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 8
Sometimes, it just doesn't pay you to work
If you've been conscientious about investing in RRSPs, there can be a point at which it doesn't make sense to keep drawing a paycheque.

"RRSPs should do more than simply allow us to defer taxes," says David Aiken, a Chartered Accountant in Toronto. "The idea is to make the contributions when your marginal tax rate is higher than it will be when you withdraw them. As well, an adequately funded and properly managed RRSP will allow retirees to continue on with a secure, carefree lifestyle.

"For example, while you're actively working, your marginal tax rate may be as much as 45 per cent or more in Ontario. If you cash out your RRSPs at age 71 when you're retired and your marginal tax rate is much lower, there's a substantial saving," Aiken explains. "An added bonus is that while your money is invested in the plan, neither the principal nor the earnings it generates are taxed.

"But if you're still working full-time past age 65, you could continue to be taxed at that higher rate, or an even higher one. Then, your income may increase because you will begin collecting Canada Pension and Old Age Security. Furthermore, if your income level is too high, Old Age Security benefits will be subject to clawback.

"By age 71, all your RRSPs must be converted to a Registered Retirement Income Fund (RRIF)," Aiken continues. "Those funds must then be withdrawn as taxable income at a gradual rate that increases with age. But if you're still getting a salary, your RRIF income could be taxed at a rate that's even higher than when you invested in the RRSP in the first place."

Factor in the expenses of working – the cost of commuting, clothes and lunches out – and that pay cheque may not be providing as much added income as you hoped.

So if you're blessed with the good health, joie-de-vivre and the desire to keep active after your 65th birthday, consider that golf, volunteer work and/or time with the grandchildren might be just as rewarding and easier on your bank account.

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RRSP Tip 2 of 8
Build RRSP room — file returns for the kids
Many kids earn income with part-time jobs and even babysitting. But because it's usually below the basic exemption level, parents typically don't bother filing tax returns for them to report it. While the amount of money involved may be small, the real loss is the RRSP contribution room that can never be made up.

Chartered Accountant Carmelo Linardi, of Carmelo Linardi Professional Corporation in Aurora, says this RRSP room could be significant, given the potential increased exemption thresholds and depending on the number of years the child's income is below the threshold.

"Imagine a child who earns $5,000 per year doing summer work for a period of six years. That's not just $30,000 of tax-free income; it's $5,400 of lost RRSP room. When that child becomes an adult wage earner and can make RRSP contributions to shelter tax at the top personal marginal rates, the savings could be as much as $2,500. That makes it well worth the trouble of preparing tax returns for six years.

"In addition, for children who reach the required age, certain credits — for example the GST credit and Ontario Sales Tax credit — are only available if a tax return is filed."

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RRSP Tip 3 of 8
What belongs in an RRSP?
Say "Registered Retirement Savings Plan" and most of us think mutual funds, guaranteed investment certificates and savings accounts. Turns out, lots of other financial products and investments are RRSP-eligible, too.

"There are a variety of other investments that qualify," says Chartered Accountant Alexandra Spinner, Senior Tax Manager at Soberman LLP in Toronto. "Some include shares of public corporations listed on prescribed exchanges in and out of Canada. Some bonds, mortgages – and, within limits, even shares of certain private corporations – are also eligible. There are many exceptions, however, so it's important that anyone considering these kinds of investments consult with a competent, knowledgeable advisor."

Remember that investments purchased inside your RRSP can lose value just as easily as they can outside the plan. Don't take chances with your financial security. If you're not sure what strategy is best for you and your situation, consult a Chartered Accountant in your community for advice about financial planning, taxes and RRSPs.

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RRSP Tip 4 of 8
Borrow to save for retirement
Is obtaining a loan to purchase an RRSP a good idea?

"An RRSP loan can be advantageous if you have accumulated a significant amount of unused RRSP room because it allows you to maximize your contribution," says Chartered Accountant Tina A. Di Vito, Director of Retirement Strategies, BMO Financial Group in Toronto.

"For example, say you have unused room of $18,500 and your marginal tax rate is 46 per cent – if you can come up with $10,000 yourself and borrow $8,500, for a total contribution of $18,500, the RRSP contribution will generate a tax refund of $8,500 – just enough for you to pay off the entire loan."

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RRSP Tip 5 of 8
Don't forget RRSP if working abroad
If you're a Canadian expat or someone who commutes to work in the United States, you can still contribute a portion of your earnings to an RRSP.

"Many countries, including the United States, tax people on their citizenship. But in Canada, we're taxed based on residency," explains Walter Benzinger, a Chartered Accountant with Deloitte & Touche LLP in Windsor.

