Deferred Income Plans

Non-Deductible Contribution Types

Types

Registered Education Savings Plans (RESPs)

Registered Disability Savings Plans (RDSPs)

Tax Free Savings Accounts (TFSAs)

Benefits

Growth of Investment Earnings Tax Free

Tax Reduction – RESP/RDSP - Use of a low income individual’s tax brackets

Tax Avoidance – TFSA Only – No tax on income earned within the account.

Structure

Time

Non-Deductible Contributions

Investment Account
Contributions & Income Grow Tax Free

TFSAs
Contributions & Earnings paid out tax free

RESPs & RDSPs
Contributions paid out tax free
Earnings taxable to recipient

RESPs

Registered Education Savings Plans

Image obtained November 1, 2013 from:
http://www.yummymummyclub.ca/life/money/your-resp-rulebook

Registered Education Savings Plans (RESPs) - Overview

- Intended to assist in saving for the education of a beneficiary (generally a child or grandchild)

- Contributions are made by the adult relative.

- Taxable withdrawals are taxed to the beneficiary (the child) if the beneficiary is in post-secondary study at the time of withdrawal.

- Otherwise taxable to the contributor.

Registered Education Savings Plans (RESPs) - CESGs

- CESGs – Canada Education Savings Grants
- 20% government grant deposited to the RESP
- Maximum of $500 per year on contributions of $2,500.
- If beneficiary not in post-secondary study when RESP withdrawn, the CESG and income on it is removed from RESP account.
- Can catch up if did not contribute or open a plan – max of $1,000 in any one year.

Registered Education Savings Plans (RESPs) – CESGs +

- For low income families, extra grant (on top of ordinary 20%) is available.

- On first $500
  - 20% if family income is $43,953 or less
  - 10% if family income is between 43,953 and 87,907
  - 0% if family income is greater than 87,907

Registered Education Savings Plans (RESPs) - CLBs

- CLB – Canada Learning Bond
- Government contributions to the RESP. $525 in the first year, $100 in each subsequent year.
- Not based on contributions made by others
- Made to a beneficiary's RESP when the family qualifies for the National Child Benefit supplement.
- Stops when the child turns 15, family income must be below $25,356.

Registered Education Savings Plans (RESPs) - Restrictions

- Tax free growth of earnings is limited to 35 years (40 years if beneficiary has a disability)

- Total contributions are limited to $50,000 for any one beneficiary

- Penalty of 1% per month on the excess over $50,000.

- Lifetime maximum CESG of $7,200.

Registered Education Savings Plans (RESPs) - Withdrawals

- Contributions can be withdrawn at any time by beneficiary or contributor unless restricted by the plan itself (the bank's terms)

- Education Assistance Payments
  - Paid from accumulated earnings, CESG amounts and CLB amounts.
  - Included in the income of the recipient if recipient qualifies due to enrollment in post-secondary education.

Registered Education Savings Plans (RESPs) - Withdrawals

- Accumulated Income to Subscribers
  - Paid after beneficiaries turn 21 & not eligible for EAP
  - CESG and CLB Repaid to the government
  - Extra 20% tax on remaining income to compensate for tax deferred growth

- Limits
  - Full time students can withdraw $5,000 in the first term, unlimited thereafter.
  - Part time students have lower limits.

Registered Education Savings Plans (RESPs) - Plans

- Single beneficiary plans – limits as we described
- Family plans – beneficiaries can be any child of the contributor.
  - Attractive if several children and not all pursue education.
  - Same contribution limits per beneficiary.
  - No restriction on which beneficiary can withdraw funds.

Practice Example A – 1 (Exam realistic)

Jeremy and his wife, Diane, have a 2 year old daughter. They make a $3,000 contribution to her RESP each year.

Calculate the amount of basic savings grants the government will contribute to the RESP.

Annual max is 20% x $2,500 = **CESG of $500 = amount contributed**

Practice Example A - Expanded

Jeremy and his wife, Diane, have a 2 year old daughter. They have made annual contributions of $3,000 to her RESP since she was born. Their family income is $120,000.

Calculate the amount the government will contribute to the RESP if the family contributes $3,000 in the current year.

No unused CESG carried forward since more than $2,500 has been contributed each year.

No Extra CESG as the family earns too much income.
No Canada Learning Bond as the family earns too much income.

Annual max is 20% x $2,500 = **CESG of $500 = amount contributed**

Practice Example B - Expanded

Jeremy and his wife, Diane, have a 2 year old daughter. Last year was the first year they opened her RESP and they contributed $1,000 to it. Their family income is $50,000.

Calculate the amount the government will contribute to the RESP if the family contributes $4,000 in the current year.

max $1,000 CESG over past lifetime (2 yrs x $500 per year), only $200 used to date = $800 max carry forward.

10% Extra CESG on first $500 as family earns between 43,953 and 87,907
No Canada Learning Bond as the family earns too much income.

