Articles Program

RRSP Checklist

- The RRSP deadline is March 1, 2011.
- To qualify as a 2010 deduction, contributions to your personal or spousal RRSP must be made on or before March 1, 2011.
- Determine your RRSP contribution limit for 2010 by referring to your previous year's *Notice of Assessment* from the Canada Revenue Agency (CRA), or visit the CRA website at www.cra-arc.gc.ca.
- Determine how much, if any, you have already contributed to your RRSP for 2010.
- You can take advantage of any unused 2010 RRSP room up to your contribution limit. You will receive a 2010 tax deduction for this amount as long as the contribution is made by the March 1, 2011 deadline.

RRSP Tip 1 of 10
An RRSP can finance your home and more
“If you plan to take advantage of the RRSP Home Buyers’ Plan, there are some important details to consider,” says Chartered Accountant Glenn Lott, Partner at Lott & Company, Chartered Accountants in Markham.

“When buying your first home you can withdraw up to $25,000 from your RRSP. But you’ll need to have the $25,000 in your RRSP at least 90 days before making that withdrawal. So, be sure to make any additional contributions to your RRSP prior to making your Home Buyers’ Plan withdrawal.

“Consider skipping a repayment of the Home Buyers’ Plan withdrawals if you have a low income year (for example, you’re on maternity leave or collecting employment insurance). If the required Home Buyers’ Plan repayment is not made, the amount of the required repayment must be included as part of your income in that year.

“This additional income will be subject to a low tax rate or possibly no tax at all if your total income is below the taxable threshold. The cash designated for the Home Buyers Plan repayment can be saved and contributed to your RRSP in a year when you are in a higher tax bracket, resulting in a tax saving,” advises Lott.

“Alternatively, if your spouse is in a higher tax bracket in the year that the repayment is skipped, have your spouse use this money to make an additional RRSP contribution. The amount could be set aside as a deductible contribution as long as there is available contribution room. The tax savings on the spouse’s contribution will exceed the income tax paid on the Home Buyers’ Plan income.”

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RRSP Tip 2 of 10
Early retirement and my RRSP
Thinking of early retirement? How and when can you start using your RRSP?

“While there are no restrictions on accessing your RRSP account at any time, all withdrawals are immediately taxable,” advises Chartered Accountant Robin Cyna, Senior Manager, Tax Services, Grant Thornton LLP.

“Make sure you determine the best timing and method to access your RRSP accounts.”

As you will need your registered and non-registered savings to support you for the remainder of your retirement, you must weigh the cost of drawing on your RRSP resources early and losing the accumulation of tax-deferred earnings. To minimize this cost, it may be prudent to use non-registered assets first, resorting to your RRSP only when necessary. Alternatively, you might also consider using a Tax Free Savings Account, or choose a withdrawal method that only draws on a portion of the RRSP per-year and keeps the remainder in a tax-deferred status.

“Another issue is the method of withdrawing the funds,” says Cyna. “At any point you may either choose to take your RRSP funds as a cash payment, transfer the funds into a Registered Retirement Income Fund, or purchase an annuity. Each method has its own benefits and restrictions, but regardless of the method chosen, the funds will be included as part of your taxable income in the year they are withdrawn.”

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RRSP Tip 3 of 10
The strategy behind a spousal RRSP
Are you the highest wage earner in your family? Do you expect to generate the bulk of your family's retirement income? If so, then a spousal RRSP can be an excellent strategy as it helps provide more equal retirement income and tax savings, according to Chartered Accountant & Portfolio Manager Loren Francis of Barometer Capital Management in Toronto.

"Even though the new pension-splitting rules may allow a split of income from a single RRSP, a spousal RRSP can be beneficial when there is an age gap between spouses, and/or for estate-planning purposes.

"Different tax rates apply to couples versus individuals. The result is that a couple receiving two smaller incomes at retirement will be taxed at a lower rate than one individual claiming the total household income. When you contribute to a spousal RRSP, you will also get an immediate tax deduction – just remember that the contributions are owned and controlled by your spouse.

