MOVE

Transfers of U.S. retirement plans to RRSPs can be non-taxable.

By SANDY CARDY AND CAROL BETAIRE

any people who've been living and working outside Canada wonder if it's possible to consolidate retirement holdings after resettling in their native land.

Canada's Income Tax Act (ITA) allows resident taxpayers in Canada to transfer benefits of some U.S. retirement arrangements (401K/403B plans) or individual retirement accounts (IRAs) to Canada on a tax-deferred basis.

Depending on age and the rules governing the U.S. plan, a Canadian resident taxpayer can collapse his or her U.S. plan and transfer lump-sum superannuation or pension benefits under subparagraphs 60(j)(i) and 60(j)(ii) of the tax code on plan assets that are individual contributions—defined as those not made by an employer or government entity on the individual's behalf.

How does it work? Under Canadian and U.S. tax rules, funds withdrawn from a foreign retirement plan such as a 401K or IRA are taxable as income in the year the plan is collapsed in the U.S. The withdrawal amount must be included as income in the Canadian tax return, but a deduction for the amount transferred to an RRSP can offset the income inclusion. Upon collapse of the U.S. plan, the U.S. administrator will withhold 15% tax for non-resident aliens or non-U.S. citizens. Normally the withholding tax is 20% for U.S. residents, but Article XXII of the Canada-U.S. tax treaty reduces this withholding to 15%. (See chart on page 28 for more information.)

The following steps smooth the process of bringing U.S. retirement accounts to Canada:

1 Examine the plan specifics (Simple IRA, Roth IRA, 401K, 403B, etc.). Plans may be comprised of employee monies, employer monies and/or non-taxable amounts. In the case of employer monies, there are no provisions in the ITA to allow a tax deferral. However, if the individual has unused RRSP contribution room, this can be employed to offset the necessary income inclusion.

- 2 Examine the tax implications of collapsing the plan in the U.S., especially if minimum distributions upon retirement will be tax-free. In some cases, it's in the best interests of the annuitant to leave the plan in the U.S.
- 3 Estimate the value of the transfer in Canadian dollars. And watch the currency fluctuations, because a favourable exchange rate can add additional dollars to the RRSP.
- 4 Consider the age of your client. If he or she is under $59 \frac{1}{2}$, the collapse of the plan will trigger a 10% early withdrawal penalty. This penalty is withheld in the U.S. and is not refundable.
- 6 Calculate the withholdings and their effect on the transfer-in. For example, a \$100,000 (Canadian) transaction for a 60-year-old client would result in a transfer-in to the RRSP of \$85,000 (\$100,000 minus 15%). The \$15,000 withholding tax would be used as a foreign tax credit against tax payable when your client files

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RETIREMENT OPTIONS

Each retirement plan has its own rules governing transfer and dispersal.

TYPE OF PLAN Who can contribute?	CANADIAN RRSP Individuals with earned income who are 69 or younger at the close of the year	IRA Individuals with earned income who are under age 70 1/2 at the close of the year	ROTH IRA Individuals of any age with earned income	401(k) Individuals redirect some pay (pre-tax) to a retirement plan in the U.S. (often employer-matched)
Contribution limits	Generally 18% of prior year's income to a yearly dollar limit (\$16,500 in 2005)	Maximum of \$3,000 U.S. (single) or \$6,000 U.S. (married), or 100% of earned income; if age 50 or older, catch-up contributions of \$500 U.S. per spouse	Maximum of \$3,000 U.S. (single) or \$6,000 U.S. (married), or 100% of earned income; if 50 or older, catch-up contributions of \$500 U.S. per spouse	Maximum of \$13,000 U.S. or 100% of pay; if age 50 or older, catch-up contributions of \$16,000 U.S. maximum per spouse
Transfer options	Transferable to another RRSP, RRIF or RPP	Can be collapsed and transferred to an RRSP	Transfer to a tax-prepaid savings account; contributions are not deductible and growth is not taxed provided funds are not withdrawn until annuitant reaches age 59 1/2 or becomes disabled. Tax deferral of an RRSP is not necessary. Contributions and growth can be transferred to a non-registered account in Canada	Transfer to an IRA upon termination of employment; contributions are not deductible by individual, and are not included in U.S. taxable income until withdrawn; if plan holds only individual monies, they can transfer to an RRSP; if employer matches it, transfer first to an IRA if possible
Classification of transfer under Canadian ITA	60(j)(i) Rollover from one Canadian plan to another	60(j)(ii) Rollover of a foreign retirement arrangement	60(j)(ii) Rollover of a foreign retirement arrangement but only to the extent funds are taxable in the U.S.	60(j)(i) Rollover of a foreign pension plan to the extent individual monies are transferred
Timing of transfer	In most situations, transfer funds directly between plan sponsors	Within taxation year of collapse of plan or within 60 days after the end of the year	Within taxation year or within 60 days after the end of the year	Within taxation year or within 60 days after the end of the year

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TYPE OF PLAN

Age at which plan must be collapsed

CANADIAN RRSP

December of the year the account holder reaches age 69

IRA

Minimum required distributions begin by April 1 of the year following the year the person reaches age 70 1/2

ROTH IRA

No mandatory age for plan to be collapsed; after age 69 1/2, contributions plus growth can be withdrawn tax-free; prior to that age, growth is taxable

401(k)

Distributions may begin at age 59 1/2, upon termination of employment, or rolled to an IRA; minimum distribution must commence by April 1 of the year after the person turns 70 1/2

Source: Mackenzie Financial Corporation

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his annual tax return. The income inclusion on the tax return will be \$100,000. This will be offset by the transfer-in of \$85,000, resulting in taxable income of \$15,000. At a 45% tax rate, this will result in tax payable of \$8,750. The \$15,000 foreign tax credit can be applied against the tax payable, and the remaining \$6,250 can be carried forward for a maximum of seven years if not used in the current year.

6 If your client doesn't have an RRSP, open an account to receive the transfer. Your client may receive the cheque personally, but if the funds are deposited by year-end—or no later than 60 days after the end of the year—the transfer will be recognized. Clients who are relocating or have already moved back from the U.S. and

are under the age of 70 are excellent prospects. This strategy can also be applied to individual retirement accounts from other regions and countries, such as the U.K. or Scotland. AE

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