

## Spousal RRSPs (Post-Pension Splitting)

Registered Retirement Savings Plans (RRSPs) are a tax-advantaged arrangement allowing taxpayers to save for their retirement. These plans are appealing, since taxpayers are able to deduct contributions (within specified limits) to these plans. Furthermore, the investment income earned in the plan grows on a tax-deferred basis. Taxes will only be paid when amounts are withdrawn from the plan.

Many taxpayers have chosen to contribute to Spousal RRSPs rather than their own RRSPs because this is a legitimate and simple method of splitting income. The tax rules provide that amounts withdrawn from a spousal plan will be included in the spouse's income, except where certain attribution rules apply. Given a 20% to 25% spread between the highest and lowest tax brackets in some provinces, this will result in tax savings where the tax bracket that the spouse is in for the year of withdrawal is lower than that of the contributor for the year in which he or she deducted the contribution.

Significant changes were made to Canada's tax laws with the introduction of the Pension Splitting regime. These new rules received Royal Assent on June 22, 2007 and are effective for the 2007 and later taxation years. Taxpayers and their advisors are now assessing whether Spousal RRSPs remain of value. Our document discusses this, but first provides an overview of the tax rules for Spousal RRSPs.

### I. Spousal or Common-Law Partner Plans

The Income Tax Act (Canada) (ITA) contains a definition of a "spousal or common-law partner plan".<sup>1</sup> We refer to these plans as Spousal RRSPs, even though it is clear that plans for common-law spouses (including same-sex partners) are also contemplated here.

The ITA definition captures two types of arrangements. The first type is where a taxpayer contributes to an RRSP under which his or her spouse (or common-law partner) is the annuitant at the time the contribution is made.

The second type is where funds are later transferred from this first type of arrangement to another RRSP that the spouse or common-law partner has contributed to and for which he or she is the annuitant. (In this document we will refer to this type of plan a "regular RRSP".) The RRSP receiving the funds will become a "spousal or common-law partner plan", even though it originally only held funds that the spouse (or common-law partner) had himself or herself contributed. Thus, plan-to-plan transfers from a Spousal RRSP to regular RRSP cause the latter to become a Spousal RRSP. This is important when we examine how the attribution rules work. (These same rules apply where amounts are transferred from a Spousal RRSP to a Registered Retirement Income Fund (RRIF).)

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<sup>1</sup> See definition of "spousal or common-law partner plan" in subsection 146(1) of the Income Tax Act (Canada) (ITA).

## II. Amount of Contribution

The ITA contains rules governing how much may be contributed to an RRSP. The “unused RRSP deduction room” is calculated for each taxpayer. (While not a defined term in the ITA, financial planners and others often refer to this as “RRSP room”. We will use these terms interchangeably in this document.) This amount could be sizeable for taxpayers who have not been contributing to an RRSP, since it is a cumulative amount that has been growing since 1991, assuming that the taxpayer has had “earned income” in any year starting with the 1990 taxation year.

The unused RRSP deduction room is of course reduced by contributions made to a regular or Spousal RRSP for the 1991 and later taxation years, and will be reduced where a taxpayer participates in an employer-sponsored Registered Pension Plan (RPP) (including Individual Pension Plan (IPP)) and/or Deferred Profit Sharing Plan (DPSP). Where the taxpayer participates in an RPP and/or DPSP, any Pension Adjustment and net Past Service Pension Adjustment that must be reported will reduce the “RRSP room”, as will certain other prescribed amounts. Any Pension Adjustment Reversal that must be reported will increase it.<sup>2</sup>

For 2007, the cumulative RRSP room could increase by as much as \$19,000 (that is, the dollar limit for 2007), assuming that the person had “earned income” of at least \$105,556 in 2006, and that the person did not participate in an employer-sponsored RPP and/or DPSP.

### RRSP Dollar Limits<sup>3</sup>

2007	\$19,000
2008	\$20,000
2009	\$21,000
2010	\$22,000
2011	Indexed

With Spousal RRSPs, the contributing spouse is looking at his or her “RRSP room” and choosing to contribute an amount to the Spousal RRSP, rather than his or her own regular RRSP. The Spousal RRSP rules do not provide for a doubling of the “RRSP room”. Instead, the taxpayer simply chooses whose RRSP to contribute an amount to.

