Unlocking LIFs

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A minimum amount must be withdrawn from all registered retirement income funds (RRIFs) in the year after a RRIF is established. If, however, the funds were transferred to a RRIF from a registered pension plan, either directly or via an RRSP, then they are considered to be “locked-in” accounts under governing pension legislation. We will refer to these as Life Income Funds or LIFs.

LIFs are governed not only by the tax rules, but also by pension regulations. These could be federal pension rules, or provincial or territorial rules, depending on which legislation governed the pension plan from where the funds were transferred. In most jurisdictions, the pension regulations provide for a maximum amount that can be taken out of the LIF annually, which is calculated based on the value of your LIF at the beginning of the calendar year. In these cases, the LIF is subject to both a maximum and minimum withdrawal amount annually. In all cases, the applicable pension regulations outline the specific circumstances under which you can withdraw money beyond your maximum amount.

While many LIF holders only plan to withdraw the minimum amount annually, and are not concerned about the maximum amount, others may like more flexibility in how much they wish to withdraw in the current or a future year. For instance, there could be a time when a LIF holder has a large expenditure to cover, necessitating a large withdrawal. Or there could be a specific year when the LIF holder has very little other income, and would like the LIF withdrawal to be taxed at a relatively lower tax rate, and possibly not adversely impact certain income-tested benefits such as Old Age Security benefits.

Rather than withdrawing the maximum amount fully this year, and being subject to tax on that withdrawal, another option is to take the minimum payment, which would be taxed as income, and then “unlock” the difference between the LIF maximum and the LIF minimum by transferring it tax-free into a regular unlocked RRIF[1] which is not subject to the pension restrictions (this strategy is not available for LIFs governed under Quebec pension regulation). Once the funds are in a regular RRIF, they can be withdrawn as income at any time in the future with no limitations other than minimum amount withdrawals.

Each jurisdiction that has a maximum LIF withdrawal amount has its own formula for calculating that maximum. Some of the provinces calculate the maximum based, at least in part, on the preceding year’s investment return, as is the case for LIFs governed by the pension rules of Alberta, British Columbia, Manitoba, Ontario, and in some situations, Newfoundland & Labrador. Where investment returns for a year have been high, this increases maximum withdrawal amounts in the next year for those jurisdictions. For instance, due to the high rates of return of many of the popular North American equity markets in 2024, there is an opportunity to “unlock” a larger than usual amount from LIFs in 2025 in Alberta, British Columbia, Manitoba, Ontario, and in some situations, in Newfoundland & Labrador.

For example, assume that Henry, aged 80, has a LIF which holds assets with a fair market value of $500,000 on January 1, 2025. Henry’s minimum amount for 2025 is $34,100. Henry realized a 15% investment return in 2024. As such, his maximum amount for 2025 is $75,000. Henry decides to unlock this maximum amount in 2025. He withdraws the minimum amount of $34,100. He then transfers the $40,900 difference between the maximum amount of $75,000 and the minimum amount of $34,100 to a regular RRIF where it will no longer be subject to maximum amount regulations in future years.

Clients with LIFs in the applicable provinces listed above may wish to take advantage of strong market returns in a year to unlock a larger maximum amount in the next year.

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[1] For those age 71 or under, transfers to an RRSP may be possible.