Residency is question of fact, Benzinger says, and the Canada Revenue Agency will consider things like the location of your home, your family members and your bank accounts in determining whether you are, in fact, a Canadian resident who is eligible to contribute to RRSPs and reap the associated tax savings.

“Commuters who live in Canada but cross the border to work in the U.S. must pay American federal, state and local taxes,” Benzinger continues. “You’ll receive a W2 form that states your earnings, and you must file a non-resident tax return called a 1040NR. You’ll need to file a Canadian T1 return as well, but don’t worry. There’s no double-taxing. Canada gives you full credit for any foreign taxes you pay, including things like the U.S. Federal Insurance Contribution Tax (FICA), Social Security and Medicare.

Any RRSP contributions you make can be used to offset any taxes still owed in Canada, but Ontario residents must still pay the Ontario Health Premium, which is calculated at a graduated rate on income over $20,000. The Ontario Health Premium payable on incomes from $48,500 to $72,000 is $600.

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RRSP Tip 6 of 8

Rules for RRSPs that lose value after death

Death and taxes are supposed to be two sure things. But when we defer taxes by investing in an RRSP, what happens if we die before age 71 with money still in the fund?

“Usually, RRSPs have a named beneficiary who inherits the contents of the plan in the event the owner dies,” says Jennifer Wheeler, a Chartered Accountant and Tax Manager with KPMG Kingston.

“On death, the holder of the plan is taxed on the entire amount, unless it’s left to a spouse or a financially dependent child or grandchild,” Wheeler explains. ”The RRSP can be transferred tax-free to a spouse’s RRSP, but if it’s left to a financially dependent child or grandchild, then the value of the RRSP is taxed in the hands of that child or grandchild, and the tax can often be delayed for many years.

“If the beneficiary is not a spouse or dependent child, there is no tax-free rollover and the funds are included in the deceased annuitant's income for the year of death. Any changes in the value of the fund that occur between the date of death and the time the funds are distributed must be included in the income of the beneficiary who is receiving the RRSP funds.”

Historically, Wheeler says no consideration was given to RRSPs that declined in value during the time the deceased’s estate was being settled.

“In the 2009 Federal Budget, a new relieving rule was introduced,” she continues. “If the value of the plan decreases between the time the RRSP holder dies and the fund’s contents are distributed to beneficiaries, the deceased taxpayer may be eligible to claim a deduction on their final income tax return. That difference can reduce the tax burden, leaving more money in the estate for beneficiaries.

“This rule generally applies to RRSPs that were wound up after 2008. However,” Wheeler cautions, “To claim the loss, the funds must have been distributed to beneficiaries, and the RRSP, which cannot hold any non-qualifying investments, must be wound up by December 31 following the year of death.”

If you think these rules may apply to your situation, be sure to review all of the facts with your tax advisor.

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RRSP Tip 7 of 8
The cost of withdrawal from your RRSP
If you withdraw money from your RRSP, here's how it will affect you financially.

"If the withdrawal is $5,000 or less, you'll be subject to tax of 10 per cent withheld at source; 20 per cent if the withdrawal is greater than $5,000 and less than or equal to $15,000; and 30 per cent for amounts greater than $15,000," says Chartered Accountant Gary H. Kopstick, Senior Tax Partner, Soberman LLP in Toronto.

He suggests that you consider several smaller withdrawals rather than one large lump-sum payment to reduce the tax withheld at the time of the withdrawal. "The reduction is only a tax deferral, as the withdrawn amounts must be reported on your tax return where they will be subject to your regular tax rate."

Keep in mind that in situations where a taxpayer makes a single request to withdraw an amount in instalments, the withholding tax would be based on the total amount to be withdrawn.

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RRSP Tip 8 of 8
"In-Kind" withdrawal for seniors – no charge
Are you a senior who is faced with the unhappy prospect of withdrawing from your Registered Retirement Income Fund (RRIF), even if it's declined in value?

"Seniors can take advantage of what's called an in-kind withdrawal," explains Chartered Accountant John Mott in Toronto. "An in-kind withdrawal allows you to transfer stocks, mutual funds or other assets from a RRIF to a non-registered account at no cost. Just like a cash withdrawal, you will pay tax on the securities being transferred, but there is no sale involved and no extra charge."

The beauty of this strategy, Mott says, is that it allows seniors to satisfy their minimum-withdrawal obligations without having to liquidate securities that may still increase in value, or even recover some of the value they lost – not an uncommon scenario given the downswing in the markets a couple of years ago.

But be aware, Mott cautions that withdrawals in excess of the minimum amount are subject to lump-sum withholding tax rates.

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