



2005-2006 RRSP OVERVIEW

For the 2005 taxation year, the deadline for making RRSP contributions that will be deductible on your tax return is midnight on **Wednesday, March 1, 2006**.

There were some major changes to RRSPs over the past year. We suggest that you take the time to read this overview to see if any of the points or strategies apply to you or other family members.

What's New?

- Retroactive to January 1, 2005, the **foreign property limit for registered plans** was eliminated in the February 2005 federal budget. Previously, investors were limited to 30% foreign content in their registered accounts, with a 1% per month penalty on any excess foreign holdings.
- The requirement to purchase an annuity with federally regulated **Life Income Funds (LIFs)** at age 80 was abolished in the February 2005 federal budget. Seniors can now continue to make withdrawals from their LIF accounts after that age, subject to limits on their annual withdrawals, like RRIF and LRIF accountholders.
- **A new federal bankruptcy law that could protect RRSP accounts from creditors** was passed in late 2005. The protection from this new law would only come into effect if the planholder declared bankruptcy. Creditors would still be able to access a planholder's RRSP under a court order that did not involve petitioning the debtor into bankruptcy. The legislation is not expected to come into force until later this year due to concerns by the Senate Banking Committee about the way in which the proposal passed quickly in Parliament just before a non-confidence vote brought down the Liberal government.
- **CRA recently issued an alert cautioning taxpayers to avoid financial schemes** where promoters promise a tax-free withdrawal of RRSP funds. These schemes typically involve the purchase of shares of a private company and loans from the promoter at low or no interest. It should be noted that most shares of private companies are not eligible to be held in your RRSP and that using your RRSP as collateral for a loan or purchasing shares in a private company results in the full value of the shares or loan being taxed as income.

**Contribution Limits:**

Year	RRSP Limit	Defined Contribution RPP Limit	Deferred Profit Sharing Plans
2005	\$16,500	\$18,000	\$9,000
2006	\$18,000	\$19,000	\$9,500
2007	\$19,000	\$20,000	\$10,000
2008	\$20,000	\$21,000	\$10,500
2009	\$21,000	\$22,000*	\$11,000*
2010	\$22,000*		

* Indexed to average wage growth

General Points to Keep in Mind:

- **Your 2005 RRSP limit equals the lesser of 18% of your 2004 earned income and \$16,500**, minus your 2004 pension adjustment (PA) factor (Box 52 of your 2004 T4 slip), plus any carry forward of unused contribution room from previous years. This carry forward amount can be confirmed on your 2004 Notice of Assessment. *(We recommend you review your RRSP limit with your E.E.S. consultant particularly if you are carrying forward undeducted RRSP contributions. CRA has a rather confusing method of reporting this amount.)*
- While we would suggest that you **maximize your RRSP contributions whenever cash flow permits**, you can carry forward the unused contribution room indefinitely.
- If you have RRSP contribution room available, but don't want to use the deduction on your 2005 tax return, **consider making your contribution now but deducting it in the future** when your tax bracket/rate is higher.
- **The RRSP over-contribution limit remains at \$2,000, with a penalty of 1% per month** on any over-contribution position. If you have previously made an over-contribution, you must reduce it to the \$2,000 level before making any new contributions to your plan(s).
- **If you withdrew funds from your RRSP under the Home Buyer's Plan (HBP) before December 31, 2003, or the Lifelong Learning Plan (LLP) before December 31, 2000, you must make a repayment by Wednesday, March 1, 2006.** You should have received a repayment statement from CRA advising you of the required amount. If you do not repay the required amount (1/15th of the original



withdrawal for the HBP or 1/10th of the original amount for the LLP), that amount will be included as taxable income for 2005.

- **If you plan to withdraw funds from your RRSP under the HBP during 2006**, the home must be purchased by October 1, 2007. Repayments begin two years after the withdrawal – i.e. for a withdrawal in 2006, you must repay 1/15th of the original amount during 2008 or the first 60 days of 2009.
- **If you left an employer-sponsored pension plan during 2005 and transferred the commuted value of that pension to your RRSP, you may be eligible for a Pension Adjustment Reversal (PAR).** Also, if your employer wound up a Defined Benefit Pension Plan or converted it to another vehicle, such as a group RRSP, you too may be eligible for a PAR. This PAR restores some of the lost RRSP contribution room resulting from past pension adjustment factors. If you have not received a form T10 advising you of your additional RRSP contribution room, contact your previous employer as soon as possible. **This additional RRSP room is available for contributions to be deducted on your 2005 tax return. You can make this contribution to your own RRSP or to a spousal RRSP.**
- **Labour-sponsored investment funds (LSIF)** offer federal and potentially provincial tax credits over and above the regular RRSP deduction. We caution you to evaluate these vehicles from an investment point of view, rather than focusing solely on the tax benefits. These funds *must* be held for at least eight years in order to avoid having to repay the tax credits. As well, they tend to be more aggressive than ordinary mutual funds.
- We recommend that you **verify the beneficiary designation** on each of your RRSP/RRIF accounts. Most institutions issue a statement at the end of the year so verify this first. However, if this information is not on the statement, check with the institution. Having either your spouse or a dependent over the age of 18 who qualifies for the disability tax credit as the designated beneficiary will allow a simple tax-free rollover of your RRSP/RRIF upon your death. If a financially dependent child is named as the beneficiary, the amount may be used to purchase an income producing term-certain annuity to mature when the child is 18.

