phi
PORTER HÉTU INTERNATIONAL

the abacus

ISSUE 85

Can you borrow from your RRSP without paying tax on the withdrawal?

In short, "Yes." Though to be a little more accurate, the real answer is, "It depends."

Registered Retirement Savings Plans (RRSPs) are popular for their immediate tax deferral when making contributions. They also allow contributions to grow tax-free until money is withdrawn in the future.

There are many misconceptions about RRSPs. For example, many people think funds in an RRSP cannot be withdrawn until retirement. Funds can actually be withdrawn at any time, although withdrawals are subject to tax. (Of course, if the funds are in a long-term GIC or other investment that can't currently be cashed out, then in practice there may be no way to get at them.)

However, it is also possible to "borrow" funds from an RRSP to use for certain purposes without paying tax on the amount borrowed (which is essentially a withdrawal from the RRSP). This option is particularly attractive given the current high interest rates and uncertainty as to what the near future holds in terms of borrowing and the associated costs.

BUYING A HOME

One of the most common situations where people borrow from their RRSP is to buy a home. Under the **Home Buyers' Plan** (HBP), you can borrow up to $35,000 from your RRSP if you use the funds to purchase your "first" home.

The word "first" is included in quotes above, as the home does not actually have to be your first home. Instead, you or your spouse must not have owned a home that you lived in either in the part of the year leading up to the withdrawal, or in any of the four previous calendar years.

The amounts withdrawn must be repaid equally to your RRSP over 15 years, starting the second year after withdrawal. Any missed repayments are taxed as income, as if you had withdrawn the repayment amount from your RRSP in that year.

The HBP can be used in conjunction with the newly created tax-free **First Home Savings Account** (FHSA).

SEE **BORROW FROM RRSP** P. 4

Foreign tax credit

Make sure the foreign tax is mandatory

As you may know, the Canada Revenu Agency (CRA) provides a "foreign tax credit" (FTC) to Canadian residents, to reduce double taxation on foreign-source income.

COMPLEXITY...

THE FTC RULES ARE COMPLEX. In general terms, CRA allows a credit to a Canadian resident for foreign income tax paid on foreign-source income, up to a limit of the Canadian tax payable on the same income.

The effect is that you pay total tax equal to the higher of the two rates of tax (Canadian and foreign) on the foreign-source income.

FOR EXAMPLE | Suppose you earn $1,000 in dividends on a US stock, and the US company withholds $150 as withholding tax. *(We'll ignore exchange rate issues for this example; assume all amounts are in Canadian dollars.)* Assume you are in a 40% tax bracket, so you pay $400 of Canadian tax on the same $1,000 of dividend income.

In this example, CRA will grant you a foreign tax credit of $150 on your Canadian tax return, so that you only pay $250 of Canadian tax on the dividends. The total tax burden ($150 to the US and $250 to Canada) will thus equal the $400 of Canadian tax you would have paid if there had not been any foreign tax. (Most developed countries have similar rules.)

... AND TRAPS

One of the many FTC traps you should be aware of is that the foreign tax must be mandatory. If you could have avoided paying the foreign tax, or recovered it from the foreign government, then you can't claim it as a foreign tax credit.

FOR EXAMPLE | Suppose your US-source income is interest rather than dividends, and the interest is exempt from US tax under the Canada-US tax treaty. If the US payor withheld US tax—and you can recover that tax from the US government by claiming relief under the treaty—then the US tax you paid is not eligible for the foreign tax credit, because CRA will consider it to be a 'voluntary' payment to the US rather than a foreign tax. So instead of claiming a foreign tax credit, your only option may be to claim back the wrongly-charged tax from the US Internal Revenue Service.

Note also that the foreign tax credit applies only to an "income or profits tax". It is not available for social security taxes other than those paid to the US. Most US Federal Insurance Contributions Act payments do qualify, due to a specific provision in the Canada-US tax treaty.

Taxable benefit updates

Including policies for virtual social events

IN AN AGE when remote working and team events have become the norm, the Canada Revenu Agency (CRA) has recently updated its taxable benefit policies to reflect this evolving way of working. Employers who make service awards, subsidize parking, or provide in-person and remote social events for their staff should review these updated policies to ensure that they are not inadvertently providing taxable benefits.

GIFTS, AWARDS AND LONG-SERVICE AWARDS

Gifts and awards to employees made in cash or "near-cash" (for example, a prepaid card or something easily convertible into cash) are generally taxable.

