year.

Registered retirement savings plan (RRSP) is a special type of savings account at a financial institution or an insurance company. You may make tax-deductible contributions to an RRSP up to an annual limit set out in the *Income Tax Act* (Canada).

Withholding tax is tax deducted at source on payments that qualify as income according to income tax regulations. For most Canadian residents, lump-sum cash distributions of up to $5,000 require a withholding tax of 10%. Lump sums between $5,000 and $15,000 have 20% withholding tax applied to the entire amount, while those of more than $15,000 have 30% withholding tax applied to the entire amount. Depending on your tax status, you may have to pay more or less when you file your tax return than the amount that was originally withheld. A withholding tax of 25% generally applies to all cash payments made to non-residents of Canada.

Be sure to read this guidebook in conjunction with your personalized Surplus Share Statement that is enclosed in this package.

This guidebook provides only a summary of pension information pertaining to the sharing of pension surplus for the *Contributory Pension Plan for Salaried Employees of McMaster University Including McMaster Divinity College 2000* (the MSPP). In the event of any conflict, error, or omission of information in this booklet, your actual entitlement will always be governed by your correct employment, plan membership, and other data; the approved Surplus Sharing Settlement Agreement; and the legal requirements of the MSPP, the *Pension Benefits Act* (Ontario), and the *Income Tax Act* (Canada). **This surplus distribution is conditional upon approval by the Financial Services Commission of Ontario.**

A copy of the Surplus Sharing Settlement Agreement, other documents related to the Agreement, and the text of the MSPP can be found on the McMaster Web site at **www.mcmaster.ca/mufa/pensurplus.html.**

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About This Guidebook

You have received this personalized Surplus Share Decision Kit because you are eligible to receive a share of the surplus being distributed from the McMaster Salaried Pension Plan (MSPP).

The amount of the surplus that you are eligible to receive – your *surplus share* – appears on your personalized Surplus Share Statement. Interest will be added to this amount according to the formula described on page 8.

The surplus is being paid out according to the Surplus Sharing Settlement Agreement reached between McMaster University and you and your representatives.

Your Important Decision

Your Decision Process

We ask you to take the following steps to make your decision:

- Read your personalized Surplus Share Statement.
- Read this guidebook and highlight the sections that describe your payment options.
- Consult a personal financial adviser or tax specialist. (This is optional, but should be considered.)
- Select your payment option(s).
- Fill out the Option Form, check that it is complete, and make a copy for yourself.
- Enclose any other required documents (see "Documents You Need" on pages 4, 6 and 7), and make a copy for yourself.
- Send the original Option Form and any other required documents in the enclosed return envelope – **postmarked by April 30, 2002**. You may also reply by fax to McMaster at (905) 529-3272. If you reply by fax, you must still send the original documents in the enclosed return envelope as soon as possible.

There is more than one way to receive your surplus share. **The specific payment options that may apply to you appear on your Statement.** The available options are restricted by pension and tax law.

It is up to you to decide among your available options, and there is a deadline for making your decision. An Option Form is provided in your Surplus Share Decision Kit, along with a return envelope, so you can inform McMaster of the payment option you prefer.

The Decision Deadline

This surplus distribution is conditional upon approval by the provincial pension regulator, the Financial Services Commission of Ontario (FSCO). Any surplus shares not already earmarked for a tax-sheltered option on the date FSCO approves the surplus distribution will be taxed as regular income in accordance with the *Income Tax Act* (Canada). We do not anticipate regulatory approval before April 30, 2002, but the exact approval date is not known.

Your completed Option Form should be **postmarked no later than April 30, 2002.** Any forms received after this date will still result in favourable tax treatment if legally possible. You should enclose other documents, if required, depending on your chosen option. If you are unable to collect the necessary documents by April 30, 2002, you should still submit the Option Form with a note that further documents will follow.

An envelope is supplied for returning your Option Form and any other required documents. If the envelope is missing, send your Option Form to:

Pension Surplus
Human Resources/Benefits
McMaster University
1280 Main St. W.
Hamilton ON L8S 4S1

You will get an acknowledgement, either by mail (if you mailed your form) or by fax (if you faxed your form and supplied a return fax number), that your Option Form has been received by McMaster.

