The Commuted Value Option at GM

In the September 2012 Detroit 3 negotiations, Unifor (then "CAW") agreed to the Ford and GM request on commuted value (CV) options. After December 31, 2012, Unifor members retiring with GM will have the option to take the commuted value of their pension in lieu of the monthly pension. The union did not propose the commuted value option, and we do not believe that it is a good option for our members. We agreed to the option because it would enable us to reach an agreement in bargaining.

Members approaching retirement will decide whether or not to opt for the commuted value. This information sheet will give members some points for consideration in making their decision.

What is the "commuted value" option?

Upon retirement, pension plan members receive a monthly pension based on their years of service, their benefit class, and their age at retirement. The pension is payable for their lifetime. With the new commuted value (CV) option, the member will be able to take the lump sum value of the pension rather than a monthly pension.

At GM, members who retire on or after January 1, 2013 need to apply for retirement 30 to 60 days in advance. If you want the CV option, you will need to advice GM at least 15 days prior to when their pension is payable. Otherwise, the default is the monthly pension. As of October 2014, the CV option is not available to members who retire after their 65th birthday.

The CV is an estimate of how much money must be set aside at your retirement in order to pay your monthly pension for your lifetime (and your spouse's life if you have a joint and survivor pension). The CV is based on life expectancy tables and interest rates at the time of retirement. In addition to the basic lifetime pension, the CV will include, for those eligible, the special allowance and supplementary pension to age 65.

The CV amount will likely exceed the income tax limits. The excess amount is paid in cash and subject to an immediate tax. The remaining funds are treated as tax sheltered retirement income and subject to locking in rules. The funds can be used as follows:

- Purchase an immediate or deferred annuity (a monthly pension). The deferral can be until age 71.
- Transfer the funds to a Life Income Fund (LIF). The LIF is similar to an RRSP in that you can oversee your investments, but LIFs have rules on the maximum amount that can be withdrawn in any year.
- Transfer the funds to another pension plan if the plan sponsor will accept the transfer (this rarely happens).

What are the drawbacks on the CV option?

The CV option is not tax efficient.

Over the years, the Unifor has bargained an excellent pension benefit with GM. Consequently, the CV is high and for the majority of Unifor members, their CV will exceed the limits set under the income tax act for tax sheltering retirement income. The Maximum Transfer Value (MTV) is the amount that you can transfer tax free to a locked in retirement fund. Here are some examples of CVs at different ages and the MTV:

	Age 55	Age 60
CV	$640,000	$510,000
MTV	$256,500	$284,000
Excess and Taxable	$383,500	$226,000
Tax payable @40%	$153,400	$90,400
Cash paid to member	$230,100	$135,600

A member age 55 with a special allowance of $3,515 per month to age 65 and a lifetime monthly pension of $2,055 thereafter, would have a CV of approximately $640,000. They could transfer

Please Note!!!!

The above examples are based on certain interest rates and assumptions. Each individual must get their own CV estimate. The example shows the tax treatment of the CV option. Because interest rates can change each month, the CV amount may vary from month to month. Employees looking at estimates for the CV should understand that their actual CV amount on retirement could be different depending on interest rates. Once the employee signs off on their retirement application, their CV amount remains fixed.

$256,500 to a LIF and receive, after taxes, an additional $230,100 in cash. They might pay $153,400 or 24% of the CV (depending on their income tax bracket) in withholding taxes.

Possible ways to reduce the tax payable:

- If you have RRSP contribution room, you can transfer some of the excess funds to your RRSP and claim a deduction. As of December 2014, GM will provide forms for the direct transfer of funds in excess of the MTV. The member is responsible to ensure that they have sufficient RRSP contribution room to make the transfer to an RRSP. There is a significant tax of 1% per month on over contributions to RRSPs. You will find your RRSP contribution room on your income tax Notice of Assessment from CRA for the income tax. Can't find your Notice of Assessment? Go to the CRA website or call 1-800-267-6999 to request a copy.
- Upon termination of employment, CRA does allow a tax-free transfer of $2,000 per year of employment prior to 1996 to an RRSP. However, that only applies to retirement allowances and not to the CV in excess of the MTV.

Annuities are expensive

If you want the steady stream of monthly payments that the GM pension provides but prefer to have the payments come from a financial institution rather than the GM pension plan, you could purchase a monthly annuity from an insurance carrier. Financial institutions provide annuities – a monthly pension with options for a joint and survivor pension and/or guaranteed periods of payment. However, these "products" are expensive.