$4,000 contributions x 20% = $800 ($500 cy + $300 py) + (500 x 10% extra) 50 = **850 CESG** (less than $500 + carryforward so ok)
Maxed at $1,000 per year = not relevant as did not reach

Practice Example C - Expanded

Jeremy and his wife, Diane, have a 1 year old daughter. This year was the first year they opened her RESP. Her grandparents opened an RESP for her last year and contributed $1,500 Their family income is $90,000.

Calculate the amount the government will contribute to the RESP if the family contributes $4,500 in the current year.

max $500 CESG over past lifetime (1 yrs x $500 per year), only $300 used to date by grandparents = $200 max carry forward.

No Extra CESG as family earns too much income
No Canada Learning Bond as the family earns too much income.

$4,500 contributions x 20% = $900 CESG (**Max #1 - maxed at $700. Carry forward of $200 + $500**)
Max #2 - Maxed at $1,000 per year = not relevant, did not reach

Practice Example D - Expanded

Jeremy and his wife, Diane, have a 21 year old daughter. She has an RESP worth $36,000 and is attending a Canadian university Full-time this Fall. She plans to withdraw $5,000 each term from her RESP.

Who will pay tax on the withdrawals? Which amounts will be taxable to them? Is the daughter permitted to take withdrawals as she has specified.

As a post-secondary student, daughter will pay tax on the withdrawals. They are considered Education Assistance Payments.

Daughter will be taxable on any earned income, CESGs, or CLBs included in her withdrawal. It will not be taxable to the extent that it is contributions made to the RESP.

Yes, as a full time student, is limited to $5,000 in her first term, and has no withdrawal limit after that point.

RDSPs

Registered Disability Savings Plan

Image obtained November 1, 2013 from: https://www.comsavings.com/Personal/ProductsAndServices/Investing/RDSP/

Registered Disability Savings Plans(RDSPs) - Overview

- Intended to assist in providing care to disabled individuals, particularly beyond the lifespan of the care providers.
- Contributions are made by the adult relative.
- Beneficiary is the disabled individual.
- No deduction on contributions, income grows tax free.
- Income portion is taxable to the beneficiary on withdrawal. Withdrawn contributions are tax free.

Registered Disability Savings Plans (RDSPs) - Restrictions

- Total contributions are limited to $200,000 over the beneficiary's lifetime.
- Similar to RESPs
  - Canada Disability Savings Grant
  - Canada Disability Savings Bond
- Additional information for those interested can be found online in CRA's guide: RC4460

TFSAs

Tax Free Savings Accounts

Image obtained November 1, 2013 from: http://www.financefox.ca/do-you-have-a-tfsa-account/

Tax Free Savings Plans (TFSAs) - Overview

- Resident individual's over 17 years old can establish a TFSA (since 2009)

- Total individual limit based on years since 2009 or over 17. No annual limit to contributions.

- No deduction on contribution, no tax on earnings, no tax on withdrawals.

- TFSA belongs to the contributor. Not established for the use of someone else.

Tax Free Savings Plans (TFSAs) – Contribution Room

- Annual Limits:
  - 2009 - $5,000
  - 2010 - $5,000
  - 2011 - $5,000
  - 2012 - $5,000
  - 2013 - $5,500
  - 2014 - $5,500
  - 2015 - $10,000
  - 2016-2018- $5,500
  - 2019 - $6,000
  - 2020 - $6,000

- As of 2020 the max an individual can contribute is $69,500 total

  ** this assumes they've been eligible since 2009.*

  ** the count begins once a taxpayer turns 18*

Tax Free Savings Plans (TFSAs) – Contribution Room

- Annual Limits:
  - 2009 - $5,000
  - 2010 - $5,000
  - 2011 - $5,000
  - 2012 - $5,000
  - 2013 - $5,500
  - 2014 - $5,500
  - 2015 - $10,000
  - 2016 & 2017 - $5,500
  - 2019 - $6,000
  - 2020 - $6,000

- An individual turns 18 in 2012. How much can they contribute in 2015 when they open a TFSA?

- $26,000 total ($5,000 for 2012 + $5,500 for 2013/2014 + $10,000 for 2015)

Tax Free Savings Plans (TFSAs) – Contribution Room

- No account needed to accumulate contribution room.
- Withdrawals are added back to contribution room the year AFTER withdrawal. (Do not treat it like a chequing account).
- Over-contributions taxed at 1% per month

Practice Example A

Francis has an starting contribution room of $13,000 in 2013. He contributed $4,000 in February, withdrew $6,000 in May, and contributed another $11,000 in September.

Calculate Francis' contribution room after the September contribution.

$13,000 Starting Balance
(4,000.00) Contribution – reduces balance
(11,000.00) Contribution – reduces balance

(2,000.00) Overcontribution (1% penalty per month).

Practice Example A

Francis has over-contributed by $2,000 at the end of 2013 and withdrew $6,000 in May 2013.

Calculate his contribution room in 2014.

