

## **Making the best of **severance**: Ottawa experts tell Kristin Goff what to do when you lose your job.**

The Ottawa Citizen  
Sunday, August 26, 2001  
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Section: Money

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Source: The Ottawa Citizen

Along with the emotional issues that face people who have lost their jobs because of the technology meltdown or other economic woes, there are big financial questions they need to deal with.

"A job is normally the second largest asset that most people have. The first is a house," says John Read, a solicitor at Beament Green of Ottawa. "So there are some very substantial issues at stake."

Some of those may deal with whether the company's offer to a departing employee is fair and adequate. Others concern ways to reduce taxes on severance payouts or assess the best way to deal with accumulated pension benefits.

More immediately, of course, there's a need to find ways to manage when bills don't stop, but the paycheque does.

To help, the Citizen interviewed several Ottawa experts on aspects of dealing with severance packages, adjusting your finances to fit your circumstances and financial issues. Overwhelmingly, the advice most often stressed was not to rush into any decision before understanding the implications.

That attitude should begin the moment the company hands over their letter of termination and severance. Typically companies want employees to respond to their offered severance package within a week or 10 days.

But if you can't get all the answers you need by then, don't panic. Ask for an extension, says Mr. Read. The company is not likely to change the severance offer just because you don't meet their deadline.

"Take the time to review it carefully and consult with professionals -- a lawyer and tax adviser -- before doing anything. What's presented is extremely important," said Mr. Read. "They should not feel rushed to sign."

Even if the company's offer is a fair one -- other potential pitfalls could occur in how the severance pay is transferred to the person and what he or she decides to do with it.

For example, an acquaintance of mine who was laid off several years ago ended up with an unexpected tax bill of several thousands of dollars because she decided to use her lump sum severance to pay down her mortgage.

It seemed like a good idea at the time. But it backfired because the severance amount (which we'll say was \$40,000 for this example) was added to her other income and taxed at the highest marginal rate.

There was tax withheld on the severance amount. But it wasn't enough then and it wouldn't be enough today. The maximum amount of tax withheld on severance is 30 per cent. But the top marginal tax rate in Ontario is about 46 per cent.

As a result of that 16-percentage-point difference in tax withholding rates, an additional \$6,400 in taxes would be owed in April, based on the \$40,000 severance amount in this example.

"This is one of the biggest pitfalls for people who get laid off, because what's withheld (by employers) at source, is not necessarily what you are paying in taxes at the end of the year," says **Marc Lamontagne**, a financial planner with Ryan, Lamontagne and Associates in Ottawa.

The amount of tax withheld on severance payouts (which doesn't include employment pay for accumulated holidays or leave days) are set by Canada Customs and Revenue Agency (formerly Revenue Canada) at a fixed schedule. In Ontario, they are: 10 per cent for severance payments of \$5,000; 20 per cent for amount above that up to \$15,000; and 30 per cent on severance payments above \$15,000.

Individuals also need to take a hard look at their personal budget and prepare to live on less.

Running up credit card bills to maintain your previous lifestyle is the road to disaster if you don't know how long it will be before your next job, or whether you'll earn as much as you had, says Stanley Kershman, a bankruptcy and insolvency solicitor at Kershman & Kerr.

Especially when you may be feeling vulnerable and uncertain, there are a lot of issues to deal with.

Here's a look at some of them along with suggestions based on information from Mr. Read, a solicitor with a background in labour law, Mr. Lamontagne, a financial adviser, and Mr. Kershman, a bankruptcy and insolvency solicitor.

## Be Prepared

If you suspect there may be layoffs coming at your company, do a few things to prepare

yourself. Build up an emergency nest egg (ideally that's three to six months' worth of expenses), try to pay down debts and take a hard look at your budget to see where expenses could be cut.

If you don't have a personal line of credit, think about getting one for emergency use before you lose your job. Interest rates on lines of credit are far cheaper than credit cards. Banks aren't likely to approve an application for a credit line if you aren't employed.

### When It Happens

If your job is cut, don't sign your letter of termination until you've reviewed it carefully. Workers are generally entitled to a certain notice, or pay in lieu of that notice, when they are let go, under Ontario's employment standards act, except when they are fired for cause. The minimum amount of termination pay is determined by a variety of factors, including your length of service and the size of the company. Questions about minimum standards can be addressed to the Ontario Ministry of Labour (1-800-531-5551). Information on the ministry's Web site, [www.gov.on.ca/lab/main.htm](http://www.gov.on.ca/lab/main.htm), also explains the rules.

Many companies offer more generous severance benefits than those required by provincial law. But employees don't necessarily have to accept their offer. Workers whose jobs have been eliminated may feel they have no clout to negotiate a better deal. They need to remember that the employer generally wants to close the files on jobs cut as quickly as possible. Since it costs them money to keep files active, it is in the company's interest to try to resolve the matter when issues are raised, says Mr. Read.

Fees for a lawyer's assistance in reviewing a package would likely be considered tax deductible. Claims which aren't settled through negotiation generally land in court-mandated mediation within a year. It is rarely the case that severance disputes drag on for years, Mr. Read said.

