TD Wealth

Spousal Registered Retirement Savings Plans (RSPs)

A spousal RSP is a type of registered plan to which the annuitant's spouse or common-law partner (hereinafter collectively referred to as the "Partner") makes the contributions. The amounts that can be contributed to the spousal RSP are subject to the personal RSP limit of the contributing Partner as stated on their Notice of Assessment.

Contributing to a spousal RSP allows the contributor to obtain a deduction from his or her taxable income. With proper planning, the funds withdrawn from the spousal plan will be included in the income of the annuitant and may be taxed at a lower rate. However, withdrawals may be subject to Canada Revenue Agency's (CRA's) three-year attribution rule (see below).

This article discusses the planning strategies available by using a spousal RSP, namely: the ability to make RSP contributions after the age 71 limit, funding pension buybacks, and making an RSP contribution on behalf of a deceased contributor.

Withdrawals from a Spousal RSP & the 3-Year Attribution Rule

Withdrawals from a spousal RSP are generally subject to CRA's three-year attribution rule. If the annuitant withdraws funds from a spousal plan and there has been a contribution to any spousal RSP in the last three calendar years, then the contributing Partner will be taxed on that withdrawal, up to the amount he or she contributed to all spousal RSPs within the 3-year period.

- For spousal Retirement Income Funds (RIFs), the three-year attribution rule only applies on withdrawals above the annual minimum payment.
- The three-year attribution rule does not apply if the Partners are separated or divorced, or if the contributing Partner is deceased.

Here is an example of how the attribution rules work (see chart below):

Gaby and Ali are married. Gaby intends to withdraw $2,000 from her spousal RSP in the current year. In the first scenario, the full $2,000 is taxed in Gaby's hands because there have been no contributions in the year of withdrawal or the two previous years. Conversely, in scenario 4, the entire $2,000 is attributed back to Ali because there was a contribution in the year of withdrawal and each of the prior three years.

	Years in which contributions were made				Taxable Income reported by	
	Current Year	Prior Year	Two Calendar Years Ago	Three Calendar Years Ago	Ali (contributor)	Gaby (annuitant)
Scenario 1	$0	$0	$0	$1,000	$0	$2,000
Scenario 2	$0	$0	$1,000	$1,000	$1,000	$1,000
Scenario 3	$0	$1,000	$1,000	$1,000	$2,000	$0
Scenario 4	$1,000	$1,000	$1,000	$1,000	$2,000	$0

The scenarios in the preceding table illustrate that a couple can effectively split income by using spousal RSPs provided they wait 24 to 36 months after the last contribution to withdraw funds from any spousal plan.

Whenever funds are withdrawn from a spousal RSP, CRA requires the annuitant to complete Form T2205 *“Amounts from a Spousal or Common-law partner RRSP or RRIF to Include in Income”* and attach a copy to the contributing Partner’s tax return. This form determines how much of the withdrawal to attribute back to the contributing Partner. Accurate records and contribution receipts should be maintained.

Planning your withdrawal

If funds are to be withdrawn from a spousal plan, then contribution dates become a key factor in determining if attribution rules apply. For this reason, it is preferable that contributions to spousal plans be made late in the year instead of postponing them until January or February of the following year. For example, a contribution made on December 31, 2011, with no subsequent contributions, will be available for withdrawal without attribution on January 1, 2014. However, a contribution made only 2 days later, on January 2, 2012, would only be available for withdrawal free of attribution on January 1, 2015.

Income Splitting – Tax Savings through a Spousal RSP

A spousal RSP can also reduce household taxes during retirement through income splitting. When deciding whether to contribute to a spousal RSP, both individuals should attempt to estimate their incomes from all sources during retirement. The goal is to equalize both incomes in order to minimize the taxes during retirement.

In the following example, Couple B used a spousal plan and saved over $3,500 in annual taxes over Couple A with the same pre-tax household income. (We are assuming that the pension income splitting provisions do not apply in this case, e.g. the retirement income is not eligible pension income because the contributing Partner is under the age of 65).

