



# Making Your Retirement Income Work for You

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**T**here is an old adage in business that says, “If you can’t see it, you can’t manage it.” Therefore, if you want to enjoy your retirement, consider a written retirement plan.

The most successful people in the world are those who plan. It’s not that they always get what they want, but because those who plan place goals in front of themselves, they’re in a better position to at least go forward in the right direction. You simply can’t move into a worry-free retirement without planning for it. If you do believe that the government will fund your retirement income entirely, or that your employer will take care of you, you are in for a shock.

We have never met anyone who enjoyed paying taxes, but we are sure there is something to be said for being in the top marginal tax bracket year after year. If only there was a way to pay less tax? Is there any difference between tax avoidance and tax evasion?

Yes, tax evasion is illegal. If you don’t pay your taxes or are hiding income illegally, you’re in trouble. However, it’s your right to plan your financial life in the most tax-effective manner. Finding ways to defer or lower your taxes is being smart. Such tax planning isn’t just for the rich. It’s something that you need to pay attention to during your working years and particularly when you’re planning your future retirement or your estate. This means the tax on your income, whether it comes from employment, pensions, or investments.

The key components of smart tax planning are the three Ds: deduct, defer, and divide. We are going to discuss the importance of dividing – specifically splitting retirement income.

## Pension Income Splitting

Effective 2007, Canadian retirees can split retirement income on their tax returns. The result is that you both pay tax at a lower tax rate, saving money today which in

the future may also reduce or avoid the OAS clawback. You can take advantage of income splitting every year when you and your spouse file your personal tax returns. To use this strategy, the higher income spouse can elect to transfer “on paper” up to one-half of his or her eligible pension income to the lower income spouse, as pension income splitting doesn’t require the physical transfer of funds. You don’t have to split pension income equally. This is particularly suitable for couples with a significant difference in income, age or both.

You can split your pension monies based on your personal tax situation for that year. Bear in mind this option is available every year and the amount transferred each year can vary.

Income eligible for pension income splitting is based on whether you are over or under age 65. For example:

Pension income that qualifies if you’re under age 65:

- Pension income from a registered pension plan (that is, money from your defined benefit or defined income plan),
- Payment from an Individual Pension Plan (IPP),
- Income from a registered annuity,
- Saskatchewan Pension Plan (SPP) annuity payments. (*This is new and only came into effect for the 2010 tax year.*)

Pension income that qualifies if you’re 65 or over:

- Pension income from a Registered Pension Plan (RPP), as above,
- Payment from an Individual Pension Plan (IPP), as above,
- Income from an annuitized RRSP or DPSP,
- Withdrawals from your RRIF, LIF, or RLIF (Registered Life Income Fund),
- Interest portion of non-registered annuities.

Regardless of your age, you can’t split income from the following:

- Canada Pension Plan (CPP)\*, Québec Pension Plan (QPP),\*

	No Income Splitting			50% Income Splitting			Optimal Split		
	Spouse 1	Spouse 2		Spouse 1	Spouse 2		Spouse 1	Spouse 2	
OAS	\$6,405	\$6,405		\$6,405	\$6,405		\$6,405	\$6,405	
CPP	\$6,149	\$3,000		\$6,149	\$3,000		\$6,149	\$3,000	
Pension	\$60,000			\$60,000	0		\$60,000	0	
RRIF	0	\$10,000		0	\$10,000		0	\$10,000	
	<b>\$72,554</b>	<b>\$19,405</b>		<b>\$72,554</b>	<b>\$19,405</b>		<b>\$72,554</b>	<b>\$19,405</b>	
Split	0	0		(\$-30,000)	\$30,000		(\$-26,575)	\$26,575	
Adjusted Income	<b>\$72,554</b>	<b>\$19,405</b>		<b>\$42,554</b>	<b>\$49,405</b>		<b>\$45,979</b>	<b>\$45,980</b>	
Tax	\$16,825	\$523	\$17,348	\$5,930	\$8,420	\$14,350	\$7,100	\$7,100	\$14,200
Net	<b>\$55,729</b>	<b>\$18,882</b>	<b>\$74,611</b>	<b>\$36,624</b>	<b>\$40,985</b>	<b>\$77,609</b>	<b>\$38,879</b>	<b>\$38,880</b>	<b>\$77,759</b>
						<b>Tax Savings</b>	\$2,998	Better than 50% by	\$150
								Better than no split by	\$3,148

- Old Age Security (OAS),
- Guaranteed Income Supplement (GIS),
- RRSP withdrawals,
- Income from Retirement Compensation Arrangements (RCAs).

### \*Sharing CPP Pension

CPP pension sharing is governed by separate, plan-specific rules and not covered by the new income-splitting legislation. Spouses or common-law partners who are together, are at least 60 years old, and receive CPP retirement pension can share their pension benefits. This may result in tax savings as well. If only one of you is a CPP contributor, you share that one pension. The overall benefit payments paid do not increase or decrease with pension sharing. To take advantage of this, you need to make a formal request through Service Canada.

### \*Sharing QPP Pension

For those residing in Quebec, you also have the option of sharing your Québec Pension Plan (QPP) between you and your spouse. To do so, you have to apply to the Régie des rentes du Québec and meet certain conditions on the date of application.

So, have some fun with the numbers to determine what works best for you and your spouse. And remember, a 50/50 split might not be ideal for everyone as the shifting of income impacts not only the tax brackets, but also the OAS clawback, the provincial surtax, provincial health premiums and both the federal and provincial tax credits. See our example in the chart above. You can see the difference in the Optimal Split chart where only \$26,575 of pension money was transferred to Spouse #2, rather than the full \$30,000.

Until 2007, the most familiar method of income splitting available to Canadians was spousal RRSPs. Even with the new pension splitting rules, spousal RRSPs still make sense because the pension splitting rules only allow you to split up to ½ of your pension income. Spousal RRSPs may help bridge the age gap between the time you retire to the time you turn age 60 or 65. A word of caution – the attribution rules are still in effect and any money withdrawn from a spousal plan will be taxed to the contributor if deposits have been made in the last three years.

Income splitting can be a smart way for you to save a lot on taxes, especially during retirement when one spouse is receiving a pension and the other isn't, or there is a substantial difference in your income levels. Remember, income splitting is complex and personal. This is something that should be reviewed every year at tax time.

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