(2,000.00) Over-contribution (ending balance)
5,500.00 New annual limit added to room
6,000.00 Prior year withdrawals added to balance.

$9,500.00 Contribution room in 2014.

Tax Free Savings Plans (TFSAs) – Miscellaneous

- TFSA’s are investment accounts

  Some investments are restricted:
  - Investments in private companies which the TFSA owner or a related individual owns.

- On Death
  - A spouse named as a beneficiary can maintain the deceased spouses TFSA account or roll it into their own account without affecting their contribution room.

Deductible Contribution Types

Types

No Sponsor Required

Registered Retirement Savings Plans (RRSPs)

Registered Retirement Income Funds (RRIFs)

Employer Sponsored

Registered Pension Plans (RPPs)

Pooled Registered Pension Plans (PRPPs)

Deferred Profit Sharing Plans (DPSPs)

Motivations

Company pension plans disappearing

- Defined Benefit
- Defined Contribution

Aging Population

Government Funded Pensions

- CPP $12,000 max
- OAS $6,500 max
- Total $18,500.

Canadian low income cutoff line $21,359

Benefits

Growth of Investment Earnings Tax Free

Tax Deferral – tax-deductible contributions eliminate current tax, and postpone it until retirements funds are needed.

Tax Reduction – Deductions are taken in high income years, retirement funds may be taxable in low income years. Better use of marginal tax rates.

