



Registered Retirement Savings Plan

Registered Retirement Savings Plans (RRSPs) allow taxpayers to save taxes by making tax-deductible contributions toward their retirement while they are in their higher-taxed, income-producing years. They can defer the tax on the growth while they build their nest egg inside the plan and then withdraw the funds when they are in lower taxed, retirement years.

Contributions

An individual's Registered Retirement Savings Plan (RRSP) deduction limit is based on 18 per cent of the previous year's earned income less the individual's pension adjustment, up to the annual limit, which is currently \$13,500. This limit will increase to \$14,500 in 2004 and \$15,500 in 2005. After 2005, the limit will be indexed.

Unused contribution room is carried forward indefinitely. Contributions made in the current year or in the first 60 days of the following year can be deducted against the current year's income. However, all contributions made after the first 60 days of the current year or the first 60 days of the following year must be reported on the current year's tax return. For example, any RRSP contributions made in February 2002 must be reported on the 2001 tax return, even if they are not claimed until 2002 or a later year. The taxpayer can choose to carry forward all or part of the contributions indefinitely to be deducted against income in a future year. Schedule 7 of the Personal Income Tax and Benefit Return tracks undeducted contributions.

Foreign property

Up to 30 per cent of the book value of an RRSP can be invested in foreign property. Foreign property of an RRSP includes property that is located outside of Canada, such as shares listed on foreign stock exchanges. It also includes mutual funds managed by Canadian mutual fund companies where more than 30 per cent of the book value of the mutual fund is invested in foreign property, as with foreign equity mutual funds.

If more than 30 per cent of the book value of the RRSP is invested in foreign property, then the RRSP will be subject to a penalty tax of one per cent per month on the excess foreign property. The plan administrator will assess the penalty tax and remit it to the Canada Customs and Revenue Agency (CCRA).

Certain investments may allow an investor to increase his or her foreign exposure within his or her RRSP, without exceeding the foreign property limit. One such investment is the 100 per cent RSP fund, which uses derivatives to mirror the performance of a foreign fund without being classified as foreign property itself. For more information, please refer to our *100 per cent RSP Funds* tax & estate info page.

Earned income includes:

- Income from employment
- Net rental income
- Net business income
- Certain support payments received
- CPP/QPP disability

Earned income does not include:

- RRSP/RRIF income
- Interest income
- Capital gains
- Dividends
- CPP/QPP (other than disability)
- Old Age Security
- Workers' Compensation



Maturity of an RRSP

An RRSP matures at the end of the year in which the annuitant turns 69. At that time, the annuitant has three options:

- Convert the RRSP to a Registered Retirement Income Fund (RRIF)
- Purchase an annuity
- Cash in the RRSP

For a discussion of these options, please refer to our *Registered Retirement Income Funds* tax & estate info page.

Spousal or common-law partner RRSPs

Contributions can also be made to an RRSP for one's spouse or common-law partner (a common-law partner includes both opposite-sex and same-sex partners), as this can provide an opportunity for income splitting upon retirement. The contributions are deductible by the contributor based on his or her contribution room. Amounts withdrawn are taxable to the annuitant. The annuitant is the owner of the spousal or common-law partner RRSP assets and has full control over the plan.

When income is withdrawn from a spousal or common-law partner RRSP, it will attribute back to the contributing spouse or common-law partner. The attribution will be up to the amount of the contributions made to all spousal or common-law partner RRSPs in the same calendar year as the withdrawal and the previous two calendar years.

Example

In March 2000, John contributed \$5,000 to a spousal RRSP for his wife, Lisa. Therefore, any RRSP withdrawals by Lisa to a total of \$5,000 out of any spousal plan in 2000, 2001 and/or 2002 will be attributed to John and taxed in his hands. However, assuming no further contributions are made, Lisa can withdraw the funds in 2003 and the withdrawal will be taxable to her.

If the spouses or common-law partners are living separate and apart because of a breakdown of their marriage or common-law relationship, then the annuitant will be responsible for the tax on any withdrawals from the spousal or common-law partner RRSP. A spousal or common-law partner RRSP must remain a spousal or common-law partner plan, even after divorce, until the death of the contributing spouse or common-law partner.

