

Pension Income Splitting

Answers to questions your clients may ask

BY JAMIE GOLOMBEK

It's now been just over one year since the notion of pension splitting was first introduced on Halloween 2006. The final legislation was passed in June and is now law. Shortly thereafter, the Canada Revenue Agency (CRA) responded to a number of technical questions on the pension splitting rules. Here's a brief summary of some of the more interesting technical points — questions your clients may be asking you.

What is pension splitting?

Starting this year, Canadian residents will be able to split up to half of their pension income by allocating to a spouse or common-law partner. The amount so allocated is then deducted by the person who received it and is taxed by the recipient spouse or partner on his or her own personal return. Naturally, both spouses or partners must elect the allocation in writing, which is to be done on an annual basis, as desired.

For a complete discussion of what constitutes pension income for the purpose of the credit, please see my article, "Finding the Right Split," in the February 2007 issue of *FORUM*.

Do I have to contact my pension provider to ask them to split the income?

No — the fact that you will be splitting pension income with a spouse or partner has no effect whatsoever on the actual payment of the pension income to the recipient. As a result, the recipient spouse or partner will continue to receive an information slip reporting the pension received, which would then be subsequently split on the tax return.

Will the attribution rules still apply on split pension income?

Since it's a notional allocation only and not

an actual transfer of funds from one spouse or partner to the other, it follows from this that the normal attribution rules preventing income splitting of income and capital gains between spouses or partners still apply. For example, even though some of the husband's income may be taxed in his wife's hands (through the election), the actual money does not become hers for subsequent investment purposes.

Tell me more about this "election."

The pensioner and his or her spouse or common-law partner will have to make a new joint election on their annual tax returns. New CRA Form T1032, "Joint Election to Split Pension Income," should be available by January 2008. The new 2007 income tax return will include a new line for the pensioner to deduct the amount of pension allocated to his or her spouse or partner. Similarly, another new line will be added for the other spouse or partner to report the allocated pension income.

What about the tax withheld — who claims this?

The CRA has stated that any tax withheld at source from the pension income must be allocated in exactly the same proportion as the pension income is allocated, as per the election.

Who claims the \$2,000 pension income amount?

Both the recipient and transferee each may potentially claim the \$2,000 pension credit. While the recipient will certainly qualify for the credit (as it's a prerequisite for splitting pension income in the first place), the recipient spouse or partner may not qualify. That's because eligibility for the credit can also depend on the age of

the recipient. For example, say Jack, age 65, decides to split his RRIF withdrawals with his wife, Jill, who is only 62.

While the RRIF income certainly qualifies in Jack's hands for the pension income credit (and thus permits him to split up to 50 per cent of it with Jill), the allocated amount won't qualify for an additional \$2,000 credit in Jill's hands since she is not yet 65 years of age.

On the other hand, if Jack were to have a defined benefit pension plan instead of a RRIF and were to begin receiving his monthly pension, the income would qualify for the pension credit in both Jack's and Jill's hands.

How, if at all, will pension splitting affect income-tested benefits, such as the Goods and Services Tax/Harmonized Sales Tax (GST/HST) credit, Canada Child Tax Benefit (CCTB), and other provincial benefits and tax credits, such as the Old Age Security (OAS) program?

Since allocating pension income to a spouse or partner merely reduces one spouse or partner's net income while simultaneously increasing the other's net income, benefits and credits that are income-tested based on the combined income of both spouses or partners will not be affected. Such credits include the GST/HST credit, the CCTB and related provincial or territorial benefits.

Pension splitting, however, does have the ability to affect other credits and benefits that are solely based on one spouse or partner's net income, such as the age amount, the common-law partner amount and any OAS clawback.

Consequently, transferring pension income from a high-income spouse or partner who is subject to the OAS clawback (i.e., net income over \$63,511 in 2007) to a spouse or partner whose income is below the OAS threshold can provide an ideal way to preserve otherwise clawed back benefits. **E**

JAMIE GOLOMBEK, CA, CPA, CFP, CLU, TEP, is the vice-president, taxation & estate planning, at AIM Trimark Investments in Toronto and a 2006 recipient of the ICAO Award of Distinction, awarded by The Institute of Chartered Accountants of Ontario. He can be reached at jamie.golombek@aimtrimark.com.