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Spousal RRSPs

Tax Managed Strategy 23

Now that we have pension income splitting, are spousal[1] RRSPs a thing of the past? At first glance, it would appear that spousal registered retirement savings plans (RRSPs) are no longer needed because the pension income splitting rules allow couples to split their income once their RRSPs become registered retirement income funds (RRIFs). Nevertheless, there are situations in which spousal RRSPs can offer some advantages.

What is a spousal RRSP?

A spousal RRSP is an RRSP that is opened by your spouse, but you contribute to it:

- Your contributions are based on your contribution limit, and you claim the tax deduction.
- Your spouse is the legal owner of the plan and makes all investment decisions and withdrawals.

A spousal RRSP provides an opportunity for income splitting at any age (subject to the attribution rules), and you choose the amount to split by deciding how much to contribute.

Income splitting at any age

Under the pension income splitting rules, you must convert your RRSP into a RRIF and you must be at least age 65. Regular RRSP withdrawals don't qualify for pension income splitting. However, with spousal RRSPs, you can split income anytime as long as the attribution rules don't apply. If a spousal contribution hasn't been made in the current calendar year or the two previous calendar years, any withdrawals from the RRSP will be taxed to your spouse.

Because the attribution rules use calendar years, it's usually best to make spousal contributions within the calendar year instead of during the first 60 days of the following year. For example, if a spousal contribution is made in February 2021 for the 2020 tax year, the income attribution will cease to apply on January 1, 2024 (provided no further spousal contributions are made). However, if the contribution is made before December 31, 2020, the attribution would cease to apply on January 1, 2023.

Income splitting can save you tax

Spousal RRSPs allow tax savings to be realized when the spouse in the lower tax bracket takes income from the plan. The following table helps illustrate how income splitting with a spousal RRSP can work. In this example, a couple withdrawing the same amount of income can save $2,400 annually by using this strategy.

	Individual RRSP – 40% tax rate ($)	**Spousal RRSP – 20% tax rate ($)**
RRSP income/withdrawal	12,000	12,000
Taxes payable	4,800	2,400
After-tax income	7,200	9,600
Tax savings (annually)		**$2,400**

Not restricted to 50 per cent

After age 65, the pension income splitting rules allow you to split up to 50 per cent of your RRIF income with your spouse. With spousal RRSPs, you determine the amount of income to split by deciding how much to contribute to the spousal RRSP.

Benefit from having a younger spouse

If you have a younger spouse, you can continue to contribute to their spousal RRSP until the end of the year your spouse turns 71, if you still have RRSP contribution room available. Also, with a younger spouse, the income from those RRSP contributions can be delayed until the year after your spouse's 71st birthday.

Take advantage of unused RRSP contribution room at death

In the year of your death, or within 60 days after the year-end, your legal representative may make a contribution to your spouse's RRSP under the normal rules. This contribution will be deductible on your final tax return.

Additional considerations for spousal RRSPs

It's important to understand that a spousal contribution becomes the property of your spouse. With pension income splitting, no assets are transferred. You and your spouse simply file a joint election each year, which gives you the option to choose whether income splitting makes sense.

Also, keep in mind that any funds withdrawn from a spousal RRSP can't be recontributed later without using future available contribution room. In this instance, a tax-free savings account may be a better option as withdrawals are added back to the unused contribution room in the following calendar year.

Ideal candidates

Income splitting using a spousal RRSP is best suited for those who:

- have a spouse in a lower marginal tax bracket
- want the flexibility to income split using the spousal RRSP at any age (subject to the attribution rules) and the ability to decide how much to split.

Take action

To take advantage of income splitting using a spousal RRSP, consider the following:

- Determine your contribution room available from your latest notice of assessment.
- Contribute to a spousal RRSP so that you can claim the tax deduction and your spouse, as legal owner, can have future withdrawals taxable to them when the attribution rules no longer apply.

With spousal RRSPs, you determine the amount of income to split by deciding how much to contribute to the spousal RRSP.

Important disclosure

1 The terms *spouse* and *spousal* include a spouse or common-law partner as defined by the *Income Tax Act* (Canada).

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