

# Establishing an educational path

## Setting up an RESP



A Registered Education Savings Plan (RESP) is a savings tool primarily designed to assist in saving for a child's post-secondary education. Contributions by the plan subscriber for the education of the beneficiary are not tax-deductible. However, investments are not taxed while they are held within the plan. The Canada Education Saving Grant (CESG) and grants offered by some provinces, which accompany RESP contributions, make these plans even more attractive as educational savings tools.

### Establishing an RESP

An RESP is set up by a **subscriber**. This is an individual who enters into a contract with the financial institution that administers the plan. Alternatively, a married couple or common-law partners can be joint subscribers.

Generally, a plan subscriber cannot be changed unless:

- The subscriber dies: The RESP assets will be disposed according to instructions in the subscriber's Will. If the Will designates someone to carry on the responsibilities of being subscriber, for example the spouse of the subscriber, the new designate takes on the rights and responsibilities of being subscriber. That would happen automatically if the spouses are joint subscribers. The subscriber could also delegate his or her executor to manage the RESP.
- Relationship breakdown: If a marriage or common-law relationship breaks down, a former spouse or partner, if the separation or divorce is recognized by a court order or divorce decree, can become the subscriber.

**Are you planning to establish an RESP for a beneficiary? Review your rights and responsibilities as a subscriber with your TD advisor.**

## Plan Types

An **individual plan** can have only one beneficiary, who does not have to be related to the subscriber. Contributions to the plan for the beneficiary can be made until the end of the 31<sup>st</sup> year after the plan was opened.

While we often think of the subscriber and beneficiary of an RESP as parent and child, you can set up a plan for yourself, where you are both subscriber and beneficiary, if you think you may attend a post-secondary institution. For an individual plan, there are no age restrictions.

A **family plan** can have more than one beneficiary who must be related by blood or adoption to the original subscriber. With a family plan, the beneficiaries can include: children, siblings, grandchildren and great-grandchildren. It does not include a subscriber's spouse or common-law partner, or nieces and nephews. The beneficiary must be under 21 when named.

With a **group plan**, the named beneficiary will receive funding from the RESP when enrolled in a qualifying post-secondary program. However, if the beneficiary does not attend a post-secondary institution, the funds can be distributed among other beneficiaries who qualify.

It's important to note that group plans have varying rules. If you intend to establish such a plan as a subscriber, you should fully familiarize yourself with the plan's rules. For example, many group plans do not permit new beneficiaries to be named as substitutes for beneficiaries who did not take advantage of the RESP.

**What type of RESP plan is most suitable for you and your potential beneficiary(ies)? Review the governing rules closely with your TD advisor, and consider the flexibility you may require for the recipient(s) as time goes on.**

## RESP Contributions

There is a \$50,000 lifetime contribution limit for each beneficiary of a plan.

Contributions are not tax deductible. Generally, the grants and income or growth that occurs within a plan are subject to deferral of tax until they are paid out:

- in the form of Educational Assistance Payments (EAPs) to a qualifying beneficiary
- as an accumulated income rollover to a beneficiary's Registered Disability Savings Plan (RDSP)
- as Accumulated Income Payments (AIPs) to the subscriber
- as a gift to a qualifying post-secondary educational institution.

Contributions can be made over a 31-year period — 35 years if the beneficiary in an individual plan is physically or mentally infirm. Enabling the plan to remain open for 35 years allows the beneficiary to continue to pursue post-secondary education while the funds are subject to deferral of tax. Generally, a plan must be terminated by the end of its 35<sup>th</sup> year, or the 40<sup>th</sup> year if the beneficiary is physically or mentally infirm and in an individual plan.

It should be noted that if funds from one RESP are transferred to another RESP for the same beneficiary, the start date for the first plan determines the eventual overall termination date.

If you transfer RESP funds to another RESP for the same beneficiary, there are no adverse tax consequences. However, if one beneficiary is replaced by another beneficiary, the Canada Revenue Agency (CRA) considers contributions for the former beneficiary as having been made for the new beneficiary. This may create an over-contribution scenario, resulting in penalties.

This scenario will not arise if the new beneficiary is a sibling of the former beneficiary and the receiving RESP was established before the replacement beneficiary turned 21.