"If you are a married couple or living in a common law relationship, and have earned income or unused RRSP deduction room, you can also contribute to a spousal RRSP until December 31 of the year that your spouse or partner turns 71," Francis advises.

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RRSP Tip 4 of 10
RRSP loans — don't borrow what you can't repay
The money we invest in our RRSP is supposed to help supplement our income in retirement. But for many in their prime earning years, the tax deferrals those RRSP contributions bring are just as important. Do those tax savings justify borrowing money to put into an RRSP?

"Under certain circumstances, borrowing for an RRSP can make sense," says Chartered Accountant Hazen Henderson in Whitby. "In a year when your income is unusually high, the loan will enable you to contribute to your plan at the higher rate of tax." But interest on the loan is not tax-deductible, and you could end up repaying more to the bank than you actually make on the RRSP investment.

"For some, it's a 'forced-savings strategy'," Henderson says. "They can't seem to save the money, but they accept having to repay the loan."

The best outcome, he says, is when the tax refund is used to pay down a significant portion of the loan. "But far better is to set up an automatic deduction that moves the money from your bank account straight into your RRSP each week or month, before you have time to spend it."

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RRSP Tip 5 of 10
RRSP vs. Tax Free Savings Account
It’s been three years since the Tax Free Savings Account was introduced to Canadians. Is it still a viable alternative to an RRSP?

“It all depends on your income tax rate at the time when contributions are made, as compared to the rate during the withdrawal phase,” explains Chartered Accountant Ken Lancaster, Tax Partner with MacGillivray Hamilton.

“If the two rates are identical, then the TFSA is a preferred option because it is more flexible and withdrawals do not affect income-tested benefits.

“Many individuals fall into the category where their income tax rates in the accumulation phase are higher. That’s because they are in their peak earning years and are paying high income tax rates. Presumably, when they retire, they will be paying much lower income taxes. Since their contribution income tax rate is much higher than the withdrawal income tax rate, an RRSP contribution is probably the preferred option for this category of individuals,” says Lancaster.

“For the few Canadians who pay a higher rate in their withdrawal years than in their contribution years, a TFSA is probably the better choice.”

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RRSP Tip 6 of 10
Smaller house — bigger RRSP?
If you’re selling the family home to move to a less expensive one, consider all the options before you stash the extra cash in your RRSP.

“Money from the sale of a principal residence is tax-free,” says Sidney Laufer, a Chartered Accountant in Vaughan. “But that’s where the commonality ends. Everyone must examine his or her particular circumstances and decide how to use the proceeds in a way that’s best for them.

“If you’re purchasing a less expensive residence, any excess funds can be applied to an individual or spousal RRSP until the maximum contribution level is reached,” Laufer explains.

To help reduce any extra income tax that you may have to pay when the RRSP funds are eventually withdrawn, Laufer suggests the following as one possible strategy: At age 65, each spouse can transfer approximately $10,000 from the RRSP to a Registered Retirement Income Fund (RRIF). Then, each partner can withdraw $2,000 from the RRIF each year until age 71. At that point the remaining RRSP funds can be moved to the RRIF, assuming both people will receive only Old Age and Canada pensions, and nothing from past employers.

If you’re planning to rent rather than buy another home, Laufer suggests you prepare a new financial budget that matches your new living arrangements. And, regardless of your situation, consult a Chartered Accountant first to be sure that you understand all the options and implications before purchasing any investments – RRSPs or otherwise.

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RRSP Tip 7 of 10
Mortgage payments vs. saving for retirement
Should you focus on paying down your mortgage or contributing to an RRSP?

"Mathematically, you can calculate which alternative is better, given assumptions about mortgage rates and the rate of return in your RRSP. Most analysts conclude that it is better to pay off your mortgage first, assuming that the rate of return of the investment in your RRSP does not exceed your mortgage rate," says Chartered Accountant Ann M. Donohue, a Partner with Campbell Lawless Professional Corporation in Toronto.

