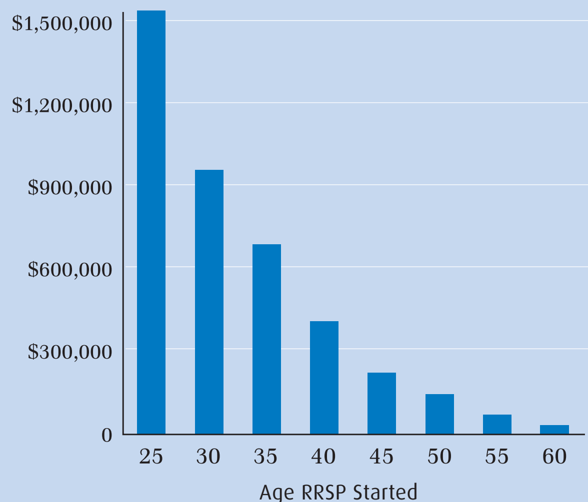
BMO NESBITT BURNS

RRSPs
Saving Tips & Strategies

A Registered Retirement Savings Plan (RRSP) continues to be the cornerstone of most retirement plans, particularly if you don't have a company pension plan. An RRSP is a tax-deferred plan designed to help you save for retirement. With an RRSP, contributions are tax deductible and once in the plan, continue to grow on a tax-deferred basis until the funds are withdrawn. Any funds removed from the RRSP are taxed in the year they are withdrawn. At retirement, the funds may be rolled into any of the RRSP maturity options where they continue to be tax sheltered, except for the amount of money taken out as income each year.

Start Early

Many people do not get serious about building their retirement assets until 10 or 15 years before they plan to retire. However, because of the tremendous impact that compound interest has on the growth of your RRSP, you should start your plan as early as possible, contributing as much and as often as possible. Let's compare the difference between starting your RRSP at age 30 and age 50. Assume that you contribute $5,000 each year until age 65 and earn 8% annually. Starting at age 50, you would accumulate $146,621 by the end of the year in which you turn age 65. By starting at age 30, you would build an RRSP worth $930,510 by age 65. Even though you would have contributed an additional $100,000 by starting 20 years earlier, your RRSP would have grown by an additional $683,889.

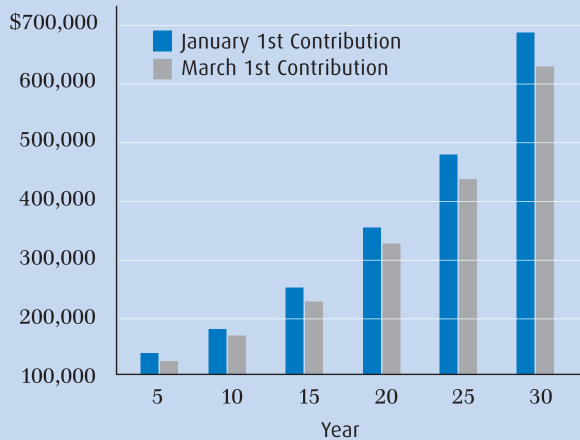


Contribute Early

Many RRSP owners make their contributions during the last two weeks of February. By doing so, you effectively lower the value of your RRSP. By contributing on January 1st rather than on March 1st of the following year, the money is in the RRSP for an additional 14 months. Compounding, especially over a number of years, can have a profound effect on the total value of the RRSP. As the graph shows, if you contributed $5,000 on January 1st each year for 30 years and earned an 8% rate of return, you would have $57,279 more in your RRSP than if you made your annual contribution on March 1st of the following year.

BMO Nesbitt Burns®
Making money make sense®

The Value of early RRSP Contributions



Contribute Longer

As long as you continue to have earned income or unused RRSP room, you may continue to contribute to your RRSP up to and including the end of the year in which you turn 71 years of age. RRSP contributions are deductible against any type of income including pension or investment income. Once you turn age 71, you have until the end of that year to mature your RRSP. However, if your spouse is still young enough to have an RRSP, you may contribute to a Spousal RRSP if you continue to have earned income or unused RRSP room. You would be entitled to the tax deduction for your contribution, even though you may no longer contribute to an RRSP for yourself.

Make an Early RRSP Contribution at Age 71

If you are still working at age 71, you will generate RRSP contribution room for the following year. Unfortunately, you can only take advantage of this contribution room if you make an early RRSP contribution.

Here's how it works. Let's assume that you turn age 71 this year, and that based on this year's earned income, you will be eligible to make a $10,000 RRSP contribution next year. Because you cannot have an RRSP next year, you can make an early contribution in December of this year. This will cause an over contribution which will attract a penalty tax of $80 for the month of December (1% x $8,000 since the first $2,000 of an over-contribution is not subject to the penalty tax).

On January 1st of next year, you will no longer be in a penalty position since new contribution room becomes available. You will be able to claim a $10,000 tax deduction on your next year's tax return and will have sheltered an additional $10,000 inside your RRSP. The benefit of the tax deduction, along with the continued tax-deferred growth in a Registered Retirement Income Fund (RRIF), or the increased annuity payment if the RRSP is used to purchase an annuity, should exceed the one month penalty tax.

