



Spousal RSP's

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(Are Two Incomes Better Than One?)

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The main objective of setting up a spousal RSP is to provide the family unit with two streams of income during retirement. Spousal RSPs present a simple means of splitting retirement income between spouses in an effort to equalize retirement income and minimize the family's tax bill.

The strategy of income splitting should be adopted due to the fact that we have a progressive tax system. In other words, the more income you earn the more tax you are to pay. Therefore, if we can utilize the rules of the Income Tax Act, hereinafter "the Act", to reallocate the family income, we can reduce the total tax bill for the family unit.

CREATION OF SPOUSAL RSP'S

In essence, a spousal RSP is a RSP which names your spouse rather than yourself as the "annuitant" or owner of the RSP, even though you have made the contribution.

Under the Act, there are basically three ways to get money into a spouse's RSP. The first is on the death of the taxpayer provided the surviving spouse is named as the beneficiary of the deceased's RSP or if the deceased's RSP proceeds are receivable by an estate, the estate and the spouse jointly elect that the amounts receivable by the estate are deemed to be received by the spouse. The second is on marriage breakdown if the couple is no longer living together. The third manner is simply to contribute to a spousal RSP based on "your" contribution room. Incidentally, for purposes of the Act, common-law partners of the same or opposite sex are treated identical to legally married spouses.

Let's examine the latter or third scenario in a little more depth. I stressed the issue that you can contribute to a spousal plan based on "your" contribution room. What the government is saying is that if you have, for example \$10,500 of RSP contribution room in a year, you are entitled to contribute all or a portion of this amount to a spousal plan and/or your own plan.

However, even though the Act permits one to transfer certain amounts such as the commuted value of pension benefits to your own Locked-In RSP they do not permit you to do this with a spousal plan. This also holds true for transferring a retiring allowance to a spousal RSP; it cannot be done.

When does a Spousal RSP make sense?

There are two main tax advantages of a spousal RSP. First, a spousal plan may enable a couple to split their retirement incomes, which in effect could create a smaller combined tax liability due to their lower marginal tax rates. Secondly, it would enable an older spouse, one that is over 69 and no longer eligible to contribute to their own RSP, to contribute to a spousal plan.

It must be stressed that a spouse age 70 or over can only contribute to a younger spouse's RSP if the older spouse has either a) earned income in the previous year and/or b) they have contribution room available. As well, the younger spouse must not be older than age 69 in the year of contribution.

TAXATION ISSUES

Income Attribution Rules

The Canada Customs and Revenue Agency (CCRA) has a set of nasty little rules that are called the attribution rules. These rules can result in RSP income being “attributed” back to the contributor. The income that was withdrawn from these plans would be then taxed in the hands of the contributor at his/her higher marginal tax rate, ouch! The net effect is that you would not have achieved the desired income splitting with this spousal contribution!

If the owner (i.e. annuitant) of the spousal plan withdraws funds from the plan during the year a spousal contribution was made or makes a withdrawal in any of the following two calendar years, the contributing spouse will have to pay the tax on the money withdrawn at his or her tax rate. The attribution of the withdrawal is limited to the total spousal RSP contributions during this three year period.

Basically, you need three years before you can withdraw the funds without any attribution back to the contributor, but three years does not necessarily equal three full calendar years. E.g. Wife makes last spousal RSP contribution on December 31, 2001 as early as January 1, 2004 her annuitant spouse can withdraw the funds from the spousal RSP with no attribution effect; net time period 2 years plus a day. Note that any further spousal RSP contributions during the remainder of 2004 will also be subject to the spousal attribution rules.

If the spousal plan contains contributions from both parties and the annuitant spouse wishes to de-register only part of the funds, there will be attribution back to the contributor if the three year time frame is not adhered to.

TAX PLANNING STRATEGIES

Now that you understand how the rules work, how about some creative planning to hopefully escape the attribution rules.

Can I Roll my Spousal RSP Into A Spousal RIF?

The attribution rules never apply if only minimum payments are withdrawn from a spousal RIF. Therefore, another common strategy is to roll the spousal RSP into a spousal RIF and then withdraw only the minimum annual payment. This strategy seems promising, but is hindered by the fact that the minimum payment in the first year of the RIF is zero! However, if you can arrange your affairs to convert the spousal RSP to a spousal RIF late in the year, your minimum payment will not be nil by January of the following year. If you decide to take out more than the minimum payment the attribution rules will apply if the three-year time period has not elapsed since the last contribution.

Spousal RSP and Regular RSP Commingled

What happens if a spousal and regular RSP with the same annuitant, are commingled? The answer is that the account will be identified as a spousal account. This may appear to be a problem due to the potential attribution concerns. However, the key concern is once again “When was the last contribution by the **non-annuitant spouse** made?”. If the last contribution was made more than 3 years ago then the attribution rules would not apply to this commingled account even though the account is labeled “spousal RSP”.

Furthermore, if there is attribution, the amounts attributable are limited to the amount that had been deposited by the contributor (not the annuitant). Also, even if the annuitant wants to take out only a portion of the funds in the commingled spousal RSP, the funds that are withdrawn first will always be those of the contributor that is not the annuitant.

Consider the following examples of both spouses contributing to one spousal RSP.

Spousal Plan (Contributions)

Year	X	Y (annuitant)
1	\$5000	\$4000
2	nil	\$3000
3	\$3000	\$2000
4	nil	\$5000
5	nil	-\$9000

If Y should decide to withdraw \$9000 in year 5, \$3000 of the \$9000 will be attributed back to X; the three-year rule was violated. This attribution could have been prevented if Y had waited until year 6 or had created a separate account for only Y's contributions.

By keeping spousal and personal RSP accounts separate, your spouse will be able to withdraw funds from their personal account without triggering the attribution rules. This will help in the de-registering of the RSP in periods of need. It is important to weigh the additional cost versus the added flexibility involved in creating more than one RSP account.

Do the attribution rules apply differently if I have two spousal plans?

If you have two spousal plans and one plan meets the attribution test and the other plan does not (violates the three-year rule) the attribution rules would still apply to either of the spousal accounts. However, this would not be the case if at the time of the withdrawal the contributor and the annuitant of the RSP plan were living separate and apart by reason of marriage breakdown.

Further, if either spouse should die or become a non-resident these rules would no longer be applicable. The collapsing of these plans would not trigger taxes at the contributor's tax rate; no attribution.

Can I transfer a retiring allowance to a spousal RSP that I am not the annuitant?

No you cannot. You can only transfer a retiring allowance to an RSP or Spousal RSP of which you are the annuitant.

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