An individual over 69 who continues to generate earned income (and therefore RRSP contribution room) and who has a spouse or common-law partner under age 69 can make contributions to a spousal or common-law partner RRSP under which his or her spouse or common-law partner is the annuitant.



Overcontributions

An individual can exceed his or her contribution limit by \$2,000 at any time. However, persons under the age of 18 are not allowed to overcontribute. There is a penalty tax of one per cent per month of the contributions in excess of the \$2,000 overcontribution limit that begins as of the end of the first month when this limit had been exceeded. CCRA Form T1-OVP *Individual Income Tax Return for RRSP Excess Contributions* is used to calculate and remit the overcontribution penalty to the CCRA. This penalty is due by March 31 of the year following the overcontribution. If the overcontributions are withdrawn in the year they are made, or the year after they are made, they can generally be withdrawn without withholding tax using CCRA Form T3012A *Tax Deduction Waiver on a Refund of Your Undeducted RRSP Contributions Made in ____*. Once that time limit has passed, the overcontributions will be taxable when withdrawn, even if no deduction is ever taken for the contribution. The contributor can continue to carry the contribution forward as an undeducted contribution and deduct it in the future if contribution room is generated.

Making a final RRSP (over)contribution

An individual can also overcontribute to his or her RRSP before the end of the year in which he or she turns 69, and before transferring the RRSP to a RRIF. Provided the individual has earned income in the year in which he or she turns 69, RRSP contribution room will be generated for the following year. As a result, in the new year overcontribution penalties will cease and the contributor will be able to deduct the contribution.

Example

Hank had \$150,000 of earned income in 2002, which generates \$13,500 of RRSP contribution room for 2003. He turned 69 in 2002. However, in December 2002, prior to converting his RRSP to a RRIF, he overcontributed \$13,500 to his RRSP. His overcontribution penalty for the month of December is one per cent of the amount of the overcontribution in excess of the \$2,000 lifetime overcontribution limit, or $(\$13,500 - \$2,000) \times 1 \text{ per cent} = \115 . In January 2003 the new RRSP contribution room will become available and Hank will no longer be considered to be overcontributed, and will no longer be subject to penalty tax. He will be able to deduct the contribution in 2003 or in a future year. Assuming a tax rate of 45 per cent, the deduction will result in a tax savings of \$6,075. After considering the overcontribution penalty, Hank is still ahead by \$5,960 ($\$6,075 - \115).



Withdrawals

Amounts withdrawn from an RRSP are taxable as income when they are received. Tax is withheld by the RRSP administrator and will be applied towards the annuitant's taxes when he or she files his or her annual tax return. Taxes are withheld based on the following schedule:

Amount of withdrawal	All provinces except Quebec	Quebec
Up to \$5,000	10%	21%
\$5,000.01 - \$15,000	20%	30%
\$15,000.01 and above	30%	35%

A first time homebuyer, and his or her spouse or common-law partner, can withdraw up to \$20,000 each of RRSP funds to purchase a qualifying home under the federal Home Buyers' Plan. Up to \$20,000 can also be withdrawn to fund the annuitant's or the annuitant's spouse's or common-law partner's post-secondary education under the federal Lifelong Learning Plan. In both cases, there is no withholding tax on the redemption and the withdrawal is not taxable when withdrawn. The client has the choice of repaying the withdrawal or taking it into income over a number of years. For more information, please refer to our *Home Buyers' Plan* and *Lifelong Learning Plan* tax & estate info pages.

Transfers

Full transfers from one RRSP or RRIF to another RRSP or RRIF for the same annuitant can be done at the adjusted cost base and without withholding tax.

Transfers from investment ("open") accounts into RRSPs are deemed dispositions and occur at the fair market value, possibly resulting in a capital gain at the time of transfer. Any capital loss resulting from the transfer would be denied. A contribution receipt will generally be issued for the fair market value of the property transferred into the RRSP. However, if property with an equivalent fair market value is simultaneously being transferred out of the RRSP (sometimes referred to as a "swap"), then a contribution receipt will not be issued for the value of the property being transferred in and a T4RSP receipt will not be issued for the value of the property being transferred out.