Taxpayers should make sure that they do not over-contribute, since a 1% per month penalty tax applies to excess RRSP contributions above a threshold amount (generally \$2,000).<sup>4</sup> Where a taxpayer becomes aware of the fact that excess contributions have been made, these should be withdrawn as soon as possible, so that this “penalty clock” stops. Specific CRA forms should be used to request the refund so that this excess may be refunded without taxes being withheld.<sup>5</sup> Remember here that excess contributions may generally only be withdrawn within specific time frames on a non-taxable basis.<sup>6</sup> (Amounts withdrawn once this period has expired will be taxable, even though the contribution was not deductible. Thus, a “double-tax” situation could arise.)

Special rules allow the penalty tax to be waived where the cumulative excess arose because of a reasonable error and reasonable steps are being taken to remove the excess.<sup>7</sup> However, the taxpayer will have to obtain CRA’s consent for this to happen.

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<sup>2</sup> See definition of “RRSP deduction limit” in subsection 146(1) of the ITA.

<sup>3</sup> See definition of “RRSP dollar limit” in subsection 146(1) of the ITA.

<sup>4</sup> See subsection 204(2.1) of the ITA.

<sup>5</sup> See *Form T3012A – Tax Deduction Waiver on a Refund of Undeducted RRSP Contributions made in 20\_\_*.

<sup>6</sup> See subsection 146(8.2) of the ITA.

<sup>7</sup> See subsection 204.1(4) of the ITA.

Because of the risk to over contributing, taxpayers want to check the amount of their "RRSP room" before contributing. Moreover, taxpayers will want to avoid the paperwork associated with requesting refunds of excess contributions, etc.

Taxpayers should check their most recent Notice of Assessment for the amount of their "RRSP room". The "2007 RRSP Deduction Limit" will be shown on the Notice of Assessment that would have been sent out for the 2006 taxation year. This is the amount that may be contributed and deducted for tax purposes in 2007. (If a prior taxation year has been reassessed, CRA may instead send a Form *T1028 – RRSP Information for 20\_\_* or may issue a Notice of Reassessment containing this information.) Taxpayers who have registered with CRA for on-line access to certain tax information (that is, have set up "My Account") will be able to access this information there.

Remember here that while the "RRSP room" governs what may be contributed to an RRSP, it has no bearing on when a taxpayer chooses to deduct an amount for tax purposes. A taxpayer may want to "save" the deduction for the contributed amount to a later taxation year in which he or she will be in a higher tax bracket (or perhaps to draw down net income so as to avoid the Old Age Security (OAS) claw-back). The deduction could even be taken after age 71. Any undeducted RRSP contributions are set out on the Notice of Assessment issued as "unused RRSP contributions".<sup>8</sup>

Some taxpayers in fact choose to over-contribute by \$2,000, as excess contributions of up to this amount do not attract the 1% per month penalty tax that applies to excess contributions. This \$2,000 would be included in the "unused RRSP contributions".

### **III. Requirement that RRSPs Mature by End of Year in which Annuitant Attains Age 71**

The 2007 Federal Budget increased the age at which registered plans (including RRSPs) must mature. Starting with the 2007 taxation year, an RRSP cannot provide for maturity after the end of the year in which the annuitant attains age 71.<sup>9</sup>

A taxpayer who is older than age 71 will still have a "RRSP room". However, since registered plans must mature by the end of the year in which the annuitant attains age 71, the taxpayer could only contribute to his or her own plan up to December 31<sup>st</sup> of the year in which he or she turned 71. The usual "60-day rule", which lets a taxpayer deduct amounts contributed no later than 60 days after year-end, does not apply.

Of course, this older-than-age-71 taxpayer could contribute to a Spousal RRSP, assuming that the spouse or common-law partner had not attained age 71. Again, care must be taken in ensuring that the contribution is actually made to the Spousal RRSP prior to when it must mature.

