Retirement-Proofing: IPP Basics

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Individual Pension Plans for Entrepreneurs

As an incorporated business owner, you have put significant time, resources, and effort into making your business successful. So how do you proceed with protecting and enhancing your retirement? It is easy to lose track of this end goal and put it off, or incorrectly believe that you have already exhausted all avenues of retirement savings.

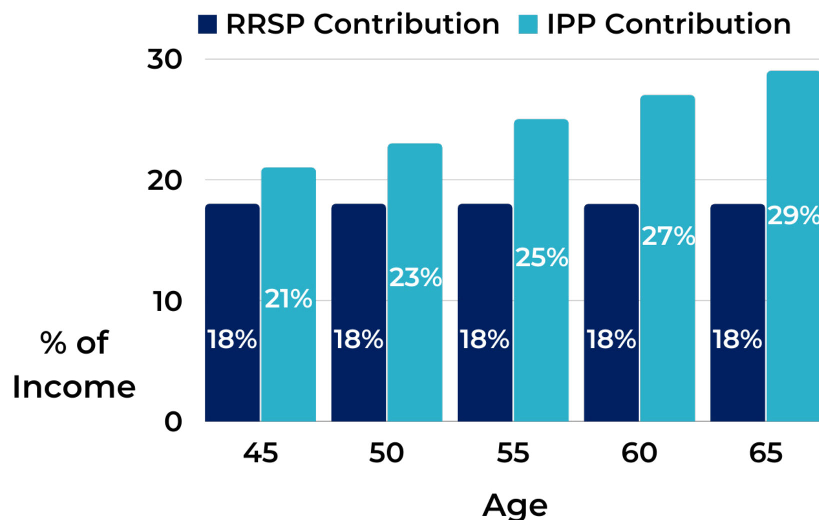
The investment counsellors at Qube believe this planning needs to be front of mind. In a scenario where you save for retirement primarily through an RRSP, maxing out your contributions may still not be enough to maintain your quality of life as you transition into retirement.

Having realized this problem, the next hurdle is to decide on how else to invest for retirement. The options can seem endless but, for a business owner who is drawing a salary, one option in particular stands out: an Individual Pension Plan (IPP).

What is an IPP?

An IPP is a registered, defined-benefit pension plan usually set up exclusively for the business's owners. Like an RRSP, it can let you build up retirement assets in a tax-sheltered account. But it also allows you to provide yourself with the largest possible pension that Canadian tax law allows.

Unlike an RRSP, tax deductible contributions are not limited to 18% of income. Instead, for individuals over age 40, IPPs can create annual contribution room that starts out higher than allowed with RRSPs. This contribution room continues to increase with age.



Source: West Coast Actuaries (for illustration purposes only).

This solves the problem of limited contribution room, bringing your retirement savings in line with your expected lifestyle post-retirement. An Individual Pension Plan can save you from being unable to enjoy your retirement the way you have always dreamed.

The Criteria

To set up an IPP and become a plan sponsor, your company must be incorporated. And to be an IPP plan member, you must:

- be an employee or a shareholder of the sponsoring company, and
- earn "T4 income" (salary that is reported on your annual T4 statement).

Beyond the above requirements, an IPP could be a good fit for you if:

- you are 45 or older,
- you have owned your business for 10 or more years, and
- you have paid yourself a T4 salary for most if not all years you have been employed by your company.

Keep in mind, these are just preliminary checks. As we will discuss further in an upcoming white paper, "Changing Perspectives on IPPs," there are a fair number of factors to account for if you want to maximize the benefits of this planning.

One caveat to IPPs is their effect on RRSPs. Unfortunately, you cannot have your cake and eat it too. Contributions to an IPP will create a pension adjustment that will decrease—and all but eliminate—new RRSP contribution room. You'll also need to make a non-taxable transfer from your RRSP account for a portion of the past-service funding.

Tax Savings

Not only can an IPP give you more retirement income by way of increased contribution room, the contributions and any associated administrative costs are tax-deductible to your company. It follows that the higher the contribution amount, the higher are the corporate tax deductions.

In the first year of your plan, your business will typically be able to contribute a large, one-time, tax-deductible lump-sum contribution known as past-service funding. This contribution opportunity is like a pension buy-back. When the plan is set up, we're able to look back to all prior years that the member was drawing T4 salary and make a catch-up payment. In truth, the past-service contribution opportunity is often the primary impetus for setting up an IPP as the amount available to contribute will often exceed $250,000.

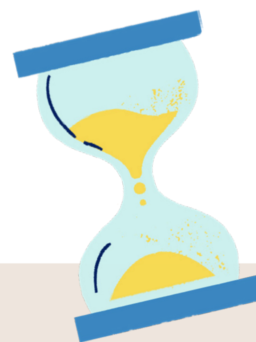
For all subsequent years, annual contribution room in the IPP will exceed the RRSP maximum. The corporation will also be able to deduct interest on borrowed funds, actuarial fees, accounting fees, and investment management fees. This is drastically different from RRSPs and other tax-preferred investment accounts.

IPPs in Retirement

So at this point, you have contributed to your IPP for a good number of years. When you retire or leave your employer, you have several options. You can:

- receive a monthly pension from the plan,
- wind up the plan and transfer the commuted value of the plan to a Locked In Retirement Ac-

In terms of the timing for these events, the rules for IPPs are like those for RRSPs. You must pursue a wind-up of the plan or start receiving income from your IPP by the end of the year you turn 71. When you die, any remaining value goes to your surviving spouse or to your estate.



In Conclusion...

You do not want to be mistaken in thinking that your current retirement planning is sufficient to cover your post-retirement needs. No one wants their quality of life to dip just as they are preparing to finally kick up their feet.

IPPs are for an exclusive group whose way of life necessitates a re-examining of their retirement plan. And an IPP may very well be right for you, but arriving at that decision and the eventual set-up will require a fair amount of expertise. We highly advise working with a wealth management firm like Qube that has a substantial depth of expertise with this planning. Send us an email, or call us at (780) 463-2688 to discuss how we can improve your retirement plan.

Again, keep an eye out for our upcoming white paper, which will provide a far more in-depth analysis on how IPPs work and, for that matter, work best.