Maximize Your Contributions

The ability to save with an RRSP is affected by many things, including the annual deduction limit, your earned income and your pension adjustment. The easiest way to find your RRSP deduction limit is to look it up on the Notice of Assessment that the Canada Revenue Agency (CRA) sends back to you after you file your income tax return each year. Here's how to verify that figure for yourself:

RRSP Deduction Limit

Step 1

Unused RRSP deduction room from previous years	**plus the lesser of:**	18 per cent of your prior year's earned income **– or –** the annual RRSP dollar contribution limit

Step 2 (if applicable)

- Deduct your previous year's Pension Adjustment (PA) and net Past Service Pension Adjustment (PSPA) or add any Pension Adjustment Reversal (PAR).

RRSP Dollar Contribution Limits

Year	Lesser of:	
2012	$22,970	or 18% of prior year's earned income
2013	$23,820	
2014	Indexed to inflation	

Contributing Securities to Your RRSP

Your RRSP contribution does not have to be made in cash. You may deposit any qualified RRSP investment you already own into your RRSP instead of cash – that is an "in-kind" contribution or transfer. You will need to report any capital gains accrued to the date of transfer on your tax return. Any capital loss accrued is denied for tax purposes. Qualified RRSP investments include Guaranteed Investment Certificates (GICs), Canada Savings Bonds, mutual funds, common and preferred shares, bonds (issued by corporations, provincial and federal governments).

Accumulate Contribution Room

Since RRSP contribution room for the current year is based on the previous year's earned income, you will be unable to make a RRSP contribution in the first year you begin working. So if you have children who are working part-time jobs, consider having them file an annual tax return even if they don't owe income tax. By filing a tax return, they will accumulate RRSP contribution room that can be carried forward and used when they eventually begin working full-time.

While the amounts may seem small, this strategy can produce significant results. If your child works throughout high school and university, they could easily accumulate $3,500 in RRSP contribution room. Assume that they begin working full-time at age 23, they could use their accumulated RRSP contribution room to make a contribution that year. Assuming the contribution earns an annual rate of return of 8%, their RRSP could be worth an additional $92,283 when they reach age 65. And perhaps more importantly, your children will develop good habits in saving for their retirement.

Transfer a Qualifying Retiring Allowance to Your RRSP

Most of us will change employers several times throughout our careers, at which time you may be offered a retiring allowance. Depending on the size of the retiring allowance, you may be able to transfer all or part of it directly into your RRSP to defer the immediate payment of income tax.

If the payment represents a *retiring allowance* (which is a defined term in the tax legislation) you can create additional RRSP contribution room equal to $2,000 for each year or part year of service with your employer before 1996, plus an additional $1,500 for years of service prior to 1989 for which you were not a member of a vested company pension plan or DPSP. This is in addition to your normal room which is calculated based on earned income.

There is a tremendous advantage to tax sheltering as much of your retiring allowance as possible in a RRSP, however this rollover can only be made to your own RRSP and not a Spousal RRSP. You have up to 60 days after the end of the year that you are paid your retiring allowance to make the RRSP contribution. To the extent that you have any unused normal RRSP contribution room, you can also use the funds from the retiring allowance to top up this contribution room.

Income Splitting with a Spousal RRSP

A Spousal RRSP is the same as a regular RRSP, except that a Spousal RRSP is registered in your spouse's name while you take full tax deduction for all the contributions you make as the contributing spouse in the plan. The primary benefit for establishing a Spousal RRSP is to allow for income splitting at some time in the future. This is accomplished since the assets in the Spousal RRSP are considered the property of the planholder (your spouse). Generally, when the funds are withdrawn from the plan, they are taxed at the planholder's marginal tax rate. So typically this strategy would be used when the planholder would otherwise have little retirement income, while the contributing spouse would have the majority of the couple's income.

Despite the opportunities created by the pension income-splitting rules, the use of a Spousal RRSP as an income-splitting tool may still be beneficial. Spousal RRSPs allow for additional income-splitting prior to age 65 and also provide a further

opportunity to increase the amount of income splitting beyond the 50% limitation allowed under the pension income-splitting rules.

Designate a Beneficiary for Your RRSP

A beneficiary designation is made in writing either directly on the RRSP application form, on a beneficiary change form, in a letter or in your Will, and can be changed only by the plan holder. In Quebec, beneficiary designations are made in your Will. You should review your beneficiary designation whenever there is a change in your personal circumstances such as marriage or divorce, death or a birth.

If you name a charity as the beneficiary of your RRSP, the payment will be considered a charitable donation and your estate will be entitled to a donation credit for the value of the plan. Although your estate will be taxable on the value of the plan, the donation credit should completely offset the tax owing on the value of the RRSP plan.

Please contact your BMO Nesbitt Burns Investment Advisor for more information and to discuss strategies to maximize your RRSP.

Note: Some terms are capitalized for purposes of greater clarity in the context of this discussion only.

September 2012

09/12-1290

® "BMO (M-bar Roundel symbol)" and "Making Money Make Sense" are registered trade-marks of Bank of Montreal, used under licence. ® "Nesbitt Burns" is a registered trade-mark of BMO Nesbitt Burns Inc.
The comments included in the publication are not intended to be a definitive analysis of tax law. The comments contained herein are general in nature and professional advice regarding an individual's particular tax position should be obtained in respect of any person's specific circumstances.
Member-Canadian Investor Protection Fund

Making money make sense®