

Opportunities for pension income splitting

Spouses¹ are allowed to split qualified retirement income with their spouse. This can result in a reduction of family taxes and can also minimize the impact on income-tested tax credits and benefits.

If you have a spouse who is in a lower tax bracket, you and your spouse are able to elect to have up to 50 per cent of eligible income transferred to the lower income spouse. Eligible income is defined as income eligible for the pension income credit.

¹ Includes a spouse or common-law partner as defined by the *Income Tax Act* (Canada).

WHAT TYPES OF INCOME ARE ELIGIBLE?

Under age 65, only income received directly from a pension plan or received from other registered plans or an annuity because of the death of your spouse qualifies for pension income splitting. Income from other registered plans such as Registered Retirement Income Funds (RRIFs), annuities purchased with your Registered Retirement Savings Plan (RRSP) and Deferred Profit Sharing Plans are only eligible for splitting if you are age 65 or older. Government plans such as Canada/Quebec Pension Plan (CPP/QPP) and Old Age Security (OAS) do not qualify under the federal pension income splitting rules. Generally, income from non-registered investments will also not qualify. One exception is when the income is received from an annuity, including a Guaranteed Interest Contract (GIC) provided by an insurance company. A GIC from a life insurance company reports the interest accrued as annuity income which qualifies for the pension income credit at age 65. The interest element of a non-registered annuity contract (prescribed & non-prescribed) also qualifies for those age 65 or older.

See *Tax Managed Strategy #14: The Pension Income Tax Credit Using an Insurance Company GIC* (MK2071E) for more information on the pension income credit and insurance company GICs.

INCOME SPLITTING OPTIONS

Eligible income

You can split up to 50 per cent of eligible income, described above, with a spouse. Because of income tested benefits such as age credits, medical expenses and clawbacks on OAS, the optimum transfer may be less than 50 per cent. The examples below demonstrate that some analysis will be necessary each year to determine the optimal amount to split with your spouse in order to maximize the reduction in taxes and minimize the impact on income tested tax credits and benefits.

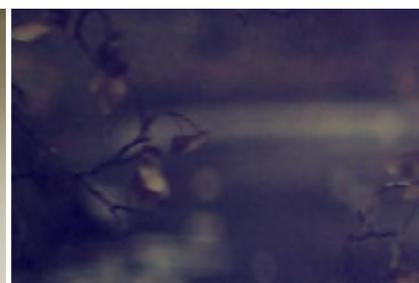
Canada/Quebec Pension Plans

Although not part of the Federal initiative with respect to pension income splitting, these government plans already allow spouses who are at least 60 years of age to share up to 50 per cent of the benefits earned while you were living together.

Spousal RRSPs

Contributing to a spousal RRSP can also result in tax savings. Under the pension income splitting rules, eligible income can only be split at age 65 or older. However, spousal RRSPs provide income splitting at any age and are not restricted to 50 per cent. Also, if your spouse is younger, the income can be delayed until the year after your spouse reaches age 71.

Following are two examples taking into account tax credits for the basic personal exemption, age credit and pension income credit, where applicable.



EXAMPLE 1: Both spouses are age 65 or older. The maximum benefit occurs by splitting just enough income to fully utilize the lower tax brackets and avoid an OAS clawback for Spouse 2.

	No Splitting (\$)		With Splitting (\$)		Difference (\$)
	Spouse 1	Spouse 2	Spouse 1	Spouse 2	
Company pension	90,000		45,000	45,000	
RRIF/Spousal RRIF	20,000	12,000	10,980	21,020	
CPP	12,780		12,780		
OAS	6,787	6,787	6,787	6,787	
Gross Income	129,567	18,787	75,547	72,807	
Tax¹	(33,492)	(1,452)	(15,634)	(14,943)	
OAS Clawback	(6,787)		(411)		
Age Credit ²		1,280	153	215	
Net Taxes Owing	(40,279)	(172)	(15,892)	(14,728)	Decrease 9,831
After Tax Income	89,288	18,615	59,655	58,079	Increase 9,831

For illustration purposes only. ¹Taxes owing are calculated using graduated rates for the province of British Columbia taking into account the Basic Personal Exemption and the Pension Income Credit (\$351) if applicable. Generally others will also apply. ²The Age Credit is \$1,281 less clawbacks.



EXAMPLE 2: Spouse 1 is 65 or older and spouse 2 is between age 60 and 65. A full 50 per cent split can maximize the tax benefits since no OAS clawbacks or age credits apply to spouse 2 and can eliminate the OAS clawback for spouse 1.

	No Splitting (\$)		With Splitting (\$)		Difference (\$)
	Spouse 1	Spouse 2	Spouse 1	Spouse 2	
Company pension	90,000		45,000	45,000 ³	
RRIF/Spousal RRIF	20,000	12,000	10,000	22,000	
CPP	12,780		6,390	6,390	
OAS	6,787		6,787		
Gross Income	129,567	12,000	68,177	73,390	
Tax¹	(33,492)	(205)	(13,567)	(15,116)	
OAS Clawback	(6,787)				
Age Credit ²			319		
Net Taxes Owing	(40,279)	(205)	(13,248)	(15,116)	Decrease 12,120
After Tax Income	89,288	11,795	54,929	58,274	Increase 12,120

For illustration purposes only. ¹Taxes owing are calculated using graduated rates for the province of British Columbia taking into account the Basic Personal Exemption and the Pension Income Credit (\$351) if applicable. Generally others will also apply. ²The Age Credit is \$1,281 less clawbacks. ³Even though under age 65, Spouse 2 now has a Pension Income Credit on the transferred Company pension income.

IDEAL CANDIDATES

- Those age 65 or who are currently receiving income directly from a pension plan
- Those who have a spouse in a lower tax bracket

TAKE ACTION

- Identify the income eligible for splitting
- Determine, with your tax preparer, the amount to be taxable to your spouse
- Make an election on your tax return



INVESTMENT OPTIONS AVAILABLE THROUGH MANULIFE

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