Save on taxes with a spousal RRSP

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According to some studies, being married can be good for your health and even help you live longer. But did you know that it can also lead to a tax break?

Contributing to your common-law or married spouse's registered retirement savings plan (RRSP), can help build your partner's retirement nest egg. At the same time, you can lower the amount of tax that you pay collectively.

A tax break now

That's because when you contribute on behalf of your spouse, you get the tax deduction. So if you earn significantly more than your spouse, you will get a bigger tax break by contributing to a spousal RRSP, than your spouse would by contributing to his or her own RRSP. Whether you contribute to your own or to a spousal RRSP, your contribution counts against your own RRSP deduction limit — the maximum RRSP contribution you can claim as a deduction on your income tax return for the current year. Your spouse's contribution limit is not affected, however, by your contribution to a spousal RRSP.

A tax break later

There can also be a tax break down the road, during retirement. Let's assume once again that you are the spouse with the significantly higher income and — as an example — that you've decided that you need to withdraw a total of $5,000 a month, as a couple, from your RRSPs. Thanks to the additional funds you have contributed, your spouse will be able to withdraw a bigger share of that $5,000 from his or her RRSP, which will allow you to withdraw less from yours. Here's how this could result in an income tax reduction for your family in total:

	Total income tax
You withdraw the entire $5,000 per month x 12 = $60,000, taxed at 26%	**$15,600**
You withdraw $4,000 per month x 12 = $48,000, taxed at 26%	$12,480
Your spouse withdraws $1,000 per month x 12 = $12,000, taxed at 15%	+ 1,800
	$14,280 *

* This is only an example; consult a tax specialist to see how it can best work for you.

Spousal RRSPs are subject to a number of rules. After you've made a spousal RRSP contribution:

- The money belongs to your spouse. He or she controls the account and when the money is withdrawn, it's taxed as his or her income as long as certain conditions are met.

- You can contribute to an RRSP until the RRSP owner turns 71. So, if you are over 71 and can no longer contribute to your own RRSP, but your spouse is younger, you can both still benefit. If you still have earned income and RRSP contribution room, you can keep putting money in a spousal RRSP and defer your taxes while your spouse's RRSP grows, until he or she turns 71.

Early RRSP withdrawals can be costly

It's important to remember that spousal RRSPs are meant for long-term retirement savings, not short-term tax shelters. That's why the government imposes a penalty if you withdraw money within three years of contributing to a spousal RRSP.

Generally speaking, if your spouse withdraws money from his or her RRSP, it's taxed at his or her rate. But if your spouse withdraws money within three years of a contribution from you, you will have to claim that withdrawal as your taxable income, not your spouse's. Contributions must remain in the spousal RRSP for the remainder of the current year, and the next two calendar years to avoid being counted as income for the contributing spouse. The date is based on calendar years, not three years from the last spousal RRSP contribution.

For example, let's say you've contributed a total of $40,000 to your spouse's RRSP, $5,000 of that within the last year.

- If your spouse withdraws $9,000 this year, $5,000 of that will be taxed as part of your income, since you contributed that amount in one of the two calendar years before the year of the withdrawal.
- The remaining $4,000 will be taxed as part of your spouse's income.

When you’re considering a spousal RRSP, it’s important to look at your and your spouse’s current financial circumstances, and project what they might look like at retirement. As everyone’s financial circumstances are different, it’s always a good idea to consult a financial professional.