### **IV. Utilizing Income Earned in Year of RRSP Conversion to Make Final RRSP Contribution**

In the above section we look at the timing of contributions made to RRSPs in the year in which they must mature. Let's look at the situation of a taxpayer who turns 71 in 2007 and knows that his or her regular RRSP must mature by December 31<sup>st</sup> of that year. Let's further assume his or her "earned income" in 2007 is \$150,000. This would allow create \$20,000 (i.e., 18% of earned income, subject to the RRSP dollar limit cap of \$20,000 for 2008) of RRSP room in 2008.

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<sup>8</sup> See definition of "unused RRSP deduction room" in subsection 146(1) of the ITA.

<sup>9</sup> See paragraph 146(2)(b.4) of the ITA.

Above we discussed the Spousal RRSP as a possible solution in this situation. There is, however, another solution. This person could contribute the \$20,000 to his or her own RRSP in December 2007, which is to be deducted in 2008. Of course, since the amount was contributed a month early, the 1% per month penalty tax would apply for that month.

CRA, in a Technical Interpretation issued in 1997, stated the following about a parallel scenario:

“... Once [the RRSP has] matured, it can not accept any further contributions. However, an individual is not precluded from deducting contributions made to an RRSP prior to its maturity after it has matured ... Furthermore ... the individual will be able to utilize income earned in the year of the conversion to determine the final contribution deduction.”<sup>10</sup>

Of course, any taxpayer contemplating doing this, would want to be sure of her RRSP room, as well as his or her “earned income” for the year in which the excess contribution is made. This is important so that the penalty applies for just the one month.

Similar steps could be taken with contributions to a Spousal RRSP.

## V. Withdrawals from Spousal RRSPs and Attribution Rules

Amounts withdrawn from a Spousal RRSP are included in the annuitant spouse’s (or common-law partner’s) income, except where the “attribution rules” apply. The attribution rules were introduced to discourage the short-term use of Spousal RRSPs as an income-splitting device.<sup>11</sup>

CRA has issued a form (*T2205 – Amounts from a Spousal or Common-Law Partner RRSP or RRIF to Include in Income for ...*) that may be used to calculate the amount that each of the (contributing) taxpayer and spouse (or common-law partner) needs to include in income where attribution does apply.

### *The Attribution Rule*

Let’s assume that Suzanne contributed \$10,000 to a Spousal RRSP for her husband Robert in the 2007 calendar year. They now need to carefully monitor withdrawals in order to avoid attribution. Attribution will apply to the withdrawal if either of the following conditions is met: (1) there are contributions to any other Spousal RRSPs at any time in the same calendar year, or (2) amounts had been contributed to any Spousal RRSP in the two prior calendar years.

Let’s assume that this \$10,000 is the only amount that Suzanne contributes to the Spousal RRSP. If Robert, her husband, makes withdrawals at any time in any of the 2007 through 2009 years from any Spousal RRSP established by her for him, the first \$10,000 of such withdrawals will be included in Suzanne’s and not his net income. Thus, these rules clearly thwart short-term income splitting.

Let’s assume attribution did apply to this \$10,000 because the amount was withdrawn in 2009. Robert would report the \$10,000 received from the Spousal RRSP in his net income, but would then take a deduction for the income (in this case \$10,000) that is to be attributed to Suzanne.<sup>12</sup> Thus, the attributed amount is essentially an “in” and an “out” on his tax return. Suzanne would then include the attributed amount in her net income.<sup>13</sup>

<sup>10</sup> See Technical Interpretation 9706655, dated April 28, 1997.

<sup>11</sup> See paragraph 7 of *Interpretation Bulletin IT-307R4 – Spousal or Common-Law Registered Retirement Savings Plans (IT-307R4)*, dated January 24, 2003.

<sup>12</sup> See subsections 146(8) and 146(8.6) of the ITA.

<sup>13</sup> See subsection 146(8.3) of the ITA.

