LIRAs and LIFs: Definitions and strategies

We all know that life doesn't always go according to plan. You may end up changing jobs, getting divorced or receiving an inheritance from your spouse. If one of these events occurs, you might have to open a locked-in retirement account (LIRA) or life income fund (LIF). If you find yourself in this situation, here's what you need to know.

What is a LIRA for?

"A LIRA (locked-in retirement account) is a bit like a cocoon," explains Mélanie Beauvais, an advisor at National Bank Private Banking 1859's Expertise Centre. It's used to put aside money until retirement.

With a few exceptions, you can't withdraw money from your LIRA before you retire. It's not really possible to add more either.

Do you need a LIRA?

You can't get a LIRA unless you have a specific reason for doing so. You can open one if one of the following life events occurs:

1. You move jobs and decide to transfer your money from your former employer's pension plan to a LIRA.
2. You receive money from your former spouse's employer pension plan, during the division of assets when you divorce, for example.

Good to know

In all cases, the money must come from a pension plan, and the employer must be under provincial jurisdiction. If the pension plan is under federal jurisdiction, the appropriate vehicle is not a LIRA, but rather a locked-in RRSP.

There are some differences between the locked-in vehicles in each province and the locked-in RRSP. For example, the funds left from a pension plan under federal jurisdiction when your spouse dies are still locked in a locked-in RRSP or LIF. Although, in some provinces, the funds left from a pension plan under provincial jurisdiction will no longer be locked in for the surviving spouse. The main differences affect the accessibility and the withdrawal of the funds.

How do you withdraw money from a LIRA?

When you retire, there are three ways to withdraw money from LIRA.

One option is to turn the LIRA into a life income fund (LIF).

With a LIF, you can choose the frequency of withdrawals that suits you while respecting the minimum annual withdrawal. The money is tax-sheltered until it is withdrawn. It works like a RRIF (registered retirement income fund) but has less flexibility, because of the following characteristics:

1. There's an upper limit to the amount you can withdraw from your LIF each year, and it varies depending on the account balance and your age, as well as a factor determined by the government. It's impossible to predict with complete accuracy what your maximum withdrawal will be from one year to the next.
2. There is also a minimum annual withdrawal, which changes depending on your age. This mandatory minimum is calculated using the same method as the annual minimum withdrawal for a RRIF.
3. In the event of death, funds from a LIF are paid to the surviving spouse first.

The second option: a life annuity

You don't have to turn your LIRA into a LIF. You could also opt for a life annuity. Like a LIF, its objective is to provide a regular income for the rest of your life.

However, there are some major differences between these two investment vehicles.

"A LIF gives you the option of choosing the types of investments you want," explains Mélanie Beauvais. "LIFs are also more flexible in terms of the amount you can withdraw."

Once a life annuity is established, the amount is fixed and guaranteed for life and will not change regardless of fluctuations in the stock market or interest rates.

The third option

You can also choose both of the above, by turning part of your LIRA into a LIF and part into life annuities.

No matter which option you choose, you must turn your LIRA or locked-in RRSP into a LIF or life annuity no later than December 31 of the year in which you turn 71 years old.

Can you withdraw money from your LIRA before you retire?

Yes, but only in very specific situations.

For example, if you have a serious illness that reduces your life expectancy, or if your income is very low. But in all cases, you will need to convert the LIRA into a LIF before accessing the money. Remember that the rules vary between provinces.

Regardless of your situation, it's always best to meet with your advisor if you have a LIRA or plan to retire in the next few years. Because everyone's situation is unique, we're here to answer your questions.

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