Structure

Time

Deductible
Contributions made
By employee

Employer
Contributions not
A taxable-benefit

Investment Account
Contributions
& Income
Grow Tax Free

Contributions & Earnings
Taxable when withdrawn

RRSPs

Registered Retirement Savings Plans

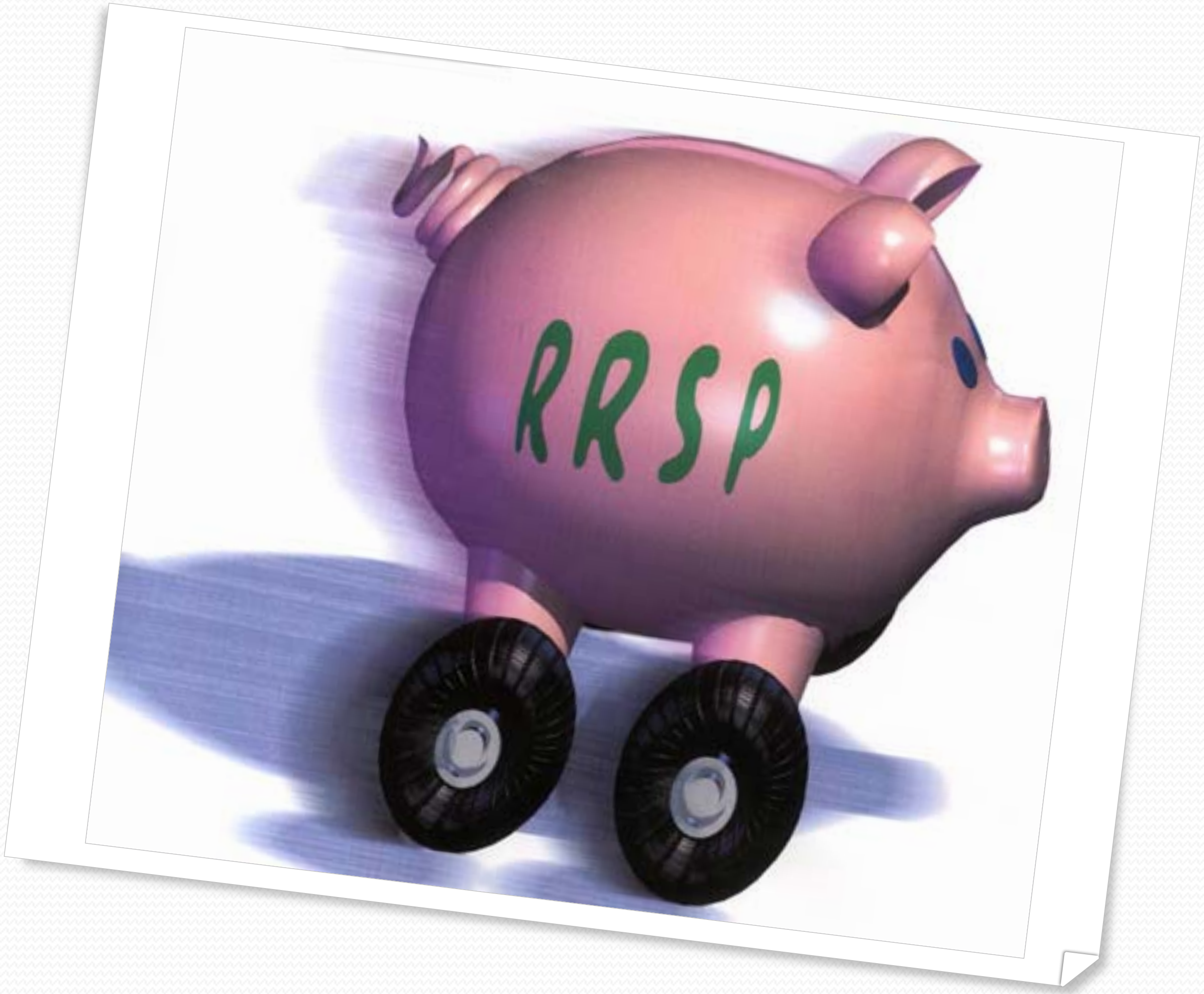


Image obtained November 3, 2013 from: http://www.helpingyoubuyyourfirsthome.ca/blog/bid/78032/Can-I-use-my-RRSP-to-buy-a-home

Registered Retirement Savings Plan (RRSPs) - Characteristics

- Administered by a financial institution
  - Banks, Insurance Companies, Mutual Funds, etc.

- Professionally managed or self-directed investing

- Defined Contribution (set pay in)

- Contributions can be made in the year or 60 days after. Payments in January, 2020 can be deducted in 2019.

Registered Retirement Savings Plans – (RRSPs) Tax Treatment

- Individual – Deductible Payments
- Income Grows Tax Free
- Individual - Taxable Proceeds as ordinary income
  - Important to note that capital gains and dividend lose their nature in an RRSP.

Registered Retirement Savings Plans – (RRSP) Special Rules

- Contributing Investments to an RRSP
  - Deemed disposition of investments
  - Capital gains included in income
  - Losses not able to be realized

- Spousal RRSP
  - Can contribute to a spouse's plan
  - Deducted from contributor's income & room
  - 3 year time delay on withdrawals.

Spousal Example A - Solution

Harriet contributes $5,000 to a spousal RRSP for her husband, Jake, in each of 2010 and 2011.

In 2013, Jake withdraws $12,000 from his RRSP.

What is the impact on Jake and Harriet's income from this withdrawal?

$5,000 attributed to Harriet and taxable in her hands. (any spousal contributes in current year (2013) or two preceding years (2012 or 2011)).

$7,000 taxable to Jake (12,000 total withdrawn – 5,000 attributed).

RRSP Deduction Room

- Prior year's ending balance
  - Plus: Lesser of:
    - 18% of prior year earned income, or
    - 26,230 (2018), 26,500 (2019), 27,230 (2020)
  - Less: Prior year's RPP (pension) Adjustment
  - Less: Current year contributions for self
  - Less: Current year contributions for spouse
- Equals: Ending Balance

- Withdrawals do NOT increase the deduction room.

Components of Earned Income

Additions:

Net employment income

Income from a business

Net rental income from real property

Income earned as a partner

Royalties where received by the author, composer, etc.

Taxable support payments (spousal support)

Research Grants, net of expenses

Canada Pension Plan Benefits

Employment Insurance Benefits

Components of Earned Income

<u>Deductions:</u>

Deductible Support Payments (Spousal Support)

Losses from a business

Losses from being a partner

Loss from the rental of real property

Example A

Mr. Kelly had $12,000 in RRSP deduction room at the end of 2012. His employer says his pension adjustment for 2012 was $4,000 on his $50,000 salary.

Mrs. Kelly has no income so cannot save for her own retirement. **Mr.** Kelly contributes $500 per month toward her retirement from January 2013 – December 2013. Because of his pension, he doesn't make payments for himself

Mr. Kelly has never deducted RRSP contributions before.

What is the impact on his taxable income and what is his RRSP Deduction room?

Example A - Solution

$12,000 Ending RRSP Deduction Room end of 2012

$9,000 $50,000 earned income from 2012 x 18% = $9,000 (less than RRSP 2013 annual limit of $23,820.)

(4,000) Pension Adjustment from T4.

17,000 2013 RRSP Deduction Room

(6,000) Spousal Contributions made by Mr. Kelly

$11,000 Ending RRSP Deduction Room end of 2013

Deduction from Mr. Kelly's income = (6,000) for Spousal Contributions

Example B

Mr. Kelly had $8,000 in RRSP deduction room at the end of 2012. He does not participate in any other pension savings. He earns $3,000 from interest and $80,000 from his rental properties in 2012.

Mr. Kelly contributes $1,300 per month to his RRSPs in 2013

What is the impact on his taxable income and what is his RRSP deduction room?

Example B - Solution

$8,000 Ending RRSP Deduction Room end of 2012

$14,400 $80,000 earned income from 2012 x 18% = $14,400 (less than RRSP 2013 annual limit of $23,820.)

22,400 2013 RRSP Deduction Room

(15,600) Ordinary Contributions made by Mr. Kelly

$6,800 Ending RRSP Deduction Room end of 2013

Deduction from Mr. Kelly's income = (15,600) for RRSP Contributions Made

Registered Retirement Savings Plans (RRSPs) – Special Rules

- Un-deducted Contributions
  - So long as there is RRSP deduction room, an employee can contribute to their RRSP.
  - There is no requirement that the contributions actually be deducted in the year made.