### *No Attribution Where Undeducted Contributions are Withdrawn*

A taxpayer may have made contributions to an RRSP (or Spousal RRSP) that they expected to be able to deduct in the year or in the immediately preceding year. These amounts (including excess amounts on which the 1% per month penalty could apply) can only be withdrawn from an RRSP (or Spousal RRSP) on a non-deductible basis within specific time frames (that is, (i) in the year the contribution is made, (ii) in the year in which the Notice of Assessment is received for the contribution, or (iii) in the year following the year referred to in (i) or (ii).)<sup>14</sup>

Where the excess is withdrawn from a Spousal RRSP under this rule, these amounts can no longer be attributed back to a taxpayer.<sup>15</sup> The (contributing) taxpayer will include the amounts in income, but will then receive an offsetting deduction.

### *Attribution where Taxpayer and Spouse (or Common-Law Partner) have contributed to the Same RRSP*

Where a taxpayer and their spouse (or common-law partner) both contribute to the same RRSP, it is considered a Spousal RRSP. When the annuitant spouse or common-law partner begins to withdraw funds, he or she cannot state that they are first drawing out their own contributions, and thus avoid attribution. Instead, the attribution rules will apply in the manner decreed by CRA. In the year of the withdrawal it will be necessary to look at how much the taxpayer contributed in the year (or two preceding years). Withdrawals of up to this amount will be attributed back to the taxpayer. (Of course, amounts previously attributed back would not be attributed back a second time.)<sup>16</sup>

Because of the application of the attribution rules in situations like this, we recommend that the taxpayer and spouse (or common-law partner) not contribute to the same plan.

### *Other Exceptions to the General Rule*

The attribution rules do not apply where the spouse or common-law partner receives the amount from the Spousal RRSP at a time that they are living separate and apart because of a breakdown of the marriage or the common-law partnership.<sup>17</sup>

Amounts that a spouse or common-law partner withdraws in the year the (contributing) taxpayer dies are not attributed back.<sup>18</sup> Nor are amounts that are withdrawn when the (contributing) taxpayer or his or her spouse (or common-law partner) is a non-resident of Canada.<sup>19</sup>

Also, effective for the 1988 and subsequent taxation years, attribution does not apply to certain amounts included in the annuitant spouse's income upon the death of that spouse.<sup>20</sup>

Where a lump sum is transferred on a direct basis from the Spousal RRSP to a RRIF, the attribution rules do not come into play at the time of the transfer.<sup>21</sup> Instead, part of the income withdrawn from the RRIF may be attributed back.<sup>22</sup>

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<sup>14</sup> See subsection 146(8.2) of the ITA.

<sup>15</sup> See subsection 146(8.21) of the ITA.

<sup>16</sup> See paragraph 14 of IT-307R4.

<sup>17</sup> See paragraph 146(8.3) of the ITA.

<sup>18</sup> See paragraph 146(8.7)(a) of the ITA.

<sup>19</sup> See paragraph 146(8.7)(b) of the ITA.

<sup>20</sup> See paragraph 146(8.7)(e) of the ITA.

<sup>21</sup> See paragraph 146(8.7)(d).

<sup>22</sup> See subsection 146.3(5.1).

Let's look at an example. Let's assume that on December 31, 2006 Sam (age 63) transferred \$50,000 in his Spousal RRSP to a RRIF. (While his wife Mary had not contributed anything to this particular Spousal RRSP, she had in fact contributed \$10,000 to another Spousal RRSP in 2005.) The minimum amount that he would have to withdraw in 2007 would be 1/27<sup>th</sup> of the Fair Market Value of the assets in the plan on January 1, 2007<sup>23</sup>. This works out to \$1,852. He instead chooses to withdraw \$5,000.

The attribution rules state that his wife Mary will have to include the least of the following three amounts in income:

- Amounts contributed by Mary to any Spousal RRSP (or RRIF) for Sam in 2007 or the two preceding taxation years (\$10,000);
- The amount paid from the RRIF (\$5,000), and;
- The amount withdrawn from the RRIF that is in excess of the "minimum amount" (\$3,148).

In our example, Mary will have to include \$3,148 in her income. The attribution could have been avoided in two ways. The first method is to have Sam wait until 2008 to withdraw an amount from the RRIF. By doing so, the first of the three amounts becomes zero, since no amount would have been contributed to a Spousal RRSP in 2008 or the two preceding taxation years. Since the least of the three amounts is now zero, there is no attribution!