The Default Option

If your Option Form is not postmarked by the time regulatory approval is granted, you will receive the default option – **a cash payment, less withholding tax**. See “Key Terms” on the inside cover for a further description of withholding tax. The tax withheld does not necessarily represent the full tax payable on the cash distribution. If you have any questions about tax withholding, or the taxes you will have to pay as a result of this surplus distribution, please consult your financial adviser or tax specialist.

Sources of Assistance

The text of the Surplus Sharing Settlement Agreement and other related documents are available on the McMaster Web site at **www.mcmaster.ca/mufa/pensurplus.html.** If you need guidance to complete the Option Form or to understand the options, help is available from these services:

- McMaster Surplus Hotline: **(905) 525-9140 ext. 24272** (Collect calls will be accepted.)
- Surplus Query E-mail: **surplus@mcmaster.ca**

If there is no staff member available when you call the Surplus Hotline please leave a recorded message with your name, employee identification number, phone number, and your question. **We anticipate a high volume of calls, so the staff will try to provide answers to all inquiries within three to five business days**.

Neither service can tell you which option is best for your situation. For such assistance, you should obtain independent advice from your own financial adviser or tax specialist.

Reading Your Statement

Surplus Sharing Amount

The amount of the surplus that you are eligible to receive – your *surplus share* – appears on your personalized Surplus Share Statement. Interest will be added to this amount according to the formula described on page 8.

The basis for calculating your surplus share is set out in the Surplus Sharing Settlement Agreement. Since the dollar amount set out in the current statement reflects the most up-to-date calculation of surplus payable to you, it may differ somewhat from the estimate provided to you in 2001.

Your Data

The personal data appearing on your Statement was drawn from McMaster records. With a few exceptions, it should be identical to the data reported on the Surplus Estimate Statement provided to you. You may direct any questions about the Statement or about your personal information to McMaster by calling the Surplus Hotline at (905) 525-9140 ext. 24272 (collect calls will be accepted), or by sending a Surplus Query E-mail to **surplus@mcmaster.ca.**

Surplus shares are determined by the liability in the MSPP for all plan members. If one plan member’s data changes, then all plan members’ surplus shares must be adjusted. As a result, all surplus shares will be recalculated for the last time based on data reported to McMaster as at April 30, 2002. Any additional surplus share amounts will be paid in cash. Any reductions in your surplus share will first be applied to Option A (cash less withholding tax) then Option B (transfer to your registered retirement savings plan) then Option C (conversion of surplus share to additional voluntary contributions).

Option Descriptions

The options available to you depend on your status in the MSPP as of April 30, 2002.

Since you are an **inactive plan member** (pensioner, terminated employee with a deferred pension, or beneficiary pensioner), your options are:

Option A: Cash less withholding tax (default option)

Option B: Transfer to your registered retirement savings plan (RRSP) to the extent that you have available RRSP contribution room and are under age 69 on December 31, 2001

Option C: Conversion of the surplus share to additional voluntary contributions (AVCs), which may be used to purchase an annuity or may be transferred to your RRSP or RRIF

You may select more than one option. If you do, you must indicate on your Surplus Share Option Form the dollar amount of your surplus share that you wish to direct to each option.

Any pension benefits you have earned under the MSPP are not affected by your allocated surplus share.

Option A: Cash Less Withholding Tax (default option)

How It Works

Anyone eligible for a surplus share may choose the cash option.

This will also be the option assigned to you if you do not return your Surplus Share Option Form by the deadline.

Tax Issues

The cash payment will increase your taxable income in the year you receive it, and applicable withholding tax will be deducted at source. This tax withheld does not necessarily represent the full tax payable on the cash distribution.

As a result of the increase in your taxable income, your eligibility for certain tax credits, such as the GST and child tax credits, may be reduced or eliminated. The degree to which you qualify for social assistance (such as the Guaranteed Income Supplement) or other government benefits (such as Old Age Security) may also be affected. Contact Human Resources Development Canada if you have any questions related to eligibility for these benefits. In Hamilton, call (905) 572-2211; for other locations, the number is located in the blue pages of your phone book.