- Excess Contributions
  - Amounts contributed in excess of the RRSP deduction room are penalized 1%/month
  - $2,000 "cushion" before penalties are applied

Registered Retirement Savings Plans – (RRSP) Withdrawals

- Lump sum payments
  - Subject to lump sum tax withholdings
  - Not eligible for pension splitting or pension credit

- Convert to an Annuity
  - Payments still taxable as received

- Convert to a RRIF
  - Like an annuity, with minimum withdrawal rates.

Registered Retirement Savings Plans – (RRSPs) Life Changes

- At Age 71 you must:
  - Transfer RRSP to an RRIF
  - Transfer the RRSP to an annuity
  - Withdraw the RRSP entirely
  - Can continue to make RRSP contributions to a spousal RRSP if the spouse is not yet 71.

- If you die the RRSP:
  - Can roll tax deferred to a spouse or dependant child
  - OR: Be fully taxed in the final return of the deceased

Registered Retirement Savings Plans (RRSPs) – Special Rules

- Home Buyers Plan
  - $35,000 limit per person for a home purchase
  - Non-taxable withdrawal from an RRSP
  - Non-deductible repayment over 15 years (straight line).
  - Repayment begins in the second year following the withdrawal.
  - Amounts not repaid are included in income each year.

Registered Retirement Savings Plans (RRSPs) – Special Rules

- Home Buyers Plan - Qualifying
  - Cannot have a HBP withdrawal outstanding when making a withdrawal.
  - Neither the individual taking the withdrawal or their spouse can have owned a home in the four years preceding the withdrawal.
  - Amounts deposited into RRSP within 90 days before purchase cannot be used.
  - Must have bought or built a qualifying home:
    - Housing unit located in Canada.

Registered Retirement Savings Plans (RRSPs) – Special Rules

- Lifelong Learners Plan
  - Maximum $10,000 per year, to a $20,000 max over four years.
  - Withdrawal to fund full-time post-secondary education for withdrawer or their spouse
  - Non-taxable withdrawal from an RRSP
  - Non-deductible repayment over 10 years (straight line).
  - Repayment begins in the fifth year following the withdrawal.
  - Amounts not repaid are included in income each year.

Registered Retirement Savings Plans (RRSPs) – Special Rules

- Lifelong Learners Plan - Qualifying
  - Cannot have a LLP withdrawal outstanding when making a withdrawal.
  - Amounts deposited into RRSP within 90 days before purchase cannot be used.

RPPs

Registered Pension Plans

Image obtained November 3, 2013 from: http://www.smallbizadvisor.ca/group-retirement/saskatchewan-pension-plan-to-apply-for-prpp-2093

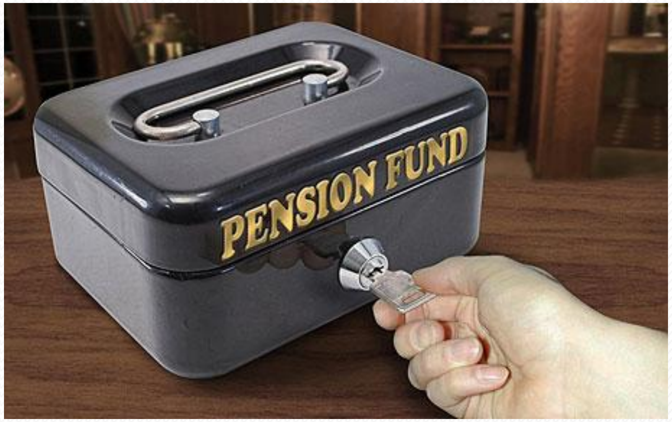
Registered Pension Plans – (RPPs)

- Characteristics
  - Run by Employer
  - Defined Contribution (set pay in)
  - Defined Benefit (set pay out)

- Tax Treatment
  - Employer Contributions – No Taxable Benefit
  - Employee Contributions – Deductible Payments, Taxable Withdrawals
  - Income Grows Tax Free

Contribution Limit

- Same limit as for RRSP contributions (a single limit for all plans).
- Delay in impact means that RPP's can use the current years expected income to absorb the deduction.
- Recall: prior year pension adjustment reduces the deduction room.



Obtained November 3 from: http://www.telegraph.co.uk/finance/personalfinance/pensions/9028142/How-to-manage-your-own-pension.html

Contribution Limit

- Key to remember:

  - If you have an employer run RPP, you must adjust your self-administered RRSP contributions accordingly.

  - Failure to do so is the most common source of over-contributing & penalties.