Planning Strategies:

- **You can produce a tax refund without putting any new money into your RRSP.** By using money that's already inside your RRSP, you can purchase a labour-sponsored investment fund in order to generate a tax credit. For a \$5,000 investment, you will receive combined federal and provincial credits totaling approximately 30%, which puts \$1,500 back in your pocket by simply moving some



money around in your RRSP. In Ontario, there is an additional credit of 5% (making the total credits received 35%) for research-oriented investment funds (ROIFs) that invest in colleges, universities, hospitals or other research facilities. Remember, these types of investments are highly speculative, require a long-term horizon, a high tolerance for risk and an already well-diversified portfolio.

- If you don't have the cash on hand to make your RRSP contribution, **consider transferring other investments into your self-directed plan**. The current market value of the investment will count as your contribution. Remember that the transfer may trigger a capital gain, which will be taxable to you. On the other hand, **if you incur a loss on this type of transaction, you will not benefit from the capital loss**. In this case, you may want to consider realizing the loss by selling the investment, then transferring the cash into your RRSP. There used to be an exception to this loss rule when an investment was sold at a loss and then repurchased in an RRSP or RRIF. The 2004 federal budget amended the definition of 'affiliation' with respect to beneficiaries of trusts (your RRSP is considered to be a trust and you are the beneficiary). Therefore, if you wish to hold that same security within your RRSP, by waiting at least 31 days before repurchasing it, you will be allowed to claim the realized loss on your personal tax return.
- **Severance payments may be transferred directly to your RRSP**, regardless of your RRSP contribution room, in some cases. If you had service prior to 1996, the eligible retiring allowance rollover is \$2,000 per year, as well as an additional \$1,500 per year prior to 1989 in which you were not a member of a company pension plan. Your former employer will report this eligible retiring allowance on a form T4A.
- **Instead of borrowing money for your RRSP contribution, transfer assets as described above, and then borrow to repurchase the same investments in your freehold account**. By doing so, the interest on your loan will be tax deductible, whereas interest on an RRSP loan is not tax deductible. It bears pointing out that banks have this in mind when setting loans rates and generally offer a lower rate on RRSP loans.
- **If you need to withdraw funds from your RRSP**, try and do so in a year when you have little or no income.
- If you hold **Canada Savings Bonds**, these can be transferred to a *Canada RRSP* with the Government of Canada without the requirement of a self-directed plan (and the accompanying administration fees). You can also purchase new Canada Savings Bonds to be deposited to this no-fee Canada RRSP directly from the government of Canada, your bank, your financial institution or your investment dealer.



- If you make your **2006** contribution in a lump sum now, **you can apply to CRA to authorize your employer to deduct less tax from your pay cheque for the next year.** While you won't receive a tax refund next April, you will have increased cash flow during the year. Essentially, you receive your refund in advance through decreased source deductions. Your E.E.S. consultant can file the appropriate form with CRA.
- **Take full advantage of spousal RRSPs where applicable.** You benefit from the current deduction and future withdrawals are included in your spouse's income thereby providing **income splitting during retirement.** Contributions to a plan for a common-law or same-sex spouse are also permitted. However, you should be aware of the three-year attribution rules. If you make a spousal RRSP contribution this year and your spouse makes a withdrawal from a spousal plan this year, next year, or the following year, this withdrawal will be included in your income. This rule would apply even if funds are contributed to one spousal plan and withdrawn from another.
- **Owner managers with control over their income** may want to ensure that they have enough employment income to maximize their RRSP contributions. In order to reach the maximum contribution level for 2007 of \$19,000, you must have \$105,556 of earned income in 2006.
- **If your child has earned income, he or she can make an RRSP contribution,** regardless of age. In most cases, it will not be worthwhile to deduct the contribution until future years when his or her income is more substantial. However, your child will still enjoy the benefits of deferring taxes on income earned inside the RRSP.
- **If you turn 69 in 2006,** you must convert your RRSP/LIRA to a RRIF/LIF/LRIF before **December 31st, 2006.** If you have contribution room available, make your contributions prior to making this conversion. An important point to remember is that the beneficiary designation for your RRSP/LIRA *does not* automatically transfer over to your newly established RRIF/LIF/LRIF. If you want your spouse or someone else to be the beneficiary of your new account, you should ensure that this is specified on your application. The tax consequences and probate fees that result from not naming a beneficiary can be significant.
- **When you establish your RRIF,** you may want to base the mandatory minimum withdrawal on the age of your spouse if he or she is younger than you. This will enable you to withdraw less from your RRIF if you do not need the funds, thereby allowing you to defer the taxes payable on the withdrawals even longer. Of course, if you should need to do so, you are able to withdraw more than the minimum amount.



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- Remember, **if you have a spouse who is younger than you, you may be able to contribute to his/her RRSP until the end of the year in which *they* turn 69**, based on *your* RRSP limit. You may have RRSP room carried forward from previous years or new room that became available because of earned income you had during the previous year. Your spouse will be able to draw on the tax-deferred income in retirement, but you will get the deduction on your tax return.
- **Taxpayers over 65 are entitled to a pension credit to offset the taxes on the first \$1,000 of pension income annually**, including withdrawals from a RRIF. If you're in the lowest marginal tax bracket (less than approximately \$35,000 of taxable income) and you do not have any other pension income, you may want to consider setting up a RRIF or an annuity to pay out just \$1,000 annually. Simple cash withdrawals are not eligible for this credit.

**PLEASE CONTACT YOUR E.E.S. CONSULTANT FOR
FURTHER DETAILS CONCERNING ANY OF THESE RRSP TOPICS.**

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