Registered Education Savings Plans Overview

Registered Education Savings Plans (RESPs) were designed to assist in saving for a child's post-secondary education. Contributions to an RESP are not tax-deductible; however, the investment income that is produced in the plan is tax-sheltered until money is withdrawn to fund the child's education. The investment income is then fully taxable as regular income in the hands of the beneficiary (regardless of how much income was produced as a result of dividends or capital gains). The taxes payable on a withdrawal from the RESP can be minimal, assuming the beneficiary has little or no other income at the time of the withdrawal.

At one time there were many restrictions on the use of RESP investment income that often outweighed the benefits of the tax deferral. With legislative changes in 1998 and, more recently, 2007, it is now a more attractive choice for education savings.

Subscriber

An RESP is established by a subscriber. This is the individual who enters into a contract with an RESP provider.

A married couple or common-law partners (hereinafter collectively referred to as the "Partner(s)") may be joint subscribers. The social insurance numbers (SIN) of all subscribers are required to open an RESP account.

Planning Point:
In most circumstances, it is beneficial for an RESP to be made joint with a Partner. If the beneficiaries do not pursue post-secondary education, the subscribers can transfer the Accumulated Income Payments (AIPs) to either or both Partner's Registered Savings Plans, based on available contribution room.

Generally, a subscriber on an RESP cannot be changed, except in the following situations:

- Death of subscriber - RESP assets are disposed of as per the deceased subscriber's Will. If the Will designates someone to carry on with the RESP, this new designate becomes the successor subscriber and is liable for over-contributions.
- Marriage breakdown - In the event of a marriage breakdown, a spouse or former spouse who acquires the subscriber's rights under the RESP may replace the original subscriber.

Note also that you can transfer an RESP to a new RESP with a different subscriber, but the same beneficiary. For example, a grandmother who has an RESP for a granddaughter can transfer this plan to her daughter's plan for the same child.

Beneficiary & Plan Types

An RESP can have either a single beneficiary or multiple beneficiaries. The beneficiary's SIN is also required to open the account.

There are three general types of RESPs: Individual Plans, Family Plans and Group Plans. However, TD Wealth only offers Family Plans.

Features of an **Individual Plan** include:

- The Plan can have only one beneficiary.
- The Beneficiary does not have to be related to the subscriber.
- The Beneficiary can be over 21 when named.
- Contributions to this plan can be made up to the end of the 21st year after the plan has been opened.

Tip: A subscriber may even set up a single-beneficiary RESP for himself/herself if planning to pursue post-secondary education in the future.

A **Family Plan** differs in that:

- These plans can have more than one beneficiary.
- The beneficiaries must be related by blood relationship or adoption to each living subscriber, or have been connected to a deceased original subscriber.
- Each beneficiary must be under 21 when named.
- Beneficiaries may include the subscriber's children, brothers, sisters, grandchildren or great grandchildren.
- Contributions for a beneficiary of a family plan can only be made until the year the beneficiary turns 21 years of age.

A **Group Plan** is one that**:**

- Operates on a pooling principle where the beneficiary named under a contract by a subscriber will receive Educational Assistance Payments when enrolled in a qualifying program, but if the beneficiary fails to qualify for payment, the earnings are distributed among other beneficiaries of the same age who do qualify.
- As the contributions are pooled, the contributor usually has no say in how the funds are invested.
- Is typically restrictive. Plans vary, so it is important to understand the terms before pursuing this type of RESP contract.

Beneficiary Change

The beneficiary of an RESP can be changed as long as the term of the plan permits it. (Historically, many group plans do not allow for substitution.)

Tax consequences:

- When one RESP beneficiary is replaced with another beneficiary, CRA considers the contributions for the former beneficiary as being made for the new beneficiary on the date they were made originally. If the new beneficiary is already the beneficiary under another RESP, this may create an over-contribution, resulting in penalties.
- This rule does not apply where the new beneficiary is a brother or sister of the former beneficiary and is under 21 years of age; or if the beneficiaries are connected by blood relationship or adoption to an original subscriber of the RESP, and both are less than 21 years of age. In these situations, CRA does not include the contributions made for the former beneficiary when determining whether the new beneficiary's annual or lifetime contribution limit has been exceeded.

Canada Education Savings Grant (CESG) repayment:

- If the beneficiary of an individual plan changes, the CESG for the former beneficiary must be repaid to the government, unless the replacement beneficiary is the brother or sister of the former beneficiary; or if they are both connected to the subscriber by blood or adoption.

For details on CESG repayment in the event that a beneficiary of a family plan does not pursue post-secondary education, see related article "CESG–The Benefit of Registered Education Savings Plans".

Plan Duration

An RESP must be fully paid out within 35 years after being established (40 years in the case of a beneficiary who is mentally or physically infirm). Income generated in the plan cannot be tax sheltered beyond this time period.

If the RESP is a 'merged' plan (the result of combining more than one RESP), it must be paid out based on the date the earliest plan was established.

Planning Point: For Family Plan beneficiaries who are widespread in age, separate accounts should be opened to ensure that the plan is still available when the youngest pursues post-secondary school.

Contributions

Contributions to an RESP:

- can be made over a 31-year period (35 years for a beneficiary with physical or mental infirmity)
- belong to the subscribers
- are not tax deductible
- are not allowed if the beneficiary becomes a non-resident

The 2007 Federal budget removed the $4,000 annual contribution limit and increased the overall lifetime limit from $42,000 to $50,000. Accordingly, subscribers now have the option to make one large lump-sum contribution to an RESP and enjoy tax-free growth on the funds until they are withdrawn.

However, the CESG will only apply to the first $2,500 of an annual contribution if there is no unused CESG carry forward from a prior year. Where there is carry forward room available, the maximum CESG for a year will increase to $1,000.

A cost-benefit analysis should be performed to evaluate whether it is worthwhile forgoing the CESG payments in exchange for the immediate tax-sheltering of a lump-sum payment into an RESP.

Excess contributions to an RESP (over $50,000 per beneficiary) are subject to a 1% per month penalty for the excess amount contributed.

Where there are multiple beneficiaries:

When an RESP has multiple beneficiaries, there is a pre-determined split establishing how to allocate the contributions. In a situation where one beneficiary begins their post-secondary education before another, the subscriber needs to change the allocation in savings.

Mary has two children, Sam and Ashley, who are 4 years apart in age. When Mary established an RESP for the children she had allocated the contribution split to be 50-50. The CESG deposited to the account annually was also allocated as such. Sam is now 18 and will be attending university this year. Mary will no longer contribute to the plan for Sam; but she will continue making contributions to the RESP for Ashley for another 4 years. As a result, Mary needs to change the allocation of savings from the previous 50-50 split between both children, by designating 100% of the contributions to Ashley. If Mary does not change the savings allocation, Ashley may not receive full entitlement to the CESG.

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