Maximizing an RDSP

Do any of your clients receive the disability tax credit? Then they should be looking at the registered disability savings plan for more financial strategies. **Geoffrey Zaldin** of Special Needs Financial explains how it works.

The registered disability savings plan (RDSP) is an amazing tool when planning for the financial welfare of an individual with a disability. But unfortunately, it's a tool that's misunderstood and underutilized.

To qualify for an RDSP you must meet ALL of the following criteria:

- Be eligible for the disability tax credit (DTC)
- Under the age of 60 (an RDSP can only be opened for an individual and contributions can be made to it until the end of the year in which he or she becomes 59 years of age)
- Be a resident of Canada and have a valid social insurance number (SIN)

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With an RDSP comes government grants and bonds, but an individual is only eligible for these until December 31 in the year they turn 49. There are two types of government funds for RDSP accounts. **The Canada Disability Savings Grant (CDSG)** is a matching government grant based on the net family income and the amount that is contributed into an RDSP. This is just a fancy way of saying the net income from Line 236 from the income tax return of the parent(s) living with the individual until the end of the year they turn 18 (this is determined by how you filed your tax returns) and then the net family income of the individual and spouse if any when over the age of 18. When determining the net family income to calculate the grant entitlement, the tax return from two years prior to the year of contribution will be used (for example, in 2019 when determining grants and bonds, the government will look at the 2017 tax returns).

The amount of CDSG matching will depend on whether the net family income is above or below a threshold set by the government, which changes each year. For 2019 the grant threshold is $95,259. If the net family income is above the threshold, then you are entitled to a grant of a dollar for each dollar contributed to a maximum of $1,000 for each qualifying year. If the net family income is below the threshold, then you are entitled to a grant of three dollars for each dollar contributed up to the first $500 contributed. After the first $500 contributed, you will be entitled to a grant of two dollars for each dollar contributed up until the next $1,000 has been contributed. This means if your net family income is under the grant threshold, you will receive grants of $3,500 for $1,500 of contributions for each qualifying year.

Canada Disability Savings Bonds (CDSB) are amounts paid by the government into an RDSP to low-income individuals that have qualified and opened an RDSP account. No contribution is required. For 2019 you would receive $1,000 of bond money if the net family income that applies was under $31,120. If the net family income for 2019 is between $31,120 and $47,630 then you would receive a portion of the $1,000 bond according to the formula in the *Canada Disability Savings Act*. Like the grants, these threshold numbers change every year.

CDSG and CDSB will be clawed back if funds are withdrawn from the RDSP within 10 years of receiving them. This is known as the assistance holdback amount (AHA).

I often get the question: When will someone will be able to withdraw funds from an RDSP and still maximize CDSG and CDSB? Because of the various rules of the RDSP, this is based upon the individual's situation and typically ranges from age 29 (which is rare) to age 49+ (which occurs more often).

Contributions made into an RDSP are not tax deductible, but the growth in the account is not subject to income tax until withdrawn. When a withdrawal is made, there is a calculation that determines the percentage of withdrawal that will be taxed (proceeds of rolled over registered accounts, the cumulative gain, grants and bonds) as opposed to the contributions that will not be taxed.

When an individual first opens an RDSP, they can carry forward unused grants and bonds up to 10 years. However, $10,500 is the maximum annual grant money they can receive, and $11,000 is the maximum annual amount of bonds. If RDSP contributions are more than grant money, that contribution is not carried forward to attract grants in future years. They only receive grant money for contributions made in the current year. There is a maximum lifetime contribution limit of $200,000 into an RDSP, and this limit does NOT include the government grants and bonds received. Also, unlike many other accounts, a beneficiary may have only one RDSP account at a time. While an individual can have one, and only one, RDSP, they can transfer from one RDSP to another if they follow the required conditions.

If the individual who is to be the beneficiary of the RDSP is under the age of majority, then either a legal parent, a guardian, or individual who is legally authorized to act for the beneficiary, or a public department, agency, or institution that is legally authorized to act for the beneficiary, can open the RDSP. If a beneficiary has reached the age of majority and is contractually competent they can open the RDSP for themselves. If the legal parent(s) of a beneficiary that has reached the age of majority and is contractually competent is/are the holder of an RDSP already existing, then the parent(s) can remain the holder, the beneficiary could be added as a joint holder, or the beneficiary could become the sole holder of the account.

When the beneficiary has reached the age of majority and there is either a question if the individual is contractually competent or it is determined the individual is not contractually competent, then a qualifying family member (QFM) can open the RDSP. A QFM includes a spouse, common-law partner, or parent of an individual. This provision is available until December 31, 2023 but it has been extended several times already. At this time, a QFM does not include a sibling. For a sibling to be the account holder they would have to be the beneficiary's legal guardian.

Anyone can contribute into an RDSP, but they will require written consent of the plan holder. Unfortunately, if the beneficiary dies, the RDSP must be closed and the funds disbursed to the beneficiary's estate by December 31 of the year following the year they died. Any grants or bonds received in the previous 10 years would be subject to repayment, and the remaining funds will be paid to the estate.

