UPPER CANADA CAPITAL
PRIVATE WEALTH MANAGEMENT

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Team Newsletter

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The "Gap-Years": Maximizing RRSP Withdrawals While Your Income Is Low

From the Desk of Evan Campbell, BAS (Hons)
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For many Canadians, retirement income can come in stages. Employment income may stop suddenly with a full retirement on a single date, or work may slow gradually with partial retirement. This may often happen before Canada Pension Plan (CPP) and Old Age Security (OAS) benefits begin, and years before a Registered Retirement Savings Plan (RRSP) legally must be converted into a Registered Retirement Income Fund (RRIF). These "gap-years" can create a period of reduced or low-income, which is a valuable opportunity to draw on savings in a tax-efficient manner.

An RRSP is tax-deferred money. For many hard-working Canadians, an RRSP is an effective tool to reduce tax liability during high-earning years, with every dollar contributed reducing your total taxable income in the year you put it in. However, every dollar that is eventually withdrawn is added back as taxable income in the year it is taken out, at the tax-payers full marginal rate. This can become an issue later in life, when before the end of the year you turn 71, an RRSP must be converted into a RRIF account (other less common options are turning the account into an annuity or cashing out entirely) [1]. Once it is a RRIF account, the government forces taxable withdrawals each year, at an increasing minimum percentage,

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whether the money is needed or not. Including other pension and CPP/OAS income, this can often push retirees into higher tax-brackets than necessary, even to the point of OAS clawback[2]. This is why these "gap-years" can be beneficial to reducing lifetime tax liability from retirement savings accounts.

The combined marginal rate (federal plus provincial) is what matters when considering early RRSP withdrawals during these years[3]. The years between stopping work and starting CPP/OAS and mandatory RRIF withdrawals can often be the last years retires spend in lower tax-brackets. The goal of this strategy is to withdraw enough RRSP money each year to fill up lower tax-brackets without drawing too much to place you in a bracket you'd otherwise avoid.

Is This Strategy Right for Me?

The right withdrawal amounts can depend on a variety of factors specific to your financial situation. Often those that are a good candidate to consider this strategy are:

1. **Retirees with large RRSP or LRSP accounts:** this strategy may help reduce the overall tax burden later in life when larger registered savings plans must convert to income funds, depending on your personal tax situation. In some cases, larger RIF/LIF withdrawals can be enough to claw-back OAS benefits on their own.

2. **Lower total income and additional income streams** (i.e. – rental income): this strategy may be worth considering if total income is low, as withdrawals could be taxed at lower marginal rates depending on your circumstances.

3. **Additional savings or a cost of living that can support this strategy:** those with a cost of living high enough that they must draw down significantly on portfolio income may not be good candidates for this strategy as they will be in a high tax bracket regardless. Additional after-tax savings may help provide a buffer to support higher cost of living during these years.

4. **Delaying CPP/OAS:** both CPP and OAS increase the longer you wait to claim them. By delaying CPP and OAS and substituting this income with RRSP de-registration, you can receive increased benefits later on and extend the "gap-years" low-income period at the same time.

5. **Lower taxable savings:** it could be more beneficial to elect for triggering capital gains during these years, depending on the specific situation for the taxpayer and the taxable investments held.

Considerations

There are also some important points to consider:

- If you have a spouse, RRIF withdrawals after age 65 can be split for tax purposes, which can lower a household's combined tax bill. It may also be worth exploring partial-RIF options to also receive the pension income tax credit if not already receiving.

- If you do not have a need for extra registered income during these gap years, and have sufficient TFSA contribution room, a worthwhile strategy is to direct RRSP withdrawals to your TFSA account for future tax-free growth.

- Additional RRSP withdrawals can reduce eligibility for income-tested benefits (such as the Guaranteed Income Supplement) – which can limit the benefits of this strategy for lower-net-worth retirees expecting these benefits.

- Withdrawing money from an RRSP when a spouse has little or no other income also needs to consider the impact on the spousal tax credit to determine if the strategy is worthwhile in your particular situation.

