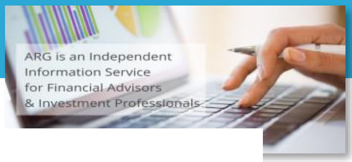
Spousal RRSPs Reduce Taxes: Now and During Retirement



Spousal Registered Retirement Savings Plans must not be universally understood by investors, because they are not utilized to their maximum benefit. These financial vehicles were designed to encourage retirement savings with tax breaks at the time of contribution and at the time of withdrawal, just like regular RRSPs.

Spousal RRSPs contain additional advantages for couples who have a partner earning a higher income than the other. Equalizing retirement income between partners can reduce overall household taxes. The greater the income discrepancy between the two partners, the larger the potential benefit from Spousal RRSPs.

What you need to Know

The contributor to an RRSP or a Spousal RRSP receives the initial tax benefit. The contributor's taxable income is reduced by the amount of the contribution. A $5,200 contribution ($100/week) reduces taxable income by $5,200 for the contributor whether it goes into their RRSP or into a Spousal RRSP.

While on deposit, the investments are treated equally, growing tax-free in an RRSP or a Spousal RRSP until the funds are withdrawn, assuming that the money is held in the Spousal RRSP for at least 3 years, or any withdrawals are taxed as income for the contributor, not the spouse.
At retirement, the household will rely on their savings in their accumulated in their RRSPs and elsewhere. Both spouses in the couple would begin to withdraw from their RRSPs (or RRIFs). If there is a large discrepancy in the amounts in their RRSPs, one spouse could have a significantly higher income than the other when withdrawals are made during retirement.

All other things being equal, a couple with a high-income spouse and a low-income spouse will pay more income tax than a couple with equal levels of income. There are ways to split income between spouses, but they have limitations and are often under threat of being repealed. Imagine an Ontario couple with a net income above their basic personal exemptions of $75,000 per year. If it is taxed in only one of their hands, $17,254 would be owed. If the income was split evenly, $37,500 each, the total tax owing would be $15,038, because both stay in lower tax brackets. With 2023 tax rates this couple would save more than $2,200 per year in combined federal and provincial taxes.

The Bottom Line

Together, along with your accountant, we should discuss the possibility of utilizing a Spousal RRSP strategy to reduce taxes now and during retirement.