RSP Over-contributions

The amount you can contribute to your registered retirement savings plan (RSP) (or your spouse or common-law partner's RSP) for a given tax year is determined by your RSP deduction limit. This is often called your "contribution room". Amounts that are contributed above this limit are often referred to as over-contributions. Aside from the fact that such an over-contribution amount is not deductible from your taxable income, there are tax implications if your over-contribution exceeds $2,000. This article will review the implications of excess contributions and how to deal with them.

What constitutes "excess contributions"?

You have "excess contributions" in your RSP (or spousal or common-law partner's RSP of which you are the contributor) if the sum of your unused contributions from prior years and your current calendar year contributions exceed your RSP deduction limit as shown on your latest Notice of Assessment (NOA), Notice of Reassessment (NORA), or Form T1028, plus $2,000.

Distinguish between "unused contributions" and "excess contributions"

"Unused contributions" simply refers to RSP contributions that have not been used as a deduction. You can determine your unused contributions from previous years by checking your latest NOA, NORA, Form T1028, online through the Canada Revenue Agency's (CRA) "My Account" portal, or by calling CRA's Tax Information Phone Service. New unused contributions should be reported by filing Schedule 7 with your tax return.

"Excess contributions", exist if your unused contributions from prior years plus your current calendar year contributions exceed your RSP deduction limit, plus $2,000.

With "unused contributions", a penalty tax may or may not apply (for example, where you have the RSP deduction room, but for whatever reason you decide to postpone taking the deduction to later years). With "excess contributions", however, a penalty tax will apply (except in the rare situation in which you made mandatory group RSP contributions prior to February 27, 1995).

In other words, the amount of RSP contribution that you can make over and above your RSP deduction limit without incurring a tax penalty is $2,000. This $2,000 amount is designed to catch those cases where the taxpayer has miscalculated the pension adjustment and contributed a little too much.

Note that:

- The $2,000 over-contribution amount is reduced when you have a negative RSP deduction limit, which may be due to the past service pension adjustment (PSPA) amount; and
- If you were younger than 18 years of age at any time during the year, you do not qualify for the additional $2,000 amount.

Over-contribution penalty

Generally, excess contributions are subject to a penalty tax of 1% per month until the excess is withdrawn. You have to complete Canada Revenue Agency's (CRA's) Form T1-OVP (Individual Tax Return for Excess Contributions) to calculate the amount subject to the tax and the tax payable. The penalty is due 90 days after the end of the year in which the excess contributions were made.

How to avoid the penalty tax

1. **Withdraw the excess contributions**

To avoid the excess contributions penalty, you should withdraw the over contributed amount from your RSP.

Normally, withdrawals of unused contributions from your RSP will have to be included as income on your tax return. However, you can deduct an amount equal to the amount withdrawn if the withdrawal is made

- in the year the unused contribution was made,
- in the following year, or
- in the year you were sent a Notice of Assessment or Notice of Reassessment or From T1028 for the year that you contributed or the year that follows, provided that you have reasonably expected that you could fully deduct the excess RSP contributions for the year that you contributed them or for the previous year.

Note: withdrawing excess contributions will only prevent future penalties; penalties incurred prior to the withdrawal will not be eliminated.

Withdrawals can be made with or without Form T3012A (Tax Deduction Waiver on the Refund of Your Unused RSP Contributions).

2. **Withdrawal without Form T3012A**

   - If the withdrawal of excess contributions is effected by simply withdrawing the amount from the RSP, a withholding tax will be applied on the amount withdrawn. The withdrawn amount must be reported as income for the year of withdrawal.

   - To have the withholding tax refunded, you will need to complete Form T746 when filing your tax return to claim a tax deduction.

3. **Withdrawal using Form T3012A**

   - If Form T3012A is completed and sent to the CRA before the withdrawal of excess contributions, and the CRA certifies the completed form, there will be no withholding tax on the withdrawal.

   - You should also complete Form T746. The withdrawal is considered as income and a claim for an offsetting deduction is still required.

Note that Form T3012A cannot be used to withdraw unused RSP contributions that have been transferred to a RIF. Therefore, the financial institution will have to withhold tax upon your withdrawal of the unused RSP contributions from a RIF.

Do not withdraw and use the excess contribution next year

You may leave the excess contribution in your RSP as an un-deducted contribution if new RSP contribution room is generated the following year. The excess contribution can be deducted and no further penalty tax will be incurred from January 1 of the following year onwards. Penalty tax will continue to accrue on the excess contribution for the remaining part of the current year. Therefore, this method is only appropriate if the excess contribution was made very close to the end of the year and the penalty tax will be minimal.