If you'd like to review your specific planning situation, and whether you may be a good fit for this strategy, please reach out to us for a review.

SOURCES

[1] https://www.canada.ca/en/revenue-agency/services/tax/individuals/topics/rrsps-related-plans/receiving-income-rrsp.html
[2] https://www.canada.ca/en/services/benefits/publicpensions.html
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Navigating RESP Withdrawals

From the Desk of Jordan Pereira, CIM®
• Financial Advisor Associate, Manulife Wealth Inc.

When families reach the post-secondary education milestone, accessing funds from a Registered Education Savings Plan (RESP) can seem complex. Understanding the different types of withdrawals, specifically taxable vs non-taxable withdrawals, can help improve tax efficiency and help you make full use of eligible government assistance, where applicable.

Here is a breakdown of the taxable and non-taxable withdrawals:

Post-Secondary Education Withdrawals (PSE) – **Non-Taxable**

What it is: A PSE withdrawal is the return of the original principal contributions made to the RESP.

These withdrawals are tax-free and there are no government limits on how much PSE can be withdrawn at once, as long as the student is enrolled in a qualifying education program.

Education Assistance Payments (EAP) – Taxable

What it is: An EAP is made up of the government grants received and the accumulated growth generated from the investments within the account. EAP withdrawals are taxed as regular income for the student.

Withdrawal limits: The government places the following EAP withdrawal limits on the first 13 weeks enrolled in a program.

- **Full-time students:** Can withdraw up to $8,000 during the first 13 weeks. After 13 weeks, any amount can be withdrawn as long as enrollment continues.
- **Part-time Students:** Up to $4,000 for the initial 13-weeks.

Strategies

Maximize EAP Withdrawals Early (In most cases): A student's income typically starts lower in their first year or two of school and generally increases as they get older. Because EAP withdrawals are taxed in the student's hands, it is usually most tax-effective to focus on EAP withdrawals early.

Ensure You Access All Government Grants: The grants received in the RESP can only be extracted through EAP withdrawals. If a student decides to not finish school, then unused grants must be paid back to the government.

Unused Funds: If a student decides not to continue with post-secondary education, the RESP contributions can still be withdrawn tax-free. Unlike the contributions, there is a steep penalty on withdrawing investment growth from the RESP if your child decides not to pursue further education.

When deciding between EAP vs PSE withdrawals, it is always best to have a conversation with our team to determine the best course of action.

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Corporate-Owned Whole Life Insurance: A Strategic Tool for Holding Companies with Retained Earnings

From the Desk of Frank Valicek, CFP, CIM®
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• Life Insurance Advisor, Upper Canada Capital Inc.

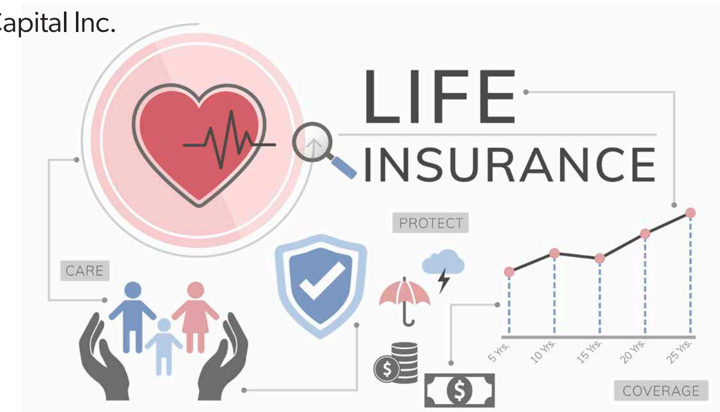
For Canadian holding companies (HoldCos) sitting on excess retained earnings, corporately owned whole life insurance may provide tax advantages in certain situations and can be used as part of a diversified corporate investment strategy, subject to product terms and tax rules. When structured properly—with the HoldCo as owner and beneficiary and a key shareholder as the insured - the death benefit may generate a credit to the corporation's Capital Dividend Account (CDA), which can allow for tax-advantaged intergenerational transfers when the CDA and tax rules apply.