For example, a 60 year old member with a single life pension (ie, no spouse) and 30 years of service with a benefit class of $68.50 could retire with a Special Allowance of $3,515 per month to age 65 and a lifetime monthly pension of $2,055 thereafter. The CV would be about $510,500 (before taxes). On the annuity market, the lifetime monthly pension of $2,055 would cost $500,000 – with NO Special Allowance.

If you have a spouse, you must purchase an annuity with a joint and survivor benefit unless your spouse signs a waiver. The GM pension has a high value joint and survivor benefit which will be very expensive to purchase in an annuity.

Update April 2014

Annuity companies such as Sun Life have started to offer annuities which mirror the GM pension plan for the same amount (or even less) than the CV. When the annuity is less than the CV, the member receives the surplus funds in cash (which is taxable). GM will make the transfer to an annuity upon the member's instructions.

The annuity provides the member with a set monthly pension, which can be assuring for those who do not want to track investment funds. And some members may prefer to rely on the insurance carrier rather than GM for the security of their pension funding.

Members will have to decide for themselves whether to purchase an annuity, and they might consider the following:

- The ITA requires that the annuity "must provide for payment of a benefit that is not materially different from the benefit the member would be entitled to under the plan."[1] CRA does not define "materially different".
- The annuity may not be exactly the same as the GM monthly pension. Some provisions to check: is there a "pop up" in the spousal benefit if the partner pre-deceases the retiree? Are the GM options for a guarantee period available in the annuity? Ask the annuity provider exactly how the annuity will differ from the GM monthly pension.[2]
- If the annuity provider were to go out of business, how is the member's annuity protected? Does the annuity provider have Assuris coverage (which can guarantee the greater of 85% of the pension and $2,000 per month)? What is covered?
- Be aware that if the annuity provider quotes on an estimated CV amount, but the actual CV amount is less than the estimate, your monthly benefit could be adjusted. Ask how the annuity provider will handle the quotes for an annuity.

So what about a Life Income Fund (LIF)?

Canada Revenue Agency (CRA) sets a MTV for the amount of your CV that can be transferred tax-free to a locked in retirement fund or LIF. The LIF has rules on annual withdrawals, but you are able to invest your funds and any interest on the funds is tax sheltered in the fund.

[1] From the Investment Planning Counsel information session for GM employees.
[2] One annuity provider recognized the "fluid" situation and recommended that each employee contact a tax specialist.

The LIF maximum annual withdrawal in 2012 (as set according to government long term bond rates) is 6.2% of the savings for a 50 year old, 6.5% of the savings for a 55 year old, 7.38% of savings for a 65 year old, and 9.71% of savings for a 70 year old. The percentage of savings that can be withdrawn in a year increases gradually to 100% at age 89. As an illustration, a 50 year old with a LIF of $250,000 could withdraw about $15,500 in 2012. (The maximum withdrawals table is available on the Financial Services Commission of Ontario website: www.fsco.gov.on.ca.)

There are several issues to consider on the locked in funds:

- Am I comfortable investing funds? Even if you pay someone to manage your investments, you will have to monitor the investments and review the investor's fees – which can take a hefty portion of your savings.
- Investment returns are currently low for even the best investors. Safe, conservative investments will provide little enhancement to your retirement savings. As an older person (you are retiring), you do not have the time horizon to take long term investment risks. You have little time to make up for any losses.
- Even the best investors cannot predict the market swings. Can you withstand a "crash" like 2008 or the poor returns of 2011?
- Are the annual maximum withdrawals sufficient for my retirement income needs?

Still interested in the CV option?

Here are some things to ask when you talk to a financial institution about the CV:

- What interest rate will I need on my fund to provide a stream of monthly payments equivalent to my GM pension? Make sure that the agent knows exactly what your GM pension is: the life time basic, the special allowance, the supplement, the (generous) joint and survivor benefit. Take your pension statement with you to the meeting.
- What is the most tax efficient option for me? CV? Annuity? GM monthly pension?
- What is guaranteed and what is not?
- How do you make your money on my money? (Make sure you absolutely understand the answer.)
- What are your credentials?
- Can you give me two references, preferably people who opted for a CV.