However, the CRA has an administrative policy that considers "non-cash" gifts and awards to not constitute a taxable benefit in certain circumstances:

- The total value of non-cash gifts to an employee must not exceed $500 in one year (other than trivial items and long-service awards).
- The gift must be in relation to a special occasion (for example, a birthday) or a general recognition of the employee's contributions. The amount must not be given for performance-related reasons.

The CRA's recent policy addition in relation to gifts and awards treats gift cards as "non-cash" if certain requirements are met.

The gift card must be pre-loaded with the amount of the gift, and the card must only be able to be used to purchase goods or services from a single retailer (or group of retailers) identified on the card.

The terms and conditions of the card must prohibit the value being converted to cash, and the employer must keep a log with certain information, including the name of the employee, the reason for providing the card, and details of the card amount and the retailers where the card may be used.

If the gift card does not meet all required conditions, it will be treated as near-cash, and a taxable benefit.

PARKING

The CRA has added an administrative policy regarding 'scramble' parking offered to employees (i.e., where there are fewer spaces available than employees who want parking).

The provision of this type of parking will not be considered a taxable benefit where certain requirements are met:

- There must not be more than two parking spaces for every three employees who want parking.
- The spaces must not be assigned to any employee. (Their use must be random or uncertain.)
- The spaces must be offered to all employees who want parking. This concession eases the burden of employers calculating benefits where parking use is sporadic. This is particularly helpful when remote working and in-person schedules vary week to week.

MORE INFORMATION CAN BE FOUND ON THE GOVERNMENT OF CANADA WEBSITE

SOCIAL EVENTS

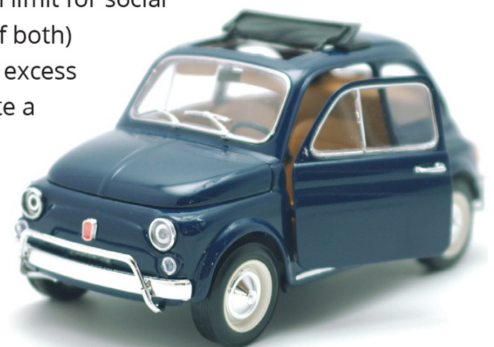
The CRA's administrative policy for social events has also been updated to cover events where the cost of virtual attendance is covered by the employer.

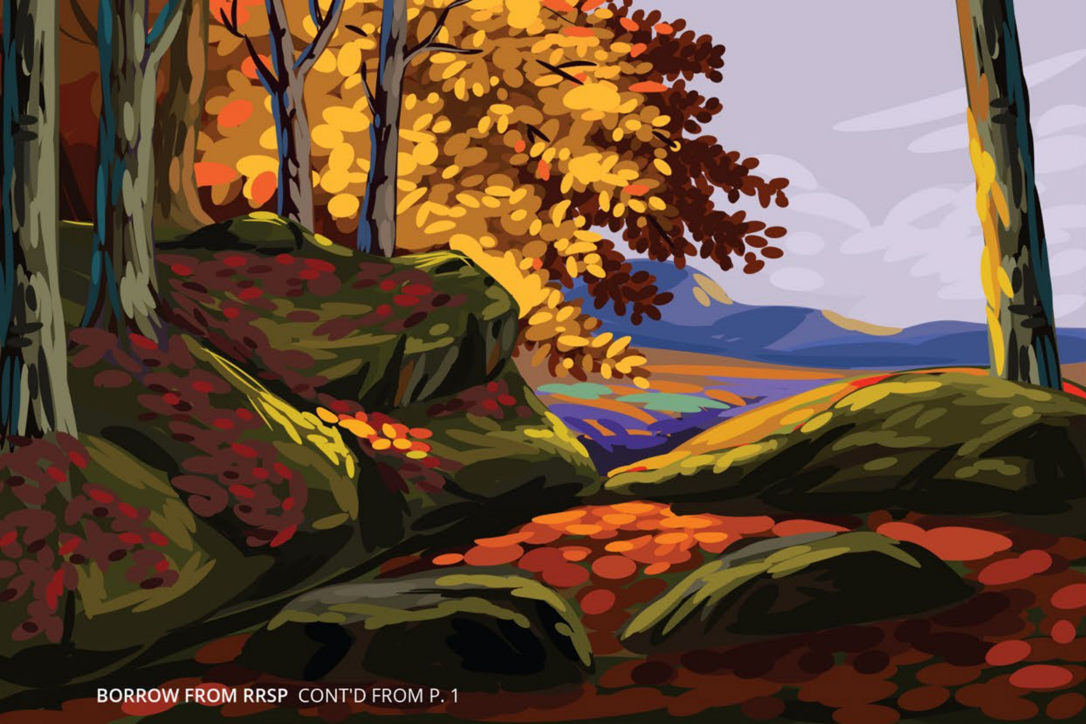
IN-PERSON social events will not constitute a taxable benefit where the event is available to all employees and the cost per employee is **$150 or less *(including taxes)***. Where there are virtual attendees, there is a further requirement that any gift cards provided for meals etc., must meet the "non-cash" requirements, discussed above.

