RRSP rollovers

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In 1994, Canadians contributed nearly $21 billion to registered retirement savings plans (RRSPs). Of this total, $17.2 billion were "normal" contributions, those charged against taxfilers' available deduction limits or RRSP room. The remaining $3.8 billion were special transfers or "rollovers" of certain types of income: retiring allowances, or severance payments, which were deposited into taxfilers' own RRSPs, and pension benefits, which were transferred to spousal RRSPs (for definitions see *Supplementary contributions*). As with normal RRSP contributions, the amounts rolled over could be claimed as deductions against current income for tax purposes.

In the early 1990s these deposits became an important part of RRSP savings, not only because of their sheer size, but also because of the types of individuals who made use of these opportunities. In 1995, however, pension transfers to spousal RRSPs were disallowed and, in 1996, limits were placed on rollovers of retiring allowances. The first change in legislation had an immediate effect on retirement savings. The second will become increasingly important in the next few years. This article examines how large these rollovers were, who benefited from them, and who will be most affected by these legislative revisions.

Considerable savings

From 1990 to 1994, rollovers represented approximately 20% of all RRSP deposits. Over this period more than 750,000 individuals claimed $16.5 billion in rollover deductions on their tax returns. The amount of pension income transferred to spousal RRSPs and the number of persons using this option make up only a small proportion of all RPP/DPSP benefits and beneficiaries. In 1994, less than 4% of these payments was rolled over and only 8% of all eligible taxfilers transferred some or all of it.[4] Since there are no data on the number and amount of retiring allowances paid each year, it is not possible to determine what proportion was rolled over or what percentage of eligible taxfilers put all or part of such benefits into an RRSP.

Retiring allowance deposits to RRSPs increased 56% between 1990 and 1994, while pension benefit rollovers grew by 28% (Table 1). For the former, the greatest annual increase occurred in 1991. This was likely the consequence of extensive job layoffs and substantial severance payments to many workers that year.[5] Both the number of persons with retiring allowance rollovers and the amounts rolled over continued to increase in 1993 and 1994, although the average rollover declined from the 1991 peak. Job terminations, particularly of older

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Supplementary contributions

Since 1966, taxfilers have been allowed to transfer tax free retiring allowances and various types of pension income to RRSPs, within certain limits. These rollovers were not subject to taxfilers' standard deduction limits or RRSP room.[1]

Retiring allowances are lump sum payments received by employees on retirement or loss of job and include settlements for unused sick leave, payments in recognition of long service or compensation for job termination. The maximum amount eligible for rollover depends on how long the taxfiler worked for the employer and whether or not he or she participated in an employer-sponsored registered pension plan (RPP) or deferred profit sharing plan (DPSP) during that time. From 1989 to 1995, the limit was $2,000 for each year or part-year of employment, plus an extra $1,500 for each year or part-year before 1989 during which no benefits were accrued under an RPP or DPSP. The allowance had to be transferred directly by the employer to the RRSP to avoid withholding taxes.[2]

Included with the rollovers reported on the tax returns are transfers of specific types of benefits from some pension plans, RRSPs and registered retirement income funds (Revenue Canada, 1993). These amounts are not identifiable, but are small in aggregate and affect few taxfilers.

Pensioners were able to roll over benefits from RPPs, DPSPs, the Canada and Quebec Pension Plan (C/QPP) and Old Age Security (OAS) into their own RRSPs until 1990, when this provision was disallowed. However, from 1989 to 1994 they were given the option to transfer up to $6,000 a year of their monthly RPP or DPSP benefits into spousal RRSPs.[3] This concession was an interim measure until the new tax-assistance legislation implemented in 1991 took full effect. For further information, see Frenken (1995b).

Spousal RRSPs have existed since 1974, when taxfilers were permitted to make contributions subject to their standard deduction limits to an RRSP registered in their spouses' names and to claim these contributions on their own tax returns. Spousal contributions permit the person with the higher income to claim the deduction and the one with the lower income to receive the retirement benefits, often resulting in significant tax savings.

Table 1
RRSP rollovers

	1990	1991	1992	1993	1994
Total					
Number of contributors ('000) *	226	236	255	274	282
Amount contributed ($ millions)	2,542	3,227	3,333	3,652	3,784
Retiring allowances					
Number of contributors ('000)	79	88	95	107	115
Amount contributed ($ millions)	1,866	2,506	2,552	2,804	2,917
Average contribution ($)	23,600	28,560	26,920	26,310	25,450
Pension payments					
Number of contributors ('000)	147	148	160	167	168
Amount contributed ($ millions)	676	721	781	848	867
Average contribution ($)	4,610	4,880	4,890	5,080	5,170

Source: RRSP room file
* *Includes some double-counting, since a few taxfilers may have rolled over both retiring allowances and pension benefits in the same year.*

workers, remained high those years.[6] Many of these workers may have received early retirement incentives, which they would likely have rolled over to their RRSPs.

More than three-quarters of the $16.5 billion rolled over from 1990 to 1994 was from retiring allowances, even though each year individuals with pension transfers outnumbered those with retiring allowance deposits. Many taxfilers making pension transfers might have done so every year and would thus be counted repeatedly, whereas those rolling over a retiring allowance would likely have done so only once.

On average, retiring allowance rollovers were much greater than pension income transfers ($25,450 versus $5,170 in 1994). Lump sum retiring allowances could be quite substantial, particularly for older employees with lengthy job tenure, while the maximum pension transferable was only $6,000 per year.

There is no guarantee that retiring allowances rolled over were saved until retirement, since these deposits are not locked in, but are accessible at any time. Some participants may have been unemployed for some time following their job terminations and others may have been forced into early retirement. They may have drawn on these savings earlier than planned. Nevertheless, the use of this tax-deferral opportunity probably resulted in lower tax charges (see "RRSP withdrawals revisited" in this issue).