The second method is to have Sam only withdraw the minimum from his RRIF (\$1,852). By doing this, the third of the three amounts becomes zero. Again, since the least of the three amounts is now zero, there is no attribution.

On the subject of RRIFs and attribution rules, special transitional rules were introduced because of the increase in the age at which RRIFs and other registered plans must mature. Some taxpayers started withdrawing amounts out of the RRIFs because they had attained age 69. However, these individuals might not have commenced taking withdrawals, had the age 71 rule already been in effect. Thus, one transitional rule that was introduced set the "minimum amount" to zero for taxpayers who were directly affected by these changes. These are the annuitants who turn age 69 or 70 in 2006, or who turn age 70 in 2007.<sup>24</sup>

A second transitional rule had to be introduced to fix the attribution rules for RRIFs. Since the first rule deemed these taxpayers to have a "minimum amount" of zero, the entire RRIF withdrawal would have been in excess of the "minimum amount", thus potentially causing attribution to apply. This second rule provides that for purposes of the attribution rules, the "minimum amount" is not set to zero. It's the amount that would have otherwise been calculated.<sup>25</sup>

Attribution can also be avoided where the proceeds of the Spousal RRSP are used to acquire an annuity, the terms of which provide that it cannot be commuted, and it is in fact not commuted, in whole or in part, within 3 years after its acquisition.<sup>26</sup>

## **VI. Contributing to a Spousal RRSP after the Death of a Taxpayer**

Contributions may not be made to a taxpayer's RRSP after his or her death. Contributions may, however, still be made to a Spousal RRSP. Let's assume John dies in 2007 prior to having contributed any amount to his RRSP. His legal representative could contribute up to the amount of his "RRSP room" to a Spousal

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<sup>23</sup> As provided for by the formula contained in Income Tax Regulation 7308(3), the 1/27th is calculated as 1 / (90 - age of the individual at the beginning of the year), which in this case is 1 / (90-63).

<sup>24</sup> See special transitional rule applying for purposes of the "minimum amount" definition in subsection 146.3(1) of the ITA.

<sup>25</sup> See special transitional rule applying for purposes of the "minimum amount" definition in subsection 146.3(1) of the ITA.

<sup>26</sup> See paragraph 146(8.7)(d) of the ITA.

RRSP, with the amount of the contribution being deducted on John's terminal tax return. (Of course, the amount must be contributed to the Spousal RRSP prior to when it is required to mature, that is, before the end of the year in which the spouse (or common-law partner) has turned age 71.)

## VII. Retiring Allowance Rollovers

The ITA contains specific rules allowing taxpayers to transfer the "eligible" portion of a retiring allowance to an RRSP. The tax rules specifically require that the transfer be to the taxpayer's own RRSP.<sup>27</sup> The transfer cannot be to a Spousal RRSP.

The retiring allowance that the taxpayer receives may be in excess of what qualifies for a transfer to his or her own RRSP. This excess could be transferred to the taxpayer's own RRSP or a Spousal RRSP to the extent of the taxpayer's "RRSP room".

## VIII. Future Establishment of an IPP

IPPs are becoming increasingly popular, especially now that many professionals may incorporate. IPPs are typically set up recognizing both current and past service. (Of course, the past service must relate to a period of employment. Professionals could not set up past service for periods of self-employment.) Tax-assistance would be received twice if the plan member contributed to an RRSP and also earned a pension in the IPP for the same year. Thus, specific tax rules prevent the doubling of the tax assistance.

CRA approval needs to be obtained where the past service for the 1989 and later years is set up in the IPP. CRA needs to certify a Past Service Pension Adjustment (PSPA). The PSPA will be certified if there is sufficient "RRSP room", or if the room is slightly deficient (there is an \$8,000 window). If this is not the case, one of two things needs to happen. The prospective plan member can either withdraw an amount from their RRSP (this is referred to as a "qualifying withdrawal"<sup>28</sup>) and include it in his or her taxable income, or can transfer an amount from his or her RRSP to the IPP (this is referred to as a "qualifying transfer"<sup>29</sup>).