Registered Pension Plans – (RPP) Withdrawals

- Lump sum payments
  - Subject to lump sum tax withholdings
  - Not eligible for pension splitting or pension credit

- Paid Out Over Time
  - Employer generally administers a scheduled payout

- Convert to an RRIF or Annuity
  - If permitted by the plan terms

PRPPs

Pooled Registered Pension Plans

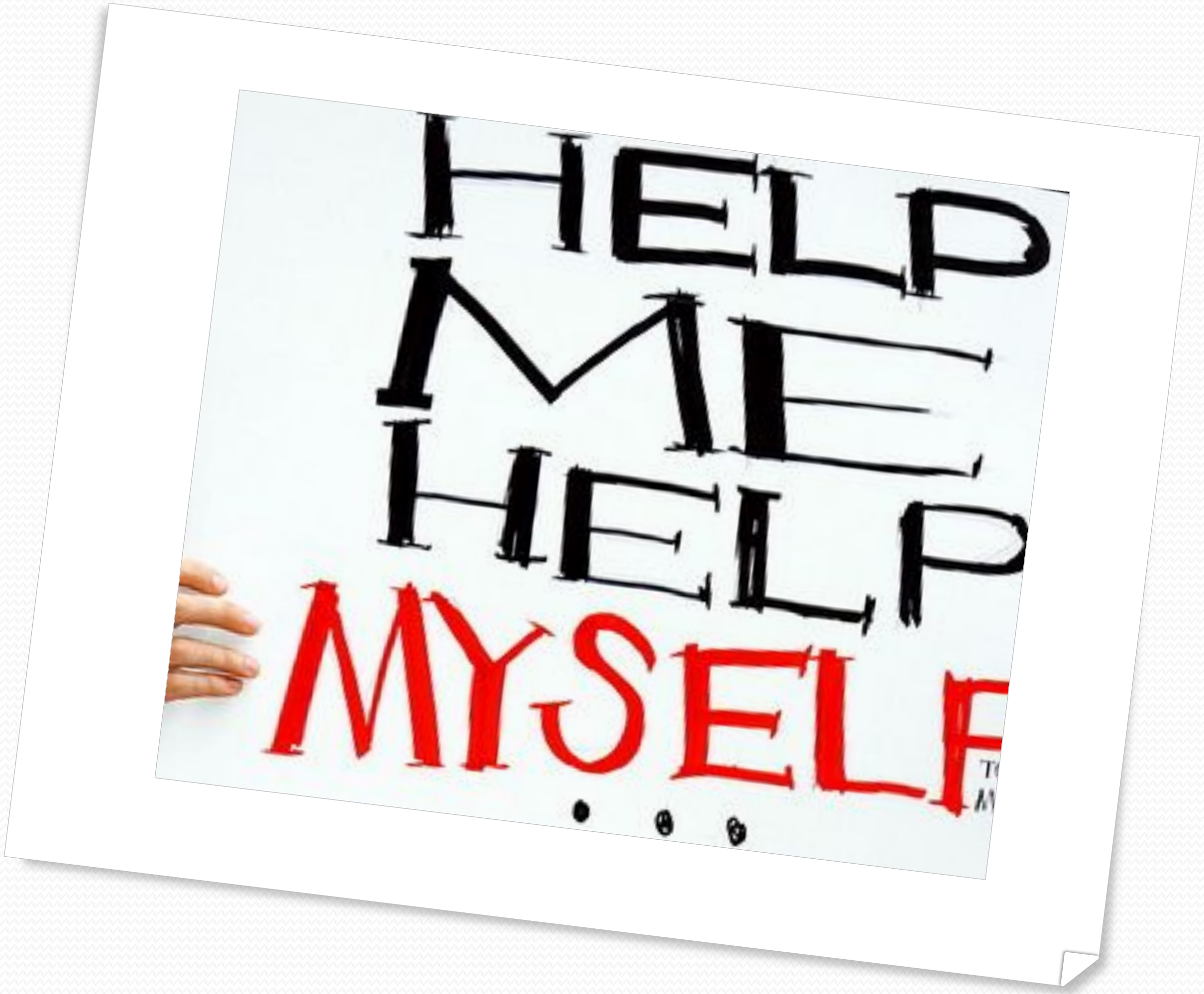


Image obtained November 3, 2013 from: http://www2.macleans.ca/2012/02/09/how-the-government-wants-to-trick-us-into-saving-more/

Pooled Registered Pension Plans (PRPPs)

- MacLean Magazine:

  "How the government wants to trick us into saving more".

- In 2011, only 24% of Canadians used RRSPs.

- The average contribution was $2,830.

Article obtained November 3, 2013 from: http://www2.macleans.ca/2012/02/09/how-the-government-wants-to-trick-us-into-saving-more/

Pooled Registered Pension Plans (PRPPs)

- Employer PRPP participation is optional.
- However, once chosen, employees of companies that opt in are automatically enrolled.
- Employees will have to opt-out to get out of the program.
- Similar to an RPP except many companies pool together to save administration costs.

Pooled Registered Pension Plans (PRPPs)

- Self-employed individuals and employees of company's that don't participate can still opt-in to a PRPP plan.
- Same contribution room as RRSPs/RPPs.
- Effective from January 1, 2013 onward federally.
- Participating requires the province of residence to have enacted legislation.