### What'S Fair?

It may help to recall the terms and conditions under which you started employment with the firm to assess if the severance package offer is fair. Did you leave a stable and secure position elsewhere to join the company? Did you move from far away? If you are likely to face moving costs again, are those costs compensated?

If you have been out of the job market for some time, or if you are an older worker, does the offer include enough job search counselling and re-employment assistance?

### Other Parts of the Deal

In addition to looking at the notice period, or cash offered in lieu of notice, find out what

vacation or leave days you are entitled to, what decisions need to be made about benefits including your pension, stock options, insurance, etc.

## Making Choices

Individual circumstances and differences among severance packages make generalizations on choices impossible. But Mr. Lamontagne points out some options to consider and a few things to watch out for.

- Accumulated time. If you are offered the option of taking vacation and leave days as a lump sum or continuing on the payroll for time owed, weigh your need for up-front cash against the prospect of continuing to receive company benefits and build up credit towards your pension for a longer period of time.
- Stock options. Check out the rules for exercising stock options if you have some. Once people leave a company, they usually are allowed only a limited time, say 30 days, in which to exercise their stock options.
- Life insurance. Companies may let former employees convert from their group plan to an individual plan, without having to provide much new medical information. But it is often cheaper to buy a new individual policy or get a group rate through a professional or interest group, such as an auto club, says Mr. Lamontagne.
- Pensions. Few technology employees who have joined companies in recent years have defined-benefit pension plans, but older employees at Nortel and elsewhere may. Leaving the pension with the company, rather than transferring the equivalent value to a locked-in RRSP, offers less investment risk and should be looked at carefully, especially by those aged 50 or more, says Mr. Lamontagne.

## Dealing With Taxes

Because you may get income from a host of different sources in the year you lose a job, dealing with taxes becomes a much bigger deal than when a single employer withholds tax amounts from pay for the year. An individual may receive income from employment, before he or she was laid off, additional pay for owed vacation and leave days, a lump sum severance payment, perhaps employment insurance benefits and pay from a second job later in the year. Because that could add up to a large amount of income in one year, the tax hit could be large. Adding insult to injury, in many cases there won't be enough tax withheld at source to meet the tax due next April on this year's income.

If you can afford to do so and have not contributed the maximum each year to your Registered Retirement Savings Plan, one way to lower your taxable income is by making a large contribution to your RRSP.

If you can get your employer to contribute to your RRSP directly, rather than handing the cash to you first, no taxes need to be withheld on that amount. Companies may require a letter from your district tax office to confirm the amount of contribution room in your RRSP, before they will do this.

A second RRSP option is open only to employees who worked for the company in 1995 and earlier. It is a special retiring allowance "rollover" that was phased out in recent years. Qualified employees may be able to rollover \$2,000 of severance pay into an RRSP for each year or partial year they worked for the company in 1995 and certain previous years. Your employer should be able to explain your eligibility. The one-time "rollover" allowance doesn't affect normal RRSP contribution rules.

### Employment Insurance

Individuals who lose their jobs should apply for employment insurance within four weeks of their termination or layoff.

If you wait longer, the program administrators may calculate the amount of employment insurance you qualify for based on \$0 earning for that period, which will reduce the EI you qualify for, says Mr. Lamontagne. The formula takes into account your salary and severance benefits, in determining how much and when benefits may be paid.

Another red flag issue for those who have collected EI benefits in the past 10 years: the clawback rule. If your total income (including a severance settlement) exceeds \$48,750 this year, you will have to pay back some or all of your EI benefits next year under the clawback formula. People who haven't collected EI in the past 10 years are exempt from the clawback.

### Living On Less

Cutting non-essential expenses and following a budget will help you adjust to living without the paycheque you received in the past.

But if you reach a point where bills can't be paid, be proactive, says Mr. Kershman. Check out options on your major loans.

Some banks let you skip one or two mortgage or car payments, if you wish, especially if you have paid faster than required.

The Bank of Montreal, and perhaps others, lets you withdraw cash from your mortgage if it exceeds what you were required to pay. (Typically people who pay weekly or biweekly will have done so.) You might also ease a cash crunch by increasing the amortization period on your mortgage up to 25 years, if it is now significantly shorter.

If you are still in danger of falling behind on bill payments, let your creditors know you

have been laid off and can't make full payments. It may potentially affect your credit rating, says Mr. Kershman. But more damage will be done if you stop paying your bills and leave your creditors wondering why.

He recommends you send a letter by registered mail, including a photocopy of your statement and account number, and ask for the appropriate person to contact you to discuss the situation. That way, you avoid the problem of dealing with different people at call centres.

Idnumber: 200108260004

Edition: Final

Story Type: Business

Illustration Type: Colour Photo

Illustration: Colour Photo: Wayne Hiebert, The Ottawa Citizen / Financial planner Mark Lamontagne points out that there are potential pitfalls in how severance pay is transferred and how the recipient handles it afterwards.

Length: 2075 words