No spousal RSP	**Partner 1**	**Partner 2**	**Total**
Couple A			
Retirement Income (pre-tax)	$90,000	$10,000	$100,000
Retirement Income (after-tax)	$67,500	$10,000	$77,500
Average tax rate	25.00%	0.00%	22.50%
With Spousal RSP	**Contributing Partner**	**Annuitant Partner**	**Total**
Couple B			
Retirement Income (pre-tax)	$50,000	$50,000	$100,000
Retirement Income (after-tax)	$40,500	$40,500	$81,000
Average tax rate	19.00%	19.00%	19.00%
Tax savings	**$81,000 - $77,500 = $3,500**		

It should be noted that a higher income at retirement may affect eligibility for the age credit and can also trigger the OAS clawback.

As a result of legislative changes in 2007 under the Tax Fairness Plan, the government now permits a Canadian resident who receives eligible pension income to allocate up to one-half of such income to his or her Partner, thereby reducing total household taxes. This change has reduced the importance of the spousal RSP as an income-splitting mechanism for retired couples who are in different tax brackets. Notwithstanding the ability to split eligible pension income; a spousal RSP still has an important role to play in retirement planning in the following situations:

1. Splitting income prior to age 65 if you do not have a registered pension plan (RPP).
2. Allocating more than 50% of your retirement income to your Partner.
3. Making RSP contributions beyond age 71 as long as you have a Partner who is younger than 71 years old.
4. Doubling Home Buyers Plan withdrawals.

Age 71 Limit

December 31 of the year the contributor turns 71 year old is that last day they may contribute to their RSPs. They must then either: withdraw them, transfer them to a RRIF, or use them to purchase an annuity. The advantage of a spousal plan is that it will only mature when the annuitant is age 71. If the contributor is older than age 71 and has earned income (i.e. self-employment income, rental income etc.), an RSP contribution can be made to the spousal plan to take advantage of the tax deduction as long as the annuitant is younger than age 71.

Pension Buybacks

Spousal proceeds can also be used to fund a pension buyback for the spousal plan annuitant. CRA's attribution rules do not apply on contributions made to a spousal plan that are subsequently transferred to a pension plan.

RSP Contribution in the Year of Death

Spousal plans can also be a useful vehicle in the year of death of the contributor. If the deceased had available RSP contribution room, a final RSP contribution can only be made in the year of death into a spousal plan so long as the surviving Partner is 71 or younger. No previous spousal plan needs to exist. The surviving Partner in conjunction with the executor can open a spousal RSP and make the contribution on the deceased's behalf. The regular RSP contribution deadline applies to this type of contribution (i.e. 60 days after year end).

Consolidating Personal & Spousal RSP Plans

If an individual RSP and a spousal RSP are combined, the combined RSP is considered to be a spousal RSP, and therefore the 3-year attribution rules will apply on withdrawals.

Retiring Allowance

CRA does not allow the rollover of an eligible retiring allowance (i.e. payment received upon leaving employment or upon retirement after long service) directly into a spousal plan.

However, if the recipient has available RSP contribution room, then the portion of the severance package that is ineligible (i.e. taxable) can be contributed to a spousal plan.

Louis received a retiring allowance of $30,000. He has unused RSP contribution room of $5,000. It has been determined that Louis is eligible to rollover $20,000 of his retiring allowance, with the remaining $10,000 taken as cash (fully taxed). Louis can roll the $20,000 amount into his personal RSP (with no effect on contribution room). He cannot rollover the $20,000 into a spousal RSP, but because Louis has unused contribution room, he can choose to contribute up to $5,000 (from the $10,000 cash portion) to a spousal RSP, thereby sheltering part of the otherwise taxable portion of the retiring allowance.

Removing a Spousal Designation

CRA rules permit an RSP/RIF issuer to remove the spousal designation from a spousal RSP or RIF on the death of the contributing Partner, as well as on the breakdown of marriage or common-law relationship between the contributor and the annuitant.

Three conditions must be met when requesting to remove the “spousal” designation on the breakdown of marriage (or common-law relationship):

1. Proof of separation caused by marital breakdown – the annuitant must provide the issuer of the RSP or RIF with a written statement that he or she is not living with the contributor.
2. No contributions – there must be no Partner contributions to any of the annuitant’s RSPs (held with any issuer) for the year of the request and the previous two years.
3. No withdrawals – there must be no withdrawal from the spousal RSP during the year of the request. In the case of a spousal RIF, no more than the minimum amount must be withdrawn.

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