Older persons benefited most

In 1994, 56% of persons with retiring allowance rollovers were aged 50 to 64 and they rolled over 64% of the total (Table 2); although 26% were under 45, their share of the total deposits was only 16%. The benefits they received would likely have been much smaller on average than those of older workers and, even if substantial, the amount eligible for rollover would have been limited by the length of their employment. Likewise, because mainly older taxfilers had pension income, most of those with pension rollovers were older. In 1994, four out of five were 60 and over and their transfers represented 79% of the total.[7]

High income was a factor

Pensioners with higher incomes were most inclined to roll over pension payments. Out of every five persons who used this tax-deferral opportunity in 1994, four had total incomes of $30,000 or more. In fact, of this group, about 23% reported $80,000 or more. Nearly all men, they were able to set aside this income in spousal RRSPs and thus reduce their tax obligations while providing retirement savings for their wives. Many of these women were at or near retirement themselves, and since older women generally have fewer income sources than their spouses, these benefits would generate low tax payments.

Similarly, the tax-exempt feature of retiring allowance rollovers tends to benefit high income

Table 2
RRSP rollovers by age groups, 1994

	Retiring allowances				Pension payments			
Age	Number		Amount		Number		Amount	
	'000	%	$ millions	%	'000	%	$ millions	%
Total	**115**	**100**	**2,917**	**100**	**168**	**100**	**867**	**100**
Under 45	29	26	469	16	1	--	4	--
45-49	11	9	272	9	3	2	13	1
50-54	15	13	431	15	7	4	40	5
55-59	26	22	755	26	24	14	130	15
60-64	24	21	673	23	46	27	242	28
65-69	9	8	251	9	52	31	264	30
70 and over	2	1	66	2	35	21	176	20

Source: RRSP room file

taxfilers. The extent to which income plays a role in the use of this option is difficult to determine from the annual tax data, however. The income reported may be misleading: persons with an early-in-the-year job loss might show lower than normal earnings, whereas the lump sum severance payments will raise total income. In any case, though only 4% of all taxfilers reported total income of $80,000 or more in 1994, 37% of those with retiring allowance rollovers did so and their deposits accounted for 60% of all rollovers.

Many taxfilers with rollovers also make normal contributions, another indication that this feature is used largely by persons with higher incomes. Previous analysis of the 6.7 million individuals who contributed at least once to RRSPs between 1991 and 1993 showed that just 3% had rollovers only (Frenken, 1995a). Those with high incomes are more likely to receive such income and more apt to maximize their RRSP contribution opportunities.

More men than women

Men were more likely than women not only to roll over pension benefits – 91% of all 1994 participants were men – but also to deposit retiring allowances (61%). This is not surprising, since women tend more to work part time and to receive fewer benefits, including severance pay.

What about the future?

The February 1995 budget eliminated the retiring allowance rollover opportunity for post-1995 employment. In due course, this change will affect workers retiring or being laid off. For example, someone who started with a particular employer in 1990 and who leaves in 2000 with $20,000 in severance pay will be able to roll over only $12,000, the amount related to employment prior to 1996.

More significantly, the chance to roll over pension benefits to spousal RRSPs ended in 1994 (see *Supplementary contributions*). Besides the tax implications for retired men in particular, this change will affect women's RRSP savings. While their RRSP participation has grown dramatically in the last 15 years, it still lags behind men's and their average contribution remains much lower.[8]

Women's RRSP savings, however, have benefited from spousal deposits, both pension transfers and normal contributions. In 1991, the most recent year for which data on the latter are available, 310,000 women received $1.5 billion in spousal deposits. More than two-fifths of both the number and the amount were the result of pension rollovers.

Because of the recent legislative changes, rollovers will play a diminishing role in the accumulation of RRSP savings. Eventually, all contributions will be subject to taxfilers' deduction limits. Taxfilers with higher incomes (and their spouses, in the case of pensioners) will be most affected. □

■ *Notes*

1 Each year, Revenue Canada calculates taxfilers' RRSP room where applicable, based on the previous year's earnings and other factors. For a detailed description see Frenken (1995b).

2 Up to 30% may be withheld by the employer at the time the benefit is paid. The employee may have to pay further taxes when the subsequent tax return is filed.

3 Benefits from the C/QPP and OAS and lump sum payments from RPPs and DPSPs were not eligible. RPP/DPSP lump sums may still be transferred tax free directly by the employer to the employee's RRSP. They continue to be considered pension savings, even though they are part of RRSP assets administered by financial institutions. Since they are not reported on tax returns, their exact volume is not known. However, they are quite significant. In 1993 (the latest year for which these data are available) $2 billion was withdrawn from trusteed pension funds alone because of terminations of employment. A large portion of this would have been locked in, as required by federal-provincial pension legislation. Most of that would have been transferred to locked-in RRSPs or similar vehicles. These amounts are expected to grow considerably. For further information see Statistics Canada (1996).

4 According to the 1994 Revenue Canada taxation statistics sample file, nearly $24 billion was paid to 2 million individuals that year as "other pensions and superannuation." Besides benefits from RPPs and DPSPs, this amount included registered retirement income payments.

5 Total employment in December 1991 was down 123,000 from a year earlier. Moreover, while some part-time jobs had been created, full-time employment had fallen 150,000 (Cross, 1992).

6 The labour force participation rate for Canadians aged 55 and older continued to drop after 1991 (Akyeampong, 1995).

7 The few who were under 55 were probably receiving disability benefits.

8 In 1994, just 43% of all participants were women and they averaged only $3,200 in contributions, versus $4,470 for men.