INITIATIVE

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Pension Income Splitting

Canadian taxpayers receive preferential tax treatment for "pension income". A non-refundable tax credit is available for the first $2,000 of qualifying income. A similar credit is available in Quebec for up to $2,000 of pension income. In addition, income qualifying for the pension credit can be split among spouses. A couple, in certain circumstances, could receive a second credit where previously only one was available to them.

Different rules apply to taxpayers who are at least age 65 at any time in a taxation year and those who have not yet attained age 65. Taxpayers who have not turned age 65 in the year will only be able to claim the pension credit if they have "qualified pension income".

Pension Income

Generally, taxpayers who are age 65 or over have easier access to the pension credit since many more sources of income qualify. Types of income that qualify are:

1. A payment in respect of a life annuity out of or under a superannuation or pension plan
    - The Canada Revenue Agency (CRA) generally accepts that amounts from foreign plans qualify including government plans such as US Social Security but excludes certain payments such as receipts from a US Individual Retirement Account (IRA)
2. An annuity payment under a Registered Retirement Savings Plan (RRSP)
    - RRSP withdrawals do not qualify for the pension credit
3. A payment out of or under a Registered Retirement Income Fund (RRIF)
4. A payment payable on a periodic basis under a defined benefit or a money-purchase plan within a Registered pension plan (RPP), including an Individual Pension Plan (IPP).
5. An annuity payment under a Deferred Profit Sharing Plan (DPSP)
6. An instalment payment under a DPSP
    - Equal instalment payments paid at least annually and not extending beyond 10 years
7. Prescribed annuities
8. Other amounts:
    - Annuities reported by the insurer as "Accrued Income: Annuities" qualify for the pension credit. The interest portion does not constitute pension income for purposes of the credit, only amounts reported as "Accrued Income: Annuities" are eligible

Vol. 12, No. 09

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The Initiative is a monthly case study and information brief for distribution partners of The Empire Life Insurance Company (Empire Life). Details are edited to illustrate relevant financial, tax & estate planning principles, generally using the Federal context. This material is current to the year and month of issue (Vol. yy, No. mm) but is not a tax or legal opinion. Retained professional advice should be engaged in relation to any actual Client matters.

The Sales, Tax, Estate Planning, Underwriting & Product (STEPUP) team provides broker support, including seminar education, advanced concept illustrations & Client case consultations.

Marilyn deRooy is a member of STEPUP. She focuses on legal, tax & estate planning concepts, and guidance for related product strategies.

Ready to discuss estate planning and client wealth strategies that matter to you and to your clients, please contact your Account Manager

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Specific exclusions from Pension Income are:

1. A pension or supplement under Old Age Security (OAS)
2. A benefit under Canada Pension Plan (CPP)
3. A death benefit
4. An amount included in income as "pension income" or "qualified pension income" but the taxpayer has taken another deduction for this amount
5. A payment out of a Salary Deferral arrangement (SDA); a Retirement Compensation Arrangement (RCA); an Employee Benefit Plan (EBP) or an employee trust or a prescribed provincial pension plan (current only Saskatchewan Pension Plan falls under this exclusion)

Qualified Pension Income

Taxpayers who have not reached the age of 65 in a taxation year have fewer opportunities for access to the pension credit. They can only claim the pension credit on income considered "qualified pension income".

1. A payment in respect of a life annuity out of or under a superannuation or pension plan.
   - No matter how old the taxpayer is, life annuities out of or under a superannuation or pension plan are considered "qualified pension income"
   - Take care not to lose access to the pension credit because of inter-plan transfers. CRA holds that once pension funds are transferred from an employer pension plan to another vehicle such as a locked in RRSP, its identity changes. CRA considers the new RRSP no longer a superannuation or pension plan, but an RRSP therefore it has lost its identity and is no longer considered "qualified pension income". The taxpayer will have to attain the age of 65 before the pension credit is available on this pension income.
   - Since access to the pension credit also determines whether the income may be split under the pension splitting rules, significant additional taxes could be paid because of inter-plan transfers. With the loss of the pension credit and the ability to pension split, additional taxes would be paid each and every year until the taxpayer attains the age of 65.
2. Other amounts qualifying as "pension income" received as a consequence of the death of a spouse or common-law partner

Gaining an understanding of the pension income splitting rules will allow the advisor to provide greater tax savings for their clients, the taxpayer.

The STEP UP team is here to help.

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