Taking the cash option prevents you from deferring tax on your surplus share. **A financial adviser or tax specialist can help you determine if this is the best option for you.**

Documents You Need

To choose the cash option, select Option A on your Surplus Share Option Form, sign the form, and return it postmarked by April 30, 2002.

You do not need to submit other forms.

Option B: Transfer to Your Registered Retirement Savings Plan (RRSP) to the Extent That You Have Available RRSP Contribution Room

How It Works

Anyone eligible for a surplus share may transfer some or all of it to a personal RRSP if the following conditions are met:

- You must be under age 69 on December 31, 2001.
- You must have available RRSP contribution room (see page 6).
- The RRSP must be in your name or the name of your eligible spouse and should be a non-locked-in RRSP.
- The transfer must comply with income tax regulations.

Under current income tax regulations, no withholding tax will apply to amounts that are transferred or contributed on behalf of Canadian residents directly to a non-locked-in RRSP.

What's the difference between a non-locked-in RRSP and a locked-in RRSP?

A non-locked-in RRSP is the most common kind of RRSP at financial institutions. *Non-locked-in* simply means that you can withdraw amounts from the RRSP at will (although the money is still subject to tax when withdrawn). Money in *locked-in* RRSPs is not available for withdrawal until retirement, and even then can only be withdrawn in regular small amounts like a pension.

What is RRSP contribution room?

Income tax law defines the amount you may contribute to a personal RRSP in a given year – this amount is called your *contribution room* or *RRSP room*. If you don't use your full RRSP room in a certain year, it can be *carried forward* so you can use it some time in the future.

Tax Issues

If you choose Option B, the amount being transferred will be considered an addition to your income. You may claim a corresponding deduction for the transfer to your RRSP or that of your eligible spouse. Therefore, the tax charged on the increased income will be offset by the deduction allowed for the RRSP contribution. The combined effect will result in no change in the income tax you pay in that year. However, as with the cash option, as a result of the increase in your taxable income, your eligibility for certain tax credits, such as the GST and child tax credits, may be reduced or eliminated. The degree to which you qualify for social assistance (such as the Guaranteed Income Supplement) or other government benefits (such as Old Age Security) may also be affected. Contact Human Resources Development Canada if you have any questions related to eligibility for these benefits. In Hamilton, call (905) 572-2211; for other locations, the number is located in the blue pages of your phone book.

You may only transfer your surplus share to an RRSP to the extent that you have RRSP contribution room available (see question below). Otherwise, a penalty tax for over-contribution will apply.

It is your responsibility to ensure that you have sufficient RRSP contribution room. If you are not a Canadian resident, withholding tax may be applied to amounts transferred or contributed directly to a non-locked-in RRSP.

How do I know how much available RRSP contribution room I have?

Each year, you receive a Notice of Assessment from the government after you file your tax return. This document shows your available RRSP contribution room, including contribution room carried forward from previous years.

In addition, you are allowed a lifetime over-contribution of $2,000. You cannot get a tax deduction for this allowable over-contribution, but the money can remain in your RRSP without penalty.

If you exceed your total contribution room, including the over-contribution allowance, the Canada Customs and Revenue Agency (CCRA) will charge a penalty tax of 1% *per month* on the extra amount until it is withdrawn from your RRSP.

Documents You Need

To receive some or all of your surplus share as a direct RRSP contribution, select Option B on your Surplus Share Option Form and complete the enclosed Transfer Form (T2151). Sign both forms and return them postmarked by April 30, 2002.

If you do not already have a non-locked-in RRSP, you will have to open one at a financial institution and complete the necessary forms. Once you have set up an RRSP, or if you already have one, you should inform your financial institution that you will be transferring money from a pension plan into the RRSP as part of a surplus sharing settlement agreement. **Your financial institution will need to know that the money being transferred is NOT locked-in**. They will supply the necessary forms for you to fill out so that the transfer can be completed.

Option C: Conversion of the Surplus Share to Additional Voluntary Contributions (AVCs)

How It Works

This option allows you, as an inactive member, to tax-shelter some or all of your surplus share if you made required contributions to the MSPP prior to 1991.