RRIFs

Registered
Retirement
Income Funds

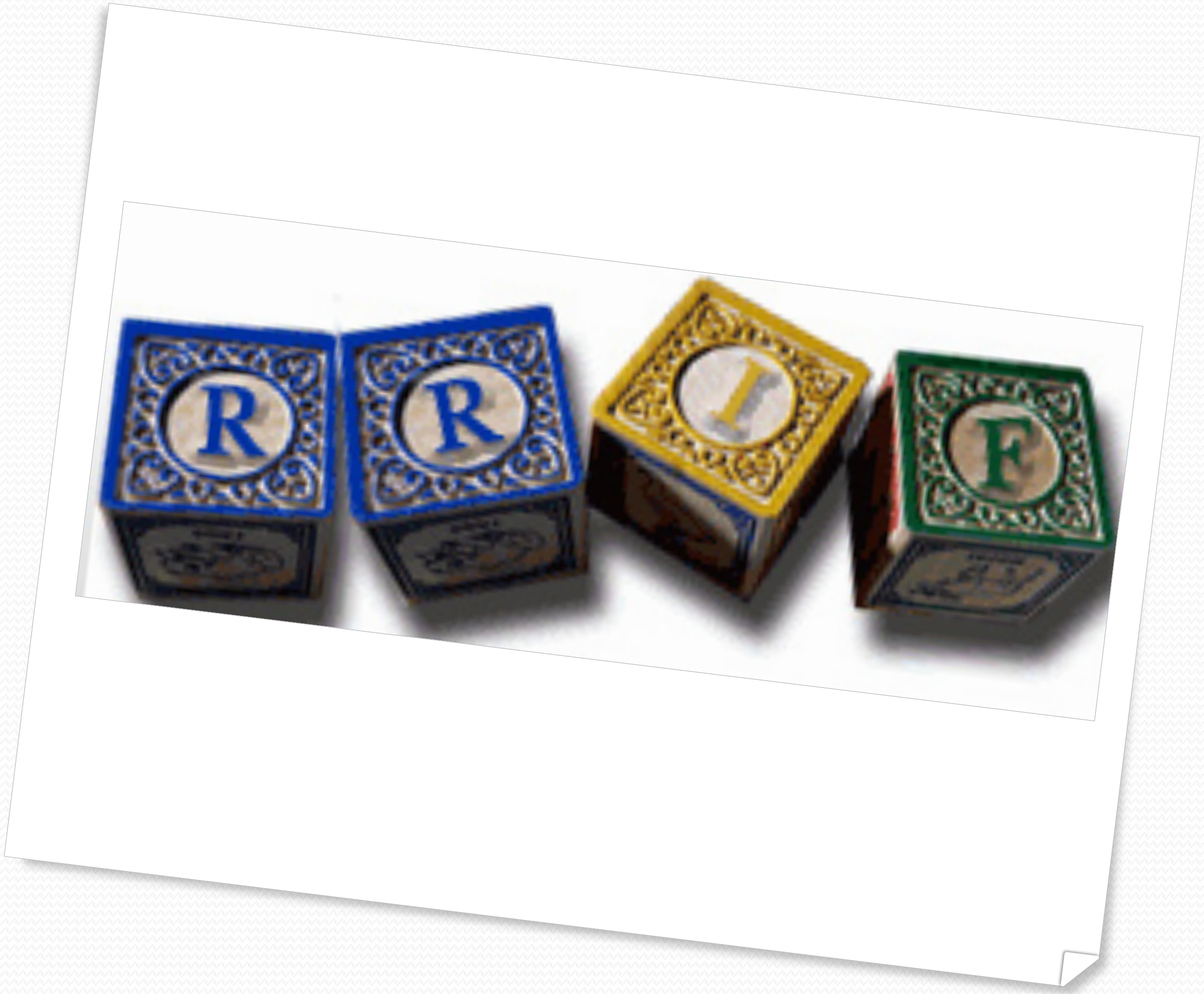


Image obtained November 3, 2013 from:
http://www.advisor.ca/news/industry-news/are-you-getting-rrif%E2%80%99d-off-18788

Registered Retirement Income Funds – (RRIFs)

- Deductible contributions cannot be made to a RRIF

- A RRIF is another retirement plan that has been converted into an income stream.

- Ie. Stop depositing money in, start taking money out.

- Rollover of an RRSP or RPP into a RRIF is tax free, and begins the process of using the funds in retirement.

Registered Retirement Income Funds – (RRIFs)

- Withdrawals are taxed as ordinary income.
- Withdrawals from RRIFs are eligible for pension splitting and the pension credit.
- Minimum annual withdrawals are set by legislation and are based on the age of the recipient and the funds in the RRIF.
- No maximum withdrawal amount.

