

Advanced Pension Income Splitting FAQ's

Starting in 2007, new tax rules permit a taxpayer to transfer up to 50% of their income eligible for the pension income credit to their spouse or common-law partner (hereinafter collectively referred to as the "Partner") by filing a joint election on or before the due date of their income tax returns. This has introduced a new planning opportunity for Canadians but has also prompted a lot of questions. For a discussion of the general rules as they relate to pension income splitting, please refer to the article "Pension Income Splitting". In this article, we seek to provide answers to some frequently asked questions.

Does my Partner have to be 65 years or over for me to split my Registered Retirement Income Fund (RIF) income with them?

So long as you (the pensioner) are 65 or over, you are not prevented from splitting RIF income with your Partner because of the age of your Partner. Therefore,

- If you are 65 or older, you can split RIF income with your younger Partner.
- However, if you are not yet 65, you cannot split RIF income with your Partner even if your Partner is older than 65.

If a pensioner has separated from their spouse and entered into a common-law relationship with another person during the year, is he or she permitted to split pension income with both the spouse (since technically they are still married) and the common-law partner?

A pensioner is only allowed to file one joint election for a particular taxation year. This is specifically provided in the *Income Tax Act* (in sub-section 60.03(3)). Thus, while a pensioner might have both a spouse and a common-law partner within the year, they may have only one pension transferee for that year.

Is income from an Individual Pension Plan (IPP) eligible for pension income splitting?

An IPP is a form of registered defined benefit pension plan, consequently income from an IPP is treated the same way as a regular company pension plan for the purpose of the pension income credit and pension income splitting.

Is income from a foreign pension plan eligible for pension income splitting?

In general, foreign pension income received by a Canadian resident is subject to tax in Canada in the same way as private pensions received from a Canadian source, and would qualify for the pension income credit. Any amount of a foreign pension that is not taxable in Canada because of a tax treaty, and income from a United States individual retirement account (IRA), are not eligible for the pension income amount and therefore not eligible for pension income splitting.

Is there a dollar limit to the amount of pension income that can be transferred between Partners?

No dollar limit is imposed. The only restriction is that a pensioner may not allocate more than 50% of his or her eligible pension income in a year to his or her Partner.

Note however that for retired executives who receive income from their basic pension plan as well as from an executive benefit plan (representing the top-up amounts), only the portion representing basic pension income is eligible for pension income splitting. The amounts from the respective plans are typically reported in separate T4A slips and so should be easily distinguished.

If one Partner dies during the year, is pension income splitting permitted for that year?

Yes, a pensioner and their Partner can file a joint election to split the pensioner's eligible pension income received in the year if both the transferor and transferee Partner are resident in Canada at the end of the calendar year or, in the case of death, on the date of death.

Example:

Lee receives \$5,000 defined benefit pension income each month. His partner Ali has little income and is therefore in a much lower tax bracket.

Scenario One – Lee dies on June 1st having received \$30,000 of eligible pension income up to that date. 50% of the \$30,000 received can be transferred from Lee to Ali.

Scenario Two – Ali dies on June 1st. Lee receives a total of \$60,000 of eligible pension income for the year. The total eligible pension income of \$60,000 has to be prorated by the number of months during which the marital relationship existed, therefore Lee can split 6 months of pension income (i.e. \$30,000) with Ali (the month of Ali's death counts as a full month). Therefore, the split-pension amount is \$15,000.

Can the pension income amount be transferred between Partners?

If your Partner does not need to claim some or all of certain non-refundable tax credits to reduce their federal tax to zero, you may be able to transfer those unused amounts to your return. Such amounts include the age credit as well as the pension income credit.

Is there any benefit in making the joint election to split pension income with my Partner if we are in the same tax bracket?

There are two possible ways to benefit from pension income splitting:

- If the transferee Partner is in a lower tax bracket than the transferor Partner, then pension income splitting will result in lower overall taxes.
- If the transferee Partner does not already have income of his or her own that is eligible for claiming the pension income credit, and he or she is 65 or over at the end of the year, then by virtue of the eligible pension income transferred from the transferor Partner, the transferee Partner can make use of the \$2,000 pension income credit.

These two considerations should be borne in mind in deciding how much (if any) pension income should be transferred from one Partner to another where both Partners are in the same tax bracket. If both Partners are already fully utilizing the \$2,000 pension income credit, there is probably no benefit in making a transfer. However, if one Partner does not have any eligible pension income of their own, then there may still be an advantage to transferring at least enough eligible pension income for the other Partner to fully utilize the \$2,000 pension income credit.

Are there instances when pension income splitting is not a good idea?

There are circumstances where pension income splitting between Partners can have more negative effects than positive.

One obvious situation is where as a result of the pension income transfer, the lower income Partner's income exceeds the threshold level for Old Age Security.

Another instance is where both Partners are taxable and one of them is claiming medical expenses. Since medical expense claims are reduced by 3% of the taxpayer's net income, there is a possibility that in such an instance the transfer of pension income could reduce or eliminate a claim for medical expenses. (However, if one of the Partners has no pension income, transferring just enough for him or her to claim the full pension income amount may still be beneficial.)



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Revised 04/01/2012