"There are many factors that you should also consider. Will you be able to catch up on your RRSP contributions once you've paid off your mortgage? Will you need the funds in your RRSP for emergencies? Do you want to diversify your investments rather than place all of your available cash in your home?

"Keep in mind that having the discipline to save money, either by paying down your mortgage or putting money in your RRSP, will mean that you will increase your net worth in the long run. Both paying off your mortgage and saving for retirement are important components of any good financial plan," advises Donohue.

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RRSP Tip 8 of 10
How RRSP contribution room is calculated
How does the government calculate the amount that you are allowed to contribute to your RRSP?

"The Canada Revenue Agency (CRA) calculates your contribution limit for the upcoming year and highlights it in a box on the *Notice of Assessment* that you receive in the mail after you file your income tax return for the current year. You can also find your RRSP room for 2010 by way of the *My Account* service or the *Quick Access Service* on the CRA website at www.cra-arc.gc.ca.

"You are entitled to contribute this amount to your RRSP without penalty, generally starting on January 1 of the tax year in question. Once you make a contribution to your RRSP, you can deduct it on your tax return in the current year or any future year," says Chartered Accountant Camillo Lento, a lecturer at Lakehead University in Thunder Bay.

Any contribution made before March 1, 2011 can be deducted on your 2010 tax return providing you have contribution room for 2010.

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RRSP Tip 9 of 10
Save for a house or invest in an RRSP
It's a big question, and the right answer depends on your goals and circumstances.

"If you have funds in an RRSP and you're looking to buy a house, you must weigh the benefits of a smaller mortgage and less interest against the loss of tax-free compounding earnings in an RRSP," says Chartered Accountant Jennifer Wheeler, Tax Manager for KPMG Kingston.

"With the Home Buyer's Plan, anyone who hasn't owned a home in the last five years can use money in their RRSP to purchase or build a home," Wheeler explains. "For couples, each partner who qualifies for the plan can withdraw up to $25,000. That's as much as $50,000 toward the purchase of an existing home, or one that you build.

"The money must be repaid to your RRSP over the course of 15 years, beginning the second year after it's withdrawn," she says. At least 1/15th of the total amount borrowed must be repaid each year, or the shortfall will be added to your income and be subject to tax.

"The money used must have been contributed to your RRSP at least 90 days prior to being withdrawn from the Home Buyer's Plan, or you won't be eligible to deduct it on your tax return," Wheeler cautions. "And, finally, for both partners to qualify for the plan, the property must be purchased jointly in both names."

It should be noted that the Home Buyer's Plan is subject to a number of intricate rules, and individuals should ensure they have all of the appropriate information prior to making a decision.

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RRSP 10 of 10
RRSP can help relatives with disabilities
For some time, there have been provisions to permit the tax-free rollover of a deceased person's RRSP to that of a spouse, child or grandchild who, due to disability, was financially dependent on the deceased person.

"But this year, the 2010 Federal Budget has extended these provisions, giving more help to those who care for relatives with disabilities," says Chartered Accountant John R. Mott of Toronto. "Now the RRSP rollovers can also be made to the Registered Disability Savings Plan (RDSP) of a child or grandchild who is financially dependent on the taxpayer due to mental or physical infirmity."

The amount rolled cannot exceed the beneficiary's RDSP contribution room, which currently has a lifetime maximum of $200,000. Rolled amounts won't be eligible for Canada Disability Savings Grants, and **will** be taxable in the beneficiary's hands when withdrawn, just like RRSP funds.

"This rollover treatment applies to the RRSPs of people who passed away after March 3, 2010," explains Mott. "Prior to this and for deaths since 2007, there were other ways to transfer RRSP funds to children or grandchildren with disabilities. In many cases, these provisions can still apply and can be claimed, providing taxpayers make the appropriate election before 2012."

Taxpayers wishing to take advantage of these provisions should review their wills and make the appropriate amendments, if needed.

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