Manulife

Tax, Retirement & Estate Planning Services

TAX MANAGED STRATEGY 4

Final RRSP Contributions at age 71

The clawback of government benefits can have a significant impact on your retirement income. With some careful RRSP planning as age 71 approaches, you can reduce taxable earnings in retirement – and reduce the clawback of government benefits.

The tax deductibility of contributions is one of the most valuable features of an RRSP. If you are approaching age 71 and closing out your RRSPs, however, the tax benefits associated with RRSP contributions can gain even greater importance.

Because RRSP tax deductions can be carried forward indefinitely – long after your RRSPs have closed – a final year RRSP contribution can be an important tool for lowering earned income in retirement and reducing the impact of any clawbacks on income-tested government benefits such as Old Age Security (OAS).

AN IN-DEPTH LOOK AT THE ISSUE... AND THE OPPORTUNITIES

If you are turning 71, there are two situations in which you can make allowable RRSP contributions before you close your RRSPs by December 31st of that year:

1. You have not maximized your RRSP contributions in previous years and have unused contribution room that has been carried forward.
2. You have earned income in your final RRSP year that generates RRSP contribution room for the following year.

In general, you should take advantage of every contribution opportunity available to you before closing your RRSPs.

By reducing taxable earnings, you can reduce the clawback on income-tested government benefits.

THE IMPACT OF THIS CLAWBACK CAN BE SIGNIFICANT

The clawback of Old Age Security benefits is 15¢ for each dollar of income in excess of a certain threshold.[1]

[1] For the current annual payment, visit https://www.canada.ca/en/services/benefits/publicpensions/cpp/old-age-security/payments.html and for the current threshold for the clawback (recovery-tax) visit https://www.canada.ca/en/services/benefits/publicpensions/cpp/old-age-security/recovery-tax.html

MAKING IT WORK

The final year RRSP contribution strategy

If you have not maximized your RRSP contributions in previous years and have unused RRSP room, you can make a lump sum contribution before closing your RRSP. The resulting tax deduction does not have to be used on that year's tax return. Instead, deductions can be used at any time in the future, whenever they are the most beneficial for you in reducing taxable earnings.

HOW IT STACKS UP

In this example, Ruth is making a $50,000 contribution. She has an annual income of $80,000 and a 32 per cent marginal tax rate.

Ruth can use her deduction whenever it is most beneficial. She could spread the deduction over 10 years by claiming $5,000 per year and save $1,600 in taxes each year The $5,000 annual deduction would also reduce the clawback of her OAS and potentially other income-tested government benefits.

TIP: RRSP contributions must be made by December 31st of the year you turn 71. However, RRSP deductions can be carried forward indefinitely, and can be spread out over several years in order to reduce taxable earnings in retirement.

The over-contribution strategy for those turning 71 in the current year

Even if you have no carry-forward RRSP contribution room, but have current year earned income that will generate RRSP contribution room in the following year, you should consider a final December over-contribution before closing your RRSP.

To take advantage of the contribution room, you can make a contribution during December, before the RRSP is officially closed.

Since the contribution is being made in December and the current year's RRSP room has been maximized, an over-contribution penalty of one per cent per month applies on any amounts in excess of $2,000. However, on January 1, the over-contribution disappears due to the RRSP contribution room generated from the current year. You can claim the tax deduction on next year's return or carry it forward to whichever future year you choose.

For illustration purposes only.

HOW IT STACKS UP

In this example, assume an income of $50,000 with a 32 per cent marginal tax rate (with no penalty on the first $2,000):

$50,000 x 18% = $9,000 contribution room created for the following year	
Tax savings on the $9,000 deduction, at 32% marginal tax rate	**$2,880**
Less 1% penalty for the month of December [($9,000–$2,000) x 0.01]	**($70)**
	$2,810

For illustration purposes only.

ARE YOU OVER AGE 71?

Regardless of an individual's age, if they have RRSP contribution room they can contribute to a spousal RRSP prior to December 31st of the year their spouse turns 71. They can then claim the deduction on their tax return whenever it is most advantageous to them. This strategy is particularly attractive if a client anticipates their spouse's retirement income will be less than their own.

IDEAL CANDIDATES

- Those who are approaching age 71 with unused
- RRSP contribution room Those who have earned income in the year they turn age 71 that generates RRSP contribution room in the following year
- Those for whom a tax deduction in retirement will either increase their eligibility for tax credits or reduce the impact on their income-tested government benefits subject to a clawback

TAKE ACTION

If you are getting ready to transfer your RRSPs to a RRIF, you should consider:

- The amount of earned income you have for the year
- Any unused RRSP room

Your final contribution or over-contribution can make a significant difference.

INVESTMENT OPTIONS WITH MANULIFE

Manulife and its subsidiaries provide a range of investments and services for retired investors:

Mutual Funds from Manulife Investments can help meet your specific financial needs, throughout your life. Whether you are just starting out, accumulating wealth or are nearing/in retirement, mutual funds offered by Manulife Investments, can provide you with solutions to help build a portfolio that meets your needs. Manulife utilizes four principal asset management firms to oversee its extensive fund family. Each firm is recognized for its strength and depth of experience in various asset classes and investment styles. Manulife is committed to providing superior investment products and services so you can enjoy life and worry less.

Manulife Segregated Fund Contracts combine the growth potential offered by a broad range of investment funds, with the unique wealth protection features of an insurance contract.

Through Manulife segregated fund contracts, investors can help minimize their exposure to risk through income, death and maturity guarantees, potential creditor protection features, and estate planning benefits – all from a single product or insurance contract.

The Manulife Investments Guaranteed Interest Contract (GIC) offers competitive rates plus investment options that include Basic, Escalating Rate and Laddered GIC Accounts. Investors benefit from a guarantee on their principal investment and from several different investment options that can diversify and add flexibility to their portfolio. Manulife Investments GICs can be an ideal solution for conservative investors looking to help grow their wealth, but who are also concerned about minimizing risk.

For more information contact your advisor or visit manulife.ca/investments

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