Planning for RRSPs Beyond Today

BY BECKY WONG

For many of us still in the wealth accumulation stage, we were likely topping up or contributing to a registered retirement savings plan (RRSP) the past two months. Longer life expectancy today forces planning for retirement to be even more important. We also need to have a plan to pass on this potentially large asset in the event of death. What are the options available to help with minimizing the tax burden at death?

So what happens at death? According to the general rule, the fair market value of an RRSP at the time of death is included in the deceased person's income for that year and taxed at their marginal tax rate. Amounts paid from an RRSP upon the death of an annuitant is known as a "refund of premiums". This amount can be transferred directly or indirectly to a qualified beneficiary of the deceased annuitant.

Spouse or Common-law Partner

One of the most recognized and accepted option is to have our RRSPs rolled over to the RRSP of the deceased person's spouse. To transfer a refund of premiums to an RRSP, the qualified beneficiary must be 71 years old or younger at the end of the year the transfer is made. As such, the amount will be exempted from the deceased person's income and added to the income of the spouse or common-law partner. The issuer who receives the transferred funds will issue a receipt to the qualified beneficiary. The beneficiary can use the receipt to claim a deduction on his or her income tax return for the year the refund of premiums was received. This spousal roll over has resulted in deferring taxes until such time that the recipient makes a withdrawal.

Dependent Child or Grandchild

When a child or grandchild who is financially dependent on the deceased person at the time of death is designated the beneficiary of the RRSP, the amount paid can also be exempted from the deceased income in the year of death. The refund of premiums received by a financially dependent child or grandchild will be included in his or her income and since the child has little income, this is generally advantageous.

A child or grandchild is considered dependent if his or her income in the year preceding the death does not exceed the basic personal tax credit for that preceding taxation year ($11,327 for 2015). In addition, if the child or grandchild is a minor, the taxation of the RRSP can be spread over a number of years by purchasing a term certain annuity with a maximum term to age 18. The annuity payments will be taxed in the minor's hands up to age 18.

Infirm Dependent Child or Grandchild

In the case of a child or grandchild who is financially dependent because of a physical or mental impairment, the income threshold is the basic personal tax credit plus the disability amount tax credit resulting in a total amount of $19,226 for 2015. This recipient can transfer the taxable amount of the refund of premiums to his or her own RRSP, again, deferring its taxation until withdrawal.

The infirm child or grandchild may also choose to purchase a life annuity with the refund of premiums and the annuity payments will be taxed to the child or grandchild.

Since July 1, 2011, proceeds of a deceased annuitant's RRSP is permitted to be rolled to a registered disability savings plan (RDSP) of a financially dependent infirm child or grandchild. The maximum rollover amount into an RDSP is $200,000. All contributions and rollover amounts made to any RDSP of a beneficiary will reduce this amount. A grant will not be paid into the RDSP on amounts that are rolled over.

All of the above options can be facilitated on a partial roll over basis. It may make sense for the deceased annuitant to report some of the RRSP income if a capital loss is available. Tax losses dies with the deceased, hence, it may be advantageous to make use of it on the terminal return.

In conclusion, planning for RRSPs beyond today should consider several factors as a combination of options may be more appropriate for your specific circumstance. Tax rules on death can be complicated and seeking the advice of a tax accountant or financial advisor is prudent.

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