When we look at the "qualifying withdrawal" rules, there is a specific requirement that the withdrawal be "from a registered retirement savings plan under which the individual [the person for whom the past service is being provided] was the annuitant".<sup>30</sup> Also, when we look at the "qualifying transfer" rules that permit transfers from RRSPs to the IPP, these provide that the IPP to which the funds are transferred must be "for the benefit of the transferor".<sup>31</sup> As a result, neither contemplates amounts being withdrawn from a Spousal RRSP.

Thus, when advisors are dealing with incorporated professionals and others who may set up IPPs in the future, it may not be appropriate to contribute amounts to a Spousal RRSP. The advisor would want to be sure that there were sufficient funds in a regular RRSP (or certain registered vehicles from which a transfer could be made).

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<sup>27</sup> See subsection 60(j.1) of the ITA.

<sup>28</sup> See subsection 8307(3) of the Income Tax Act Regulations (Regulations).

<sup>29</sup> See subsection 8303(6) of the Regulations.

<sup>30</sup> See paragraph 8307(3)(a) of the Regulations.

<sup>31</sup> See subparagraph 8303(6)(a)(i) of the Regulations and paragraph 146(16)(a) of the ITA.

## **IX. Spousal RRSPs and the Home Buyer's Plan (HBP)**

The HBP is a special plan allowing the annuitants of an RRSP to withdraw \$20,000 on a non-taxable basis from the RRSP to buy or build a qualifying home.<sup>32</sup>

The annuitant of a Spousal RRSP can withdraw up to \$20,000 from the Spousal RRSP. The (contributing) taxpayer can also withdraw up to \$20,000 from his or her own RRSP. Thus, where a spouse (or common-law partner) does not have any "earned income", and could not contribute to a regular RRSP, a Spousal RRSP set up for him or her allows for a potential doubling of the access to the HBP.<sup>33</sup>

There is a special rule that looks at whether amounts were contributed to a particular Spousal RRSP during the 89-day period before the withdrawal under the HBP.<sup>34</sup> Let's assume that \$30,000 was contributed to a Spousal RRSP on July 1, 2007. Two months later \$20,000 is withdrawn from that Spousal RRSP, leaving a value of \$12,000 in that plan. The taxpayer will not be able to deduct the full amount contributed.

The amount that cannot be deducted is calculated as: Amounts contributed by you (and your spouse or common-law partner) to that Spousal RRSP in the 89-day period less Fair Market Value of the assets of that Spousal RRSP after the withdrawal. In our situation, a deduction will be denied for \$30,000 less \$12,000, or \$18,000.

Suffice it to say, care should be taken to avoid the application of the 89-day rule. A discussion of all of the rules (including rules relating to repayment) is beyond the scope of this document and professional advice should be sought in this regard.

## **X. Spousal RRSPs and Lifelong Learning Plan (LLP)**

The LLP is a program allowing an RRSP to be accessed to finance certain training or education.<sup>35</sup> An annuitant can withdraw up to \$10,000 per annum (up to \$20,000 in total each time the program is used) on a non-taxable basis to finance the training or education of a "student". Either the annuitant or his or her spouse (or common-law partner) must be the "student".

Let's assume that John wanted to enroll in a qualifying educational program. A total of \$10,000 per annum for this purpose could be withdrawn from a combination of his or his spouse's or common-law partner's RRSPs, including Spousal RRSPs. However, the combined amount withdrawn from all plans in the year cannot exceed \$10,000.

If John's common-law partner Nancy also enrolled in a qualifying educational program, another \$10,000 per annum could be withdrawn. As outlined above, this could be from a combination of plans.

In our example, John and Nancy are each limited to \$20,000 for each time the program is used.

Spousal RRSPs simply represent an additional source from which the required funds can be withdrawn. They do not provide for a doubling of the limit.

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<sup>32</sup> See section 146.01 of the ITA. CRA has also issued RC4135 – *Home Buyer's Plan (HBP)* (RC4135), which may be referenced for additional information.