Certain pension plan and retiring allowance transfers result in RRSP contribution receipts, however they may or may not use up RRSP contribution room. For more information, please refer to our Retiring Allowances tax & estate info page.

Death

The fair market value (FMV) of an RRSP is normally included in the deceased's income in the year of death. However, if the annuitant's spouse or common-law partner or financially dependent child or grandchild is named as a beneficiary of the RRSP (either directly or indirectly via the will), then the amount received by that beneficiary may qualify as a refund of premiums, which is eligible for special treatment.



If the deceased's spouse or common-law partner is named as the beneficiary, then the value of the RRSP will be taxable to the beneficiary, rather than to the deceased. The spouse or common-law partner generally has the option of transferring the refund of premiums to his or her own RRSP or RRIF, which will generally offset the income inclusion from the deceased's RRSP.

The value of an RRSP that is included in the deceased's income at death can be reduced if it is being transferred as a refund of premiums to a beneficiary who is a financially dependent child or grandchild. A (grand)child is considered financially dependent if his or her income in the year prior to the year of the annuitant's death does not exceed the basic personal exemption amount (approximately \$7,600 federally in 2002). In order to qualify for refund of premiums treatment, a grandchild must have been financially dependent on the deceased annuitant. If the beneficiary is a financially dependent minor, the refund of premiums can be used to purchase an annuity for the (grand)child to age 18. If the beneficiary is financially dependent and disabled, then he or she can transfer the refund of premiums into his or her own RRSP or RRIF.

If the estate is named as the RRSP beneficiary, and the spouse, common-law partner or financially dependent child or grandchild receives the RRSP property as a beneficiary of the estate, the legal representative of the estate and the beneficiary can jointly elect to treat the amount as if it had been transferred directly to the beneficiary. This will preserve the refund of premiums treatment.

Where the estate is named as the RRSP beneficiary (or no beneficiary designation is made on the RRSP), the RRSP assets may be subject to probate taxes, where applicable. Naming the beneficiary(ies) directly on the RRSP, rather than in the will, can save probate taxes (in provinces where applicable). The assets will transfer directly to the beneficiary designated on the plan. The charitable donation tax credit is also available to the deceased on donations made when charities are named directly as beneficiaries on RRSPs.

Contributions cannot be made to an RRSP on which the annuitant is deceased. However, if the deceased taxpayer has a surviving spouse or common law partner, contributions can be made by the estate to the surviving spouse's or common-law partner's spousal or common-law partner RRSP based on the deceased's remaining RRSP contribution limit at the time of death. The deduction can be taken on the deceased's terminal tax return.

For more information please see our *Death and Taxes and Probate Planning to Minimize Estate Costs* tax & estate info pages.



Locked-in Plans

Locked-in RRSPs and Locked-in Retirement Accounts (LIRAs) are RRSPs that are “locked-in” under federal or provincial pension legislation. They can only receive funds by way of transfer from a pension plan. The funds are generally locked into the plan until the annuitant reaches an age determined by the governing pension legislation or originating pension plan, often 55. Any time between that point and maturity, the funds can be transferred to a locked-in Registered Retirement Income Fund (LRIF) or a Life Income Fund (LIF), depending on the legislation. LRIFs and LIFs require the annuitant to withdraw retirement income, up to an annual maximum determined by pension legislation. In some cases, for example due to financial hardship or shortened life expectancy, the annuitant may be able to access the locked-in funds.

Minors

Minors are permitted to have RRSPs. Even if a child does not have to pay taxes, filing a tax return will create RRSP contribution room in respect of any earned income. As discussed earlier, persons under the age of 18 are not permitted to make the \$2,000 overcontribution. Contributions that are made into a child’s RRSP in respect of earned income but are not immediately deducted, for example because the child does not need the deduction in the year of contribution in order to receive a full tax refund, may be carried forward indefinitely and deducted in a future year to reduce taxable income.

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