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MAKING YOUR LEGACY COUNT

Tax Matters

Case Study: Accessing Registered Retirement Savings Plan (RRSP) Assets

Pat Barlow is a 68-year-old widow who lives outside of Calgary. She is financially secure and has no children. Pat is active with charities that provide medical aid and clean water to families in developing countries, and has even travelled to remote areas to see these programs at work. Pat has about $3 million in her RRSP and would like to create a Foundation before she has to convert her plan to a RRIF in three years.

The Philanthropic Solution

Pat's adviser provided both philanthropic and financial advice to help his client find the best solution. First, he helped her understand the benefits of a Personal Foundation Account at Canada Gives, using the documents "Creating a Foundation is Easier than You Think" and "Canada Gives in Perspective," available on the Canada Gives website.* Next, the adviser presented the most tax-efficient plan for collapsing Pat's RRSP and moving the assets into her Personal Foundation Account.

By The Numbers

Pat knew that Canadians who make a charitable donation can claim a tax credit against their income. The maximum tax credit is usually 75% of the individual's income for the year; individuals who donate more than that may carry the unclaimed portion forward up to five years. Pat's adviser explained that Alberta is particularly tax-friendly to philanthropists: the federal and provincial governments provide a combined 50% tax credit on donations, whereas the top combined income tax rate is only 39%. This means that a $100 donation can effectively shelter up to $128 of income.

Her financial adviser then explained how Pat can get the most from this tax credit. She begins by withdrawing $1 million from her RRSP in the first year. The government requires a 30% withholding tax, so she is left with $700,000 to donate to her Personal Foundation. Because Pat is in the highest tax bracket (39%), her tax liability on the $1 million withdrawal is $390,000. After claiming the donation credit of $350,000, she would owe $40,000 in income tax. This amount is subtracted from the $300,000 withheld when she made the initial withdrawal, netting her a tax refund of $260,000.

By repeating this strategy over three years, Pat can build a $2.1 million endowment in her Personal Foundation, generating annual grants that provide continual funding for her key charities. If she wishes to donate the tax return refunds as well she could claim a further tax credit of $130,000 each year and increase the size of her Foundation assets.

To maximize both Pat's giving potential and the tax advantages, her adviser worked with her accountant to file a "Request to Reduce Tax Deductions at Source." This strategy can potentially reduce the tax withholdings on her RRSP withdrawals from the standard 30% to nil during all three years. This would allow Pat to donate $1 million annually (rather than $700,000) and to claim the donation credit against both the RSP withdrawal and her income from other sources. As a result, she could potentially donate the entire $3 million and shelter income up to about $3.8 million from income tax.

** See "For Advisors" at www.canadagives.ca and go to "advisor resources".*

Please note that this example is provided for illustrative purposes only and does not constitute tax advice. Individuals should seek professional advisory services specific to their own circumstances.

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