<sup>33</sup> See page 7 of RC4135.

<sup>34</sup> See subparagraph 146(5.1)(a)(iv) of the ITA.

<sup>35</sup> See section 146.02 of the ITA. CRA has also issued RC4112 – *Life Long Learning (LLP)*, which may be referenced for additional information.

Again, the 89-day rule described in the HBP discussion applies and should be avoided. A discussion of all of the rules (including rules relating to repayment) is beyond the scope of this document and professional advice should be sought in this regard.

## **XI. The New Pension Splitting Rules**

The new Pension Splitting rules that are effective starting with the 2007 taxation year are causing taxpayers and advisors to assess whether Spousal RRSPs should still be used. For more information on Pension Splitting, refer to another item in the Taxing Issues series: *Pension Splitting – An Analysis of the Legislation* [PC 6147].

Prior to the introduction of these rules, a high-income taxpayer would make contributions to a Spousal RRSP. In Ontario, a taxpayer in the top tax bracket in 2007 could realize tax savings equal to 46.41% contribution. If the spouse (or common-law partner) withdrew the amounts when he or she was in the lowest tax bracket (and attribution did not apply), the withdrawals would be taxed at 21.55% (2007 tax rate assumed). Thus, the tax rate differential was 25%.

With the new Pension Splitting rules, a taxpayer who has “eligible pension income” could allocate up to 50% of this amount to their spouse (or common-law partner). The allocation is done at the time the tax returns are filed as part of the tax return filing process.<sup>36</sup> Where control of the assets is important, the loss of control that arises where amounts have been contributed to a Spousal RRSP is avoided.

“Eligible pension income” includes amounts that qualify as “pension income”, as that term is defined for purposes of claiming the \$2,000 Pension Credit. The annuitant of the RRSP will want to be sure that the manner in which these funds are accessed qualify for splitting.

In order to have “pension income”, the taxpayer must have turned age 65 in the year.<sup>37</sup> Lump sums withdrawn from a RRSP do not qualify. The taxpayer should instead acquire a registered annuity with the RRSP funds or should transfer the amounts to a RRIF. “Taxable amounts” (the “minimum amount” plus any excess) withdrawn from the RRIF will qualify.

If the couple requires funds, and the purpose of the Spousal RRSP is not to provide retirement income, tax savings could arise where amounts are contributed by a high-income taxpayer and withdrawn by the low-income spouse (or common-law partner). They will benefit from the tax savings provided by the difference in the tax rates, provided attribution is avoided. This strategy might be appropriate where one partner stays at home to rear children and the funds are needed for the family’s living expenses.

If, however, the purpose of a RRSP is to provide for retirement income, the value of the Spousal RRSP appears to have diminished, especially once age 65 is attained. A taxpayer could just as well contribute the amounts to his or her regular RRSP, and then save the taxes by pension splitting at age 65.

They are also of value where a taxpayer is older than 71 and can no longer contribute to his or own RRSP. This taxpayer could consider contributing to a younger spouse’s (or common-law partner’s) RRSP.

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<sup>36</sup> See definition of “eligible pension income” in subsection 60.03(1) of the ITA.

<sup>37</sup> See definition of “pension income” in subsection 118(7) of the ITA.

Spousal RRSPs also can play an important role where a couple plans to retire early, i.e., before 65. As stated above, pension splitting where the source is RRSPs, is not available prior to age 65 of the annuitant so spousal plans can provide the desired tax efficiency.

Spousal RRSPs also represent a last chance to save taxes, where an executor is able to use a deceased taxpayer's "RRSP room" to contribute to a Spousal RRSP.

We do remind advisors to proceed cautiously when an IPP could be established at some future point in time. Amounts in the Spousal RRSP cannot be withdrawn or transferred to the IPP as part of the process of setting up post-1989 past service.

## **XII. Summary**

RRSPs are a valued retirement tool. Even though the value of Spousal RRSPs has been diminished with the introduction of the Pension Splitting rules, there are situations in which they should still be considered. Financial planners will want to review the opportunities that the new Pension Splitting rules provide for their clients, and will want to assess whether new strategies are appropriate.

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