RDSPs can be opened at most financial institutions. This includes banks, credit unions, and independent financial advisors. While most banks and several credit unions offer RDSPs, some staff who sell RDSPs aren't educated in the complex rules. I strongly suggest that an individual find someone who is knowledgeable about RDSPs and concepts of higher financial and estate planning from a special needs perspective. This would include a discussion of the concept of a Henson trust (which is a type of trust designed to benefit disabled persons by protecting assets — usually an inheritance — of the disabled person, as well as the entitlement of government benefits and entitlements) and other methods of ensuring continued entitlement of government benefits and services. I would also suggest that a financial advisor that is planning on selling a client an RDSP do the necessary research so they know how to properly advise the client, or that they partner with another advisor that has the necessary knowledge and expertise to properly guide the process.

Overlooked Rules

UPDATED RULE ABOUT WHAT HAPPENS IF THE BENEFICIARY IS NO LONGER ELIGIBLE FOR THE DTC.

In this case, no future contributions can be made into the RDSP unless the Beneficiary re-qualifies for the DTC. There are also further grants or bonds that are received unless re-qualified. If you voluntarily close the RDSP, any grant or bond money received in the 10 years preceding the date that the Individual was no longer eligible for the DTC. The only way to retain all the government grant and bond money would be to hold the RDSP and let it grow until the Beneficiary turns 60.

In addition, if a beneficiary has a reduced life expectancy of less than five years they can apply with the assistance of a written certification by a licensed medical doctor or nurse practitioner to have their RDSP turned into a specified disability savings plan. This prevents the triggering of repayment of grants and bonds received in the prior 10 years and allows withdrawals of up to$10,000 of the taxable amount (or the greater of the lifetime dis-ability assistance payment formula) to be paid out each year. This freezes the RDSP and prevents any further contributions, grants, or bonds. Several parents feel there is no point in opening an RDSP as their child has a diminished life expectancy and they would never be able to retain the grants and bonds. This may convince them that they should reconsider, as there is a chance that both they and their child may benefit from an RDSP.

Furthermore, you can rollover retirement savings into an RDSP if you have an unused amount of the overall RDSP lifetime limit. This amount would not be taxable to the estate of the deceased retirement savings holder and the income tax would be deferred for the beneficiary until they start withdrawing from the RDSP (this would significantly reduce the amount of income tax paid by the estate). The beneficiary would have to be a financially dependent child or grandchild of the deceased for the rollover to be allowed. The proceeds from a rollover do not count as a contribution that can attract grant money but they do count against the beneficiary's lifetime contribution limit. This has the potential of significant tax savings and can materially affect the estate planning of the parents and grandparents of a dependent disabled individual.

While some advisors may mention that a client can roll over an registered education savings plan (RESP) to an RDSP, I find that many do not explain how this works. It is the accumulated income payment (AIP) from an RESP that gets rolled over. This could be advantageous if there are significant gains in the RESP and you know for certain that the beneficiary will never attend a post-secondary institution that RESP funds could be utilized for. The RESP grant money would be sent back to the government, and the principal returned to the subscriber. The monies from an RESP rollover do not attract grant money but count against the beneficiary's lifetime contribution limit to the RDSP.

PROVINCIAL ASSET BREAKDOWN

In Alberta, Saskatchewan, Manitoba, Ontario, Nova Scotia, Newfoundland and Labrador, Yukon Territory, Nunavut, and Northwest Territories, the RDSP is considered an exempt asset for and exempt income when determining eligibility for disability benefits. In New Brunswick, Quebec, and PEI, it is an exempt asset and partially exempt from the income calculations. In addition, a RDSP does NOT impact Old Age Security, Canada Pension Plan, Guaranteed Income Supplement, GST, or other federal social assistance benefits. There are some situations whereby you may elect to use an RDSP not for grants and bonds but exclusively for the ability to supplement provincial disability benefits that would have otherwise been lost due to asset threshold issues. — *G.Z.*

Withdrawing from an RDSP

Money is taken out from an RDSP either as a disability assistance payment (DAP), which is a singular payment from an RDSP to a beneficiary and can be done on their own, or as an LDAP, which, once started, cannot stop until the RDSP has ended). The beneficiary can take both a DAP payment and an LDAP payment from an RDSP. There is a minimum amount of money that one MUST take from an RDSP by the end of the year the beneficiary turns 60, and this is when the LDAP must be started. The amount of the required LDAP payment for the year is determined by this LDAP formula:

$A \div (B + 3 - C) + D$

where:

A = the fair market value (FMV) of the property held in the plan at the beginning of the year, (excluding the value of locked-in annuity contracts held by the plan trust).

B = the greater of 80 and the age of the beneficiary at the beginning of the calendar year.

C = the actual age of the beneficiary at the beginning of the calendar year.

D = the total of all periodic payments paid, or deemed to have been paid, under certain locked-in annuity contracts, to the plan trust in the calendar year, if applicable.

Some people with RDSP accounts are not aware that if the amount that was contributed into an RDSP is less than the total grants and bonds received, then the RDSP would be considered a PGAP (primarily government assisted plan). This will limit the total amount of money that can be withdrawn annually from the plan to either the LDAP formula or 10 per cent, whichever is greater. This knowledge could significantly change a financial plan given the potential restriction of withdrawals.

RDSP rules and specifications can be overwhelming, so when opening up an RDSP ensure that you are aware of the rules and processes.

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