Essentially, by choosing Option C, you will convert those required contributions (with accumulated interest to July 1, 2000), up to the value of your surplus share, into additional voluntary contributions (AVCs) under the Plan. Once you have done this, you have several options for using the AVCs. In connection with the distribution of the surplus, you can

- leave the AVCs in the MSPP until December 1 of the year of your sixty-ninth birthday,
- use the AVC amount to purchase an annuity of any type, or
- transfer the AVC amount to an RRSP or RRIF (depending on your age*). You do not need to have available RRSP room to make this transfer.

** You must choose a RRIF if the date of transfer is later than December 1 of the year you reach age 69.*

The amount of your surplus share that you may convert to AVCs cannot be greater than your total pre-1991 required contributions to the Plan (increased with interest to July 1, 2000). If your surplus share is greater than your required contribution amount, the excess surplus share that cannot be converted to AVCs should be allocated to one of the other options.

Documents You Need

To apply some or all of your surplus share to the AVC option, select Option C on your Surplus Share Option Form, sign the form, and return it postmarked by April 30, 2002.

You do not need to submit other forms unless you wish to transfer these AVCs out of the MSPP immediately (e.g., to an RRSP or a RRIF). In that case, you should complete the enclosed Transfer Form (T2151) and submit it with your Option Form.

If you wish to transfer the AVCs to an annuity, you will need to contact an insurer to make the annuity purchase. They will supply a Form T2037. Once you have completed this form with the insurer, the University will require a copy in order to make the transfer to the insurer.

Interest on Your Surplus Share

The amount shown on your Surplus Share Statement is your final surplus sharing distribution, subject to adjustments for data changes, but does not include interest. Interest will be calculated on your surplus share and paid to you in cash, less withholding tax, *regardless of the payment option you chose for your surplus share*.

From July 1, 2000 to the end of the month prior to the month in which regulatory approval for the surplus distribution is received, interest will be credited at the rate of return earned by the assets of the MSPP (net of investment expenses). The maximum annual rate will be 6.5% and the minimum rate will be 0%. The maximum rate is the same as the interest assumption used in the actuarial valuation of the MSPP on July 1, 2000 (going-concern basis).

From the first day of the month in which regulatory approval is received until the date the surplus is distributed, interest will be credited at the Government of Canada 30-day treasury bill rate.

Questions & Answers

Q1: Can I make use of more than one option in the Option Form?

A1: Yes. You can make use of more than one option. The total dollar amount allocated to the options used must add up to your surplus share. There are limits on each of the tax-sheltered options that are unique to each individual. You are advised to read the section of the guidebook pertaining to that particular option to see how to determine your limit.

Q2: I am the surviving spouse of a now-deceased member of the MSPP. Can I make use of the member's pre-1991 contributions with interest to tax-shelter some of my surplus share?

A2: Yes. A surviving spouse in receipt of a survivor pension can use the pre-1991 contributions with interest accumulated by the plan member as a tax shelter. These contributions with interest made by the plan member are connected to the pension paid to the member or his/her spouse. Therefore, the individual in receipt of the pension can make use of the contributions made in respect of the pension being paid.

Q3: Whom can I designate as a beneficiary for this surplus payment in the event that something happens to me before the actual surplus distribution takes place?

A3: Section 48 of the *Pension Benefits Act* (Ontario) deals with the appointment of beneficiaries. It states that the beneficiary is the member's spouse or the same-sex partner on the date of the plan member's death, unless that person is living separate and apart from the plan member on that date. If there is no qualifying spouse or same-sex partner, the plan member may designate a beneficiary to receive the value of their benefit. If there is no such beneficiary designated, the member's estate becomes entitled to the value of the member's benefit.

Unfortunately, there is no provision to designate a separate beneficiary for situations such as surplus sharing. The beneficiary of your current pension entitlement will also be the beneficiary for your surplus entitlement.

For a plan member who has no residual benefit payable after his/her death (e.g., a current retiree who is receiving a pension but has no survivor benefit or guaranteed payments remaining), there is no provision to name a beneficiary. Therefore, in such a situation, any surplus payment would go to the estate of the plan member.

Q4: What happens if the plan member has passed away and the Option Form has to be completed by the executor of the estate or someone with Power of Attorney?

A4: Please call the Surplus Hotline at (905) 525-9140, ext. 24272 and describe this situation, noting who is the proper person to contact. A representative of the University will call this contact person to determine how to proceed.

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