2007 RRSP update

www:liwanpo.com

Higher limits, wider investment choices and two more years to defer tax

Recent revisions aimed at boosting the popularity of registered retirement savings plans include higher contribution limits, an expanded list of qualified investments and an extension to the age at which one may contribute to a plan.

Significantly higher contribution limits for 2006 and beyond were established in the 2006 federal budget. For 2007, the maximum contribution is the lesser of $19,000--an increase of $1,000 from the previous year's limit--or 18% of the previous year's earned income. (See table)

Year	Contribution limit
2007	$19,000
2008	$20,000
2009	$21,000
2010	$22,000
2011	Indexed based on average wage growth

In a more recent change also designed to increase the use of RRSPs, the 2007 federal budget expanded the list of RRSP-eligible securities to include foreign-issued Canadian-dollar denominated bonds and virtually any securities listed on a designated exchange. High-risk derivatives remain off limits, while notable new inclusions are foreign-listed trusts and partnership units. The revamped qualified list took effect on March 19, 2007.

The 2007 federal budget also extended the age at which an RRSP must be converted to a vehicle that makes taxable payouts, such as a registered retirement income fund (RRIF) or an annuity. Now, an RRSP must be wound up by the end of the year in which the planholder turns 71, up from age 69.

That gives RRSP holders two additional years of tax-deferred compound growth for their retirement savings and also allows Canadians to make tax-deductible contributions to an RRSP for two more years, provided they have qualifying income.

While the move is meant to address the phase-out of mandatory retirement in many provinces in recent years and the fact that Canadians now tend to stay in the workforce longer, in reality, the new age limit marks a reversion: the age limit for RRSPs was initially reduced to 69 from 71 in 1996.

A less direct change that may affect RRSP strategies pertains to pension splitting and was introduced on Oct. 31, 2006, by federal Finance Minister Jim Flaherty at the same time he announced a new tax on income trusts.

Feb. 29 is RRSP contribution deadline
Last-minute RRSP contributions continue to be a way of life for many Canadians, according to the results of a poll by RBC Asset Management Inc. That survey showed 32% of those who plan to make, but have not yet made, an RRSP contribution for the 2007 tax year will do so just before the Feb. 29, 2008 deadline.

While that deadline is important for those planning to claim the corresponding tax deduction for the previous tax year, in reality the deduction may be claimed at any time.

The new rule, which took effect on January 1, 2007, allows a pensioner to split up to 50% of qualified pension income with his or her spouse. Qualified pension income for splitting purposes is generally paid by an employer-sponsored pension plan.

By comparison, contributions to a spousal RRSP generally allow the contributor, who is usually the higher-earning spouse, to reduce his or her income with a tax deduction. For tax purposes, this income-equalization strategy holds the potential for tax savings later on since withdrawn funds are taxed in the hands of the presumably lower-earning annuitant rather than be attributed to the contributor.

Even with the new found ability to pension split, spousal RRSPs may still be worthwhile for many Canadians. One reason is that there is no restriction on the percentage of income that may be split using a spousal RRSP, while the new rules restrict splitting to 50% of pension income.

Another reason is that spousal RRSPs effectively allow pension splitting for someone who retires before age 65 and who may not have an employer pension plan. Remember, the just-introduced pension-splitting rule allows income from a corporate plan to be split before age 65, while RRIF or RRSP proceeds may be split only at age 65 and later. Before age 65, a contribution to a spousal RRSP may still allow the withdrawals down the road to be taxed in the lower-income spouse's hands.

Please give me a call if you have any question concerning your RRSP, and remember don't wait until the February 29 deadline to contribute to your RRSP!

Jacques

www.liwanpo.com