Why Use a Holdco to Own Whole Life Insurance?

Holding companies often accumulate retained earnings after paying corporate tax on active business income. These funds, if invested passively, are subject to annual tax on investment income, which erodes compounding over time. By redirecting a portion of these retained earnings into a corporately owned whole life policy, the Holdco can:

- **Achieve tax-deferred cash value growth** inside the policy, similar to the tax-sheltered growth in an RRSP but without contribution limits.
- **Preserve capital** with a guaranteed death benefit that can be used for estate planning or business succession.
- **Create a CDA credit on death**, which allows the corporation to pay out a tax-free capital dividend to shareholders (often the estate or next generation).

Because premiums are paid with after-tax corporate dollars, the strategy is most effective when the corporate tax rate on active income is lower than the personal marginal rate, or when HoldCo has limited high-yield investment alternatives.



How the CDA Credit Works on Death

The Capital Dividend Account is a notional CRA tracking account that records certain non-taxable receipts a private corporation can distribute to shareholders as tax-free capital dividends. Key mechanics include:

- **CDA credit calculation:** On the insured shareholder's death, the HoldCo receives the death benefit tax-free. The CDA credit equals the death benefit minus the policy's Adjusted Cost Basis (ACB) immediately before death.

CDA Credit = Death Benefit – ACB

- **ACB dynamics:** For older or long-held whole life policies, the ACB often declines over time (as the net cost of pure insurance is deducted), meaning the CDA credit can approach 100% of the death benefit.
- **Tax-free payout:** The HoldCo may be able to elect to pay the CDA balance as a capital dividend to the deceased's estate or other shareholders, which is generally received tax-free for the recipient when the CDA election and tax rules are satisfied. Any portion of the death benefit not credited to the CDA (i.e. the ACB) can be paid as a taxable dividend if needed.

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This mechanism typically converts what would otherwise be a taxable estate receipt into a tax-efficient inter-generational transfer, depending on the policy structure, corporate circumstances, and applicable tax rules.

Whole Life as a Proxy to Fixed Income

Within a Holdco's investment portfolio, whole life insurance can serve as a fixed-income proxy for several reasons:

- **Predictable policy values:** The cash value may grow based on contractual guarantees (where applicable) and, for participating policies, may also receive dividends, which are not guaranteed, offering a certain stability.

- **Low correlation to markets:** Unlike equities or GIC's, the policy's value is not directly tied to interest rate fluctuations or market volatility.

- **Liquidity via policy loans:** The HoldCo may be able to access cash value through policy loans; the tax treatment and suitability depend on the policy structure and the corporation's circumstances.

For Holdcos seeking to diversify away from traditional fixed income (especially in a low-yield or volatile rate environment), whole life offers a tax-advantaged, capital-preserving alternative; the tax treatment and suitability depend on the policy structure and the corporation's circumstances.

Strategic Considerations for Ontario HoldCos

Holdco vs Opco ownership: While Holdco typically owns the policy, naming the operating company (Opco) as beneficiary (where legally permissible) can add flexibility for business succession or share redemption strategies.

Passive income tax rules: Be mindful of the $50,000 passive income threshold for small business deduction claw backs; life insurance cash value growth does not count as passive income, but other HoldCo investments might.

Estate integration: Coordinate the policy with a well-drafted estate plan, including share redemption agreements, to ensure the CDA payout aligns with your overall wealth goals.

BOTTOM LINE

For Ontario-based Holdcos with excess retained earnings, corporately owned whole life insurance could represent a powerful tool to:

- Grow wealth tax-deferred inside the policy
- Create a large CDA credit on death for tax-free inter-generational wealth transfers
- Provide a stable, fixed-income-like asset within a diversified corporate portfolio

After establishing a need for life insurance itself, and when integrated with proper legal and tax planning, this strategy can significantly enhance after-tax estate value while preserving capital for future generations.

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https://www.rbcinsurance.com/en-ca/life-insurance/whole-life-insurance/

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