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DID YOU KNOW?

(A publication for the clients and contacts of Gary S. Aslett, Chartered Accountant)

YOUR RR$P – 10 PLANNING TIP$

As the RRSP deadline quickly approaches (Friday, March 1, 2002 to get a tax deduction for your 2001 tax year), listed below are 10 RRSP planning tips.

1. If funds are limited, which spouse should contribute? Cash flow demands may not allow both spouses to contribute their maximum amounts. Therefore, the spouse in the higher tax bracket should contribute to generate the largest tax savings. For example, the RRSP deduction for a taxpayer in the top tax bracket is worth 46% (Ontario rates) but only 22% for a taxpayer in the lowest tax bracket.

2. Spousal RRSP: Now that you know which spouse should contribute, you must decide to whose plan the funds will be deposited. For example, assume Mr. A will make an RRSP contribution; he can contribute to his own RRSP and/or his spouse's RRSP. Mr. A will still take the tax deduction on his personal return even if he contributes to his spouse's RRSP as long as the RRSP slip indicates that Mr. A is the 'contributor'.

   Generally, both spouses would want to accumulate approximately the same amount of retirement assets such that during retirement, their incomes will be similar and prevent one taxpayer from being in a high tax bracket and the other spouse in a low tax bracket. Consideration must be given to any other potential sources of income during retirement such as company pension plans.

   Note that the spouse must wait until the third year after a contribution is made to a spousal plan before making a withdrawal or the income will be taxed in the hands of the contributor and not the spouse.

3. Over-contributions: $13,500 is the maximum RRSP contribution limit earned each year based on earned income of $75,000 x 18%. A taxpayer (other than a minor) can over-contribute a maximum of $2,000 to an RRSP (without penalties) with the income earned sheltered from tax. The $2,000 over-contribution limit is not an annual amount but rather, the maximum amount that you can be over your allowable limit at any point in time. In a later year, you will contribute $2,000 less than your RRSP limit and will then deduct the over contribution paid earlier.

4. File a tax return for minors: Although your children may not have sufficient taxable income to use a tax deduction for RRSP contributions, this does not prevent them from contributing to an RRSP and deducting the contribution in a later year. However, in order to contribute, the child must have ‘earned income’ (for example, employment or self-employment income) AND, the child must have filed a tax return. Filing the tax return allows Canada Customs & Revenue Agency to calculate RRSP room for your child. Therefore, if your child has earned wages or other eligible income, consider filing a quick tax return for the child to start accumulating RRSP room.

5. Contribute monthly: Many taxpayers will wait until March 1, 2002 to make their 2001 RRSP contribution. This can cause a strain on cash flow and the taxpayer will have missed the advantages of buying investments at varying times during the year. Consider setting up a monthly contribution plan where the funds will be withdrawn directly from your bank account and deposited in to your RRSP monthly. If you are part of a company group RRSP plan and contributions are paid directly from your employer to your RRSP, your employer is not required to withhold income tax on the amount transferred directly to your RRSP (and of course, there would be no refund at the end of the year).

6. Naming beneficiaries: Probate fees are often assessed at the time of a taxpayer’s death, which is essentially a provincial fee charged for authorizing an executor to proceed with following the terms of the approved Will of the deceased. RRSP assets can be excluded from the assets subject to the probate fee by simply naming a specific beneficiary in the RRSP plan documents. Simply naming your ‘estate’ as the beneficiary would not be sufficient.

7. Catch up on unused contribution room: During the early part of our careers and given the other demands on our cash resources (mortgages, education funding, purchase of a car), you may have not maximized your contributions to your RRSP. Refer to your 2000 Notice of Assessment to find your available RRSP contribution room for 2001. This will include RRSP room generated from the income you earned in 2000 plus any unused room from prior years. Any RRSP room not used is carried forward indefinitely.

   Many financial institutions offer loans at their prime rate. After applying your tax refund resulting from the RRSP contribution, your may find that your monthly loan repayments are manageable while at the same time you have your RRSP working for you.

8. Do you really want to deduct your RRSP contributions this year? If your taxable income fluctuates such that your 2001 tax bracket is lower than your 2002 tax bracket, you may want to defer the tax deduction for your RRSP contribution until a later year. As discussed above, a $1,000 deduction is worth $460 if you are in the top tax bracket and $220 if you are in the low bracket. [Note that you will still contribute to your RRSP earning tax-deferred income. You are just delaying the deduction on your tax return and will carry forward the contribution to 2002.]

9. Using your RRSP to purchase a home or to pay for education. A maximum of $20,000 can be withdrawn from your RRSP to purchase a home if you have not owned a home in the preceding five years. The amount must be repaid to your RRSP in equal amounts over a maximum of 15 years (although earlier repayment is allowed). Amounts not repaid as required are included in

taxable income. RRSP contributions must be made at least 90 days prior to any withdrawal for the contribution to be allowed as a deduction.

Similarly, up to $10,000 per year to a maximum cumulative amount of $20,000 can be withdrawn to finance certain education programs. Amounts must be repaid over a ten-year period.

10. <u>Base your RRIF payments on your spouse's age if your spouse is younger</u>. Your RRSP must be closed by December 31 of the year in which you turn 69 years of age. You may decide to transfer your RRSP to a Registered Retirement Income Fund ("RRIF") or purchase an annuity. If you plan to contribute to your RRSP for the year in which you are 69, your deadline is December 31 and not March 1 of the following year. The minimum amount that must be withdrawn from your RRIF is based on your age. However, you can reduce the minimum withdrawal amount and therefore, maximize your deferral by using your spouse's age in the formula (assuming your spouse is younger).

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