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Mid 60's Tax Planning Tips

"We are living in unprecedented times."

How many times have you heard this in 2020?

While it has been an eventful year, I am a believer that we will continue to fight and eventually get thru this difficult chapter of life.

With that said, planning for your retirement should still be top of mind.

If you (or a parent) are in their 60's, read on, this article is for you!

Post Highlights:

1. Look at potential tax planning opportunities for those in their 60's.
2. Analyze a case study re: private corporation and spousal RRSPs.

Maximize RRSP Contributions

This strategy relies on the assumption that you are currently earning income in at least the 2nd tax bracket ($48,000-$95,000), preferably higher.

Why you ask? RRSP contributions allow for the deferral of income tax. Current year contributions reduce income in a higher bracket. Eventually, when withdrawn, the contributions are brought into income at a lower rate.

Married? Consider contributing to a spousal RRSP in order to equalize retirement income.

Pro tips:

- Check your RRSP contribution room (prior to contributing) in order to avoid penalties.
- Avoid borrowing funds to invest in an RRSP at this stage in life.

Turn RRSP funds into Tax-Free RRIF Withdrawals

Will you be using the $2,000 pension tax credit when you turn age 65?

If not, consider transferring funds ($50,000) from your RRSP to a RRIF and subsequently withdrawing $2,000/year between age 65-71.

This will essentially allow you to access $2,000/year from your RRSP on a tax-free basis.

Pro tips:

- Whether you need the income or not, don't miss out on this opportunity.
- Consider deferring OAS under this scenario if you're still working to avoid OAS pension clawback.

Maximize TFSA

If your RRSP is maximized or you are in a lower tax bracket, consider contributing to a Tax Free Savings Account.

The current annual limit is $6,000 plus any unused limit from prior years, up to a maximum of $69,500 (2020).

TFSAs provide numerous investment options to meet your risk tolerance including cash, GICs, mutual funds, and others. Generally, low-risk investment options would be advisable at this stage of life.

Investments and investment income grows tax-free and can be withdrawn any time.

Pro tips:

- Although funds can be withdrawn at any time, there are limitations on re-depositing funds.
- Similar to RRSPs, be careful not to "over-contribute" to your TFSA. Penalties apply.

Defer OAS Pension

OAS monthly payments can be increased by 36% (0.6% per month) if deferred until age 70. This is especially beneficial if you intend to continue working into your late 60's.

Look out for an auto-enrolment form from the government when you turn 64. If your intent is to defer the pension as you are still working, make sure you take the necessary steps to cancel the auto-enrolment.

The option to defer OAS is only available if you haven't started collecting OAS or have only collected for 6 months.

Pro tips:

- Deferring your OAS pension, while still working, will help you avoid clawback of these benefits.
- Even if your income isn't at the clawback threshold ($79,000), you're likely in a higher tax bracket than when you retire.

Defer CPP Pension

Similar to OAS, your CPP pension can also be deferred. CPP monthly payments can be increased by 42% (0.7% per month) if benefits are deferred after age 65.

CPP has a similar auto-enroll feature but this doesn't occur until 70 so it is less of a concern than the OAS auto-enroll.

Pro tips:

- As there is no clawback on CPP payments, the advantage of deferring comes from the increased monthly payment.
- If you are able to defer CPP when you are in a higher tax bracket to a time when you are in a lower bracket, this results in permanent tax savings.

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Case Study

For this case study, we'll analyze a potential tax planning strategy that a husband & wife could use as they look to wind down their private corporation.

Facts:

- Husband and wife own 100% (60/40) of the shares in their private corporation.
- Shares in the corporation qualify for the "excluded shares" exemption re: TOSI.
- Both shareholders are working for third parties now.
- Corporation to be wound down over the next five years.
- Both shareholders have sufficient RRSP contribution room to absorb wind-up dividends.

While the corporation could be left open throughout the couple's retirement, this would lead to needless professional fees for many years, reducing the couple's nest egg.

Instead, the couple could use their available RRSP contribution room to shelter tax on dividends issued to withdrawal the retained earnings of the corporation.

Personal tax planning could be completed for the couple to determine the ideal amount to contribute to their RRSPs on an annual basis.

If there is a portion of the annual dividend that does not need to be contributed in order to shelter tax on the dividend income, the balance could be invested in a TFSA.

Consideration should be given to spousal RRSPs to ensure the couple is optimizing their retirement funds.

If one spouse retires from third party employment earlier than the other, he/she could consider withdrawing approximately $10,000 year from their RRSP. Tax would be held at source but would be returned when a personal tax return is filed.

If withdrawing an RRSP, ensure that you are not removing funds from the spousal RRSP within 3 years of the initial deposit. This will result in attribution rules applying to the withdrawal and the income being taxed in the hands of the contributing spouse.

With this plan, both individuals should defer their OAS/CPP pensions in order to avoid clawback concerns relating to OAS and to take advantage of tax savings relating to CPP.

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Conclusion

By leveraging RRSP & TFSA contribution room & deferring government pensions, a private corporate shareholder can close out his/her company in a tax efficient way.

An accountant should be consulted to determine an optimal timeline for dividend payments and the optimal mix of RRSP/TFSA contributions.

Additionally, an investment broker should be consulted to ensure the funds in each registered account are invested correctly to provide for your retirement.

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