Registered Retirement Income Funds – (RRIFs) Life Changes

- If you die the RRIF:
  - Can roll tax deferred to a spouse or dependant child
  - OR: Be fully taxed in the final return of the deceased

DPSPs

Deferred Profit
Sharing Plans

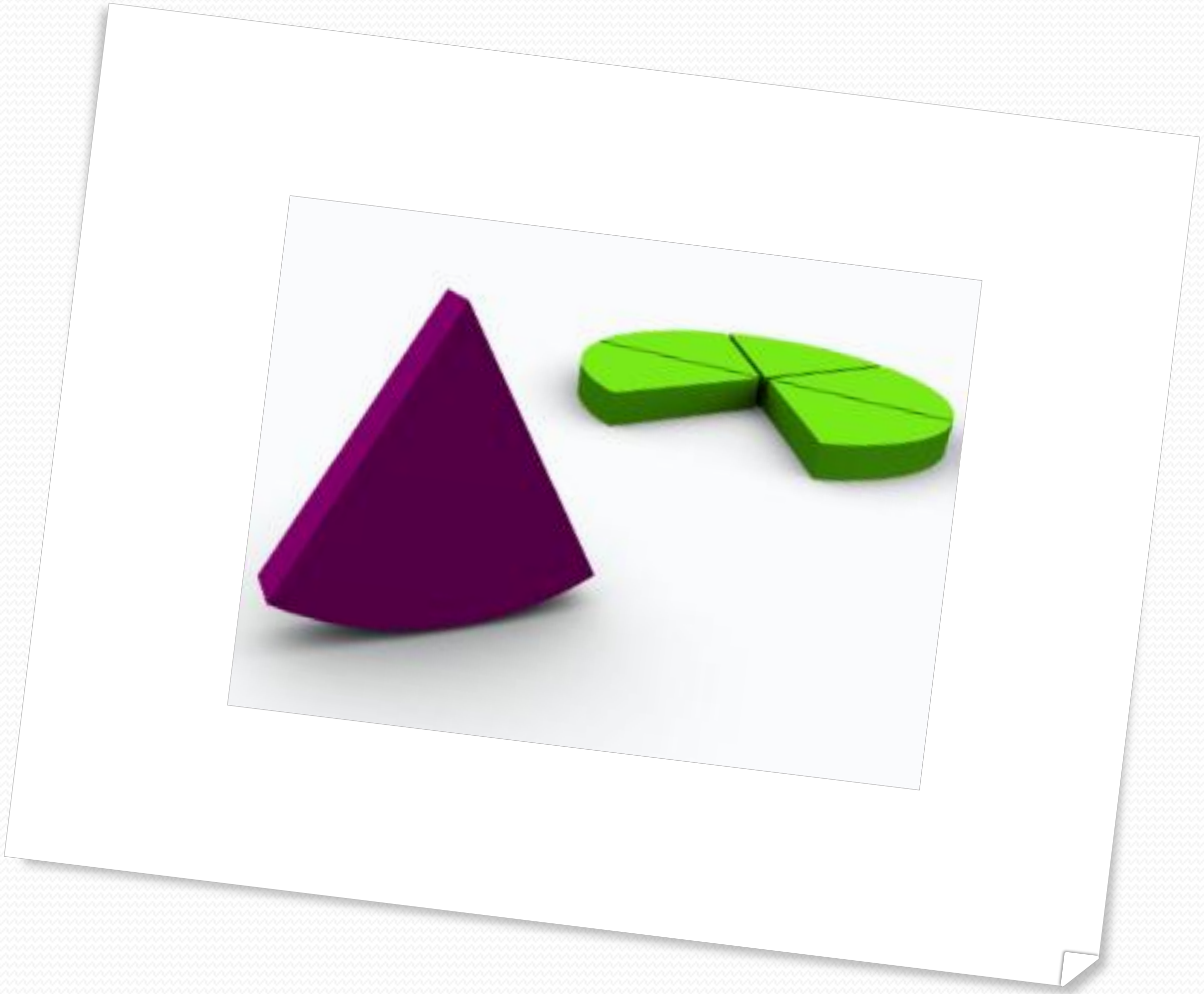


Image obtained November 3, 2013 from:
http://www.benplans.com/services/profit-sharing-plans.html

DPSP

- Characteristics
  - Payment made to plan by employer based on business profits
  - Not allowed for those related to those owning 10% or more of company
  - No specific payout schedule

- Tax Treatment
  - Employer Contributions – Payments not a taxable benefit, deductible
  - Employee Contributions – Not allowed to pay in
  - Income Grows Tax Free

Review

- Registered Education Savings Plans (RESP)
- Registered Disability Savings Plans (RDSP)
- Tax Free Savings Accounts (TFSA)
- Registered Retirement Savings Plans (RRSP)
- Registered Pension Plans (RPP)
- Pooled Registered Pension Plans (PRPP)
- Registered Retirement Income Funds (RRIF)
- Deferred Profit Sharing Plans (DPSP)