A word on comparing "apples to apples"

The GM pension has some generous provisions to keep in mind if you are "buying" retirement income with your commuted value:

Joint and survivor benefit:

Under the GM plan, if you have a spouse, your lifetime pension is automatically reduced to 95%, and your spouse will receive 66 2/3% of your pension upon your death.[3] If your spouse predeceases you, you may cancel the survivor option and your lifetime pension will be restored to 100% (from 95%). The value of this benefit will be included in your CV calculation, but you are unlikely to purchase such a benefit at the same cost on the annuity market.

Special Allowance

Members retiring early with 30 years of service have a special allowance payable to age 65.

Supplementary Pension:

For members retiring at age 60 with 10 or more years of service or age 55 and 85 points, GM provides a supplementary monthly pension to age 65 based on $18 per year of service.

Early Retirement Pension:

Even if you are not eligible for the special allowance or supplementary pension, the reduction in the GM pension for early retirement may be less than what is charged on an annuity.

I have short life expectancy. Am I better off with the CV?

If you are terminally ill, you may be better to opt for the CV, particularly if you do not have a spouse. Your beneficiaries will be entitled to your retirement funds upon your death. With the GM monthly pension, there is an option for guaranteed payments of the basic pension (with a reduction) for up to 15 years.

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[3] The law requires the survivor option unless the spouse signs a waiver, in which case the retiree receives 100% of the pension, but there is no survivor benefit upon the death of the retiree. The 95% factor is increased if the spouse is more than 5 years older than the retiree and decreased if the spouse is more than 10 years younger.

If you have a spouse, you and your spouse should consider if the spouse is better off with the monthly survivor pension for the rest of their life or with the remaining funds in your retirement income fund.

If you are not terminally ill, be careful about predicting your life expectancy. You could pleasantly surprise yourself with a long life but have the unpleasant prospect of outliving your retirement funds.

What if GM goes bankrupt? Aren't I smart to take the CV now at 100%?

GM intends to pay the CV at 100%, subject to the regulator's approval.

At September 1, 2011, the GM pension plan is funded at 63% on a transfer ratio basis. GM is making contributions to fund the pension plan and if the plan were to wind up, GM would be required to bring the plan to 100% funding within 5 years.

Granted, if GMCL goes bankrupt and the US parent does not make up the fund shortfall, all plan members would be paid according to the funded status of the plan. In this "worst-case scenario," GM pension plan members are unlikely to receive their full pension entitlement.

However, GM has made a good recovery since 2009, is now a profitable corporation, and continues to meet its obligated payments to the pension plan. For members choosing the monthly lifetime pension, the risk of bankruptcy and an underfunded pension plan may be a concern. However, there are risks with the CV option: immediate loss in value on income taxes, market downturns, high fees paid to financial institutions, poor investment strategies, and the potential to outlive the funds.

Will the CV option affect the funded status of the GM pension plan?

When Ford offered the CV to the salaried staff, less than 10% of retirees took the option. Most people approaching retirement want the steady stream of monthly payments rather than the responsibility of investing their retirement funds. GM is not anticipating a significant draw on the CV option.

There are some regulatory checks in place to ensure that the CV option does not weaken the funded status of the pension plan:

* GM must have FSCO[4] approve the CV option. Because FSCO monitors the GM pension plan carefully, the regulator will not approve the CV option if they believe it will reduce the funding security.
* If the CV transfers reduce the pension funded transfer ratio by 10%, no additional transfer is allowed without the approval of the Superintendent of pensions. The current transfer ratio is 63%, so the transfer limit would be imposed if the transfer ratio of the GM pension fund were to reach 57%.
* GM must do annual actuarial valuations to determine the funded status of the pension plan. Any shortfalls occurring during the year, must be funded over the upcoming 5 years.

What about my retiree health care benefits?

Unifor members with GM who meet all eligibility requirements for retiree health care benefits under the asrTrust, will be covered if they take the monthly pension or the CV option. The asrTrust Board of Directors confirmed this position with the legal counsel for the asrTrust at their December 4, 2012 Board meeting.

Retirees currently make health care contributions to the asrTrust through deductions on their monthly GM pension. Retirees opting for the CV will have to arrange pre-payments to cover their health care contributions to the asrTrust.

For further information:

* GM Canada Benefits centre: www.gmclbenefits.com or 1-877-442-4625 (have your user ID and password ready)
* Unifor GM Pension Rep in the workplace: Robert Acker, 905-641-6443, 905-682-2611 extension 232

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[4] Financial Services Commission of Ontario (FSCO) regulates pension plans in Ontario.