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Barristers and Solicitors

RRSP Designations and Taxes

RRSPs are a popular retirement savings device and can be a valuable asset. It is important to ensure that proper planning is in place to avoid unintended consequences which could be devastating to an estate plan.

Under Part III of the *Succession Law Reform Act*, RRSPs are registered plans that can be designated to pass to a particular beneficiary on the participant's death. If passing to a designated beneficiary other than the participant's estate, the proceeds of the RRSP will pass outside of the estate and will therefore not be subject to estate administration taxes. They may generally be immune from the claims of creditors of the estate as well.

This can be a double-edged sword, however. Unless the plan is rolled over, the *Income Tax Act* deems the participant to have withdrawn all of the funds in the RRSP at the date of death. This can lead to a significant tax burden that will, in the absence of planning to the contrary, be borne by the estate of the deceased and not by the designated beneficiary of the RRSP. In other words, the RRSP may pass to the designated beneficiary, and the beneficiaries of the residue of the estate will end up paying the tax. In some estates, this can mostly or entirely wipe out the inheritance that the residual beneficiaries might otherwise be expecting. When this happens, the results can be ugly and can lead to litigation.

There are a few ways to avoid this problem. One is to take advantage of rollover provisions in the *Income Tax Act* that allow the RRSP to be rolled over to a spouse or a dependent child under the right circumstances. Another is to maintain an insurance policy to cover the tax liability on death. Finally, this issue can be avoided if the RRSP is designated to the estate to provide a pool of funds from which to pay the tax. Even though it will attract estate administration tax, it may be the simplest solution.

The best option will depend on the particular circumstances in each estate plan. With some careful attention and planning, this problem is an avoidable one.