VIRTUAL social events will not constitute a taxable benefit if the event is available to all employees and the cost per employee is **$50 or less *(including taxes)*** if the event only includes meals, beverages and delivery services, or **$100 or less *(including taxes)*** if the event also includes entertainment. If amounts are forwarded to the employee in advance, or reimbursed to the employee after the virtual event, receipts must be provided. As with in-person events, gift cards must meet the "non-cash" requirements.

In both situations, the maximum annual limit for social events (in-person, virtual, and a mixture of both) is six employer-paid events. Any events in excess of this number will automatically constitute a taxable benefit.

It is critical to note the lower monetary limits for virtual events, compared to in-person events. If these limits are exceeded, the full amount will be a taxable benefit.




BORROW FROM RRSP CONT'D FROM P. 1

The FHSA is a hybrid between a TFSA and an RRSP. It allows you to save up to $8,000 per year (up to $40,000 in total) in a separate account. When making contributions, you receive an up-front tax deduction similar to an RRSP, and withdrawals can be made tax-free provided the funds are used to purchase your "first" home (which has the same "first" home requirement as the HBP).

FINANCING EDUCATION

The **Lifelong Learning Plan** (LLP) allows you to borrow RRSP funds to finance ongoing education. This plan allows you to borrow $10,000 per year, up to a maximum of $20,000, for you or your spouse to pursue full-time education. Withdrawals can be made over four years.

There are strict requirements for the type of course eligible for the LLP. You should confirm with the course provider that your intended course is eligible.

As with the HBP, borrowings must be repaid to your RRSP, and you will be taxed on any missed repayments. Repayments start one year after the course is completed (or the fifth year after the first amount borrowed if this is sooner), and must be repaid in equal installments over ten years.

The LLP is generally most beneficial to individuals who want to undertake full-time study but will still receive taxable income while doing so. Low-income individuals may be better advised to make a taxable RRSP withdrawal instead. Although this would be subject to tax, the tax rate may be low. In addition, the withdrawal may be covered by the basic personal amount (the amount of income that can be earned before any tax is payable), which is currently $15,000.

IMPORTANT POINTS

- Borrowing from your RRSP may not be suitable for everyone, and professional financial advice should be obtained before making any withdrawal.
- Any third-party interest charges that can be saved by borrowing from your RRSP, rather than approaching a commercial lender, must be weighed against the tax-free returns in your RRSP that will be lost during the time the borrowed funds are not invested in your RRSP.
- The HBP and LLP come with strict reporting and repayment requirements. There are significant tax implications if they are not complied with. You should involve your accountant at an early stage if you are considering any of these plans.

Information on these plans can be found on the Government of Canada website at this link.

Rawluk & Robert
CHARTERED PROFESSIONAL ACCOUNTANTS

Porter Hétu International
Professional Services Group

226 St. Mary's Road
Winnipeg, Manitoba
R2H 1J3

Telephone: (204) 237-6053
Fax: (204) 231-1461

Ryan Rawluk, CPA, CGA
Eric Robert, B.A., B.Comm, CPA, CGA
www.accountants.mb

Visit us online at **porterhetu.com**

Make a Porter Hétu International member firm your strategic partner

Independent member firms of Porter Hétu International offer a full range of professional services in accounting and auditing, management advisory, business plans and proposals, estate planning, tax planning, forensic accounting, mergers and acquisitions, business reorganization and more...

Call us today or visit **porterhetu.com** for a listing of all member firms.

To receive a free copy of the *Porter Hétu Tax Tips* booklet, visit **porterhetu.com** and click on the office nearest you for our email address.

Or simply email us at **taxtips@porterhetu.com** with your mailing address and a request for the tax tip booklet.

PUBLICATION Porter Hétu International
COORDINATION Aubree Miller
DESIGN JAM Design

Please send your comments/questions to Aubree Miller at **admin@porterhetucpa.com**

DISCLAIMER The information contained in this newsletter is of a general nature. Although all attempts are made to ensure the accuracy and timeliness of the information, an individual or organization should not act upon it without appropriate professional advice and thorough examination of the facts of their particular situation.