If contributions are made in excess of the lifetime limit, the CRA will apply a penalty of 1% of the excess amount per month. While withdrawing the over-contributed amount will stop the penalty from being applied, the over-contribution will still count against the beneficiary's lifetime limit.

**Review the RESP you have established with your TD advisor. Make sure you know what your annual contribution limit is. Ensure that you don't over-contribute.**

### Basic and Additional Canada Education Savings Grant (CESG)

To enhance the benefit of setting up an RESP, the federal government has established the CESG. Beginning in 1998 or the year of the beneficiary's birth, whichever is later, every Canadian begins to accumulate CESG room of \$400 a year until 2006 and \$500 per year since then. This continues until the child reaches 17 years of age.

Since January 1, 2007, CESG payments are based on a maximum of 20% of annual RESP contributions or \$2,500, whichever is less. This stipulation encourages contributions to be made over an extended period.

Unused CESG room is carried forward. You have the ability to make two year's of contributions if you didn't contribute in a former year. The total contribution amount could therefore be \$5,000 (2 x \$2,500) in that year, attracting a total of \$1,000 in CESG, rather than usual, annual maximum of \$500.

For example, assume that a child was born in 2012 and his parents do not open and contribute to an RESP until 2014. The following table illustrates the Basic CESG received and the CESG carryforward available based on the assumed annual contributions. It is important to note that in 2017, only the annual maximum of \$1,000 (\$5,000 x 20%) CESG is received based on the \$6,000 contribution. However, the entire \$6,000 is counted towards the lifetime contribution limit of \$50,000.

Year	Annual CESG amount	Accumulated grant room	Qualifying RESP contributions	Assisted contributions*	Basic CESG paid to RESP	CESG carry forward
2012	\$500	\$500	\$0	\$0	\$0	\$500
2013	\$500	\$1,000	\$0	\$0	\$0	\$1,000
2014	\$500	\$1,500	\$2,500	\$2,500	\$500	\$1,000
2015	\$500	\$1,500	\$1,000	\$1,000	\$200	\$1,300
2016	\$500	\$1,800	\$0	\$0	\$0	\$1,800
2017	\$500	\$2,300	\$6,000	\$5,000	\$1,000	\$1,300
<b>Sub totals:</b>			<b>\$9,500</b>	<b>\$8,500</b>	<b>\$1,700</b>	

\*Once qualifying contributions have attracted CESG they become assisted contributions.

Contributions for beneficiaries who are 16 or 17 will receive CESG if:

- contributions of at least \$2,000 are made before the end of the year that beneficiary turned 16; or,
- there are contributions of at least \$100 in any four years before the beneficiary turns 16.

CESG is available from the federal government up to the end of the year the beneficiary turns 17. The maximum amount of CESG that a beneficiary can receive is \$7,200.

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**One of the benefits of an RESP is the receipt of the CESG. Do you know how much CESG your annual contribution will attract? Speak with your TD advisor about how your contributions fit into your overall financial plan to enable you to make the most affordable contributions possible.**

### Canada Learning Bond

The Canada Learning Bond (CLB) may be available to a child born on or after January 1, 2004. Eligibility is available if the child's family receives the Canada Child Benefit, which involves a combination of net income and the number of children the family's primary caregiver has.

To receive the CLB, a family must have more than three children and a net income equal to or less than \$45,916. An initial \$500 is provided when the beneficiary becomes eligible, and an additional \$100 is made for every year of eligibility until the child turns 15, up to a maximum

of \$2,000. The funds are paid into an RESP and do not affect the lifetime contribution limit. The RESP must be an individual or family plan. The CLB cannot be shared with other beneficiaries but any earnings from the CLB can be shared.

### Provincial Government Educational Assistance

Some provincial governments also offer additional educational assistance. However, not every financial institution's RESP includes the ability to add this extra assistance. Before opening a plan, ensure you know the plan's rules around accepting both federal and provincial assistance.

In 2013, **B.C.** introduced the B.C. Training and Education Savings Grant (BCTESG), a payment of \$1,200 that is deposited into an RESP on behalf of the child. The beneficiary must be a resident of B.C. and born in 2006 or later.

If the child was born in 2006, the application must be made between August 15, 2016 and August 14, 2019. If the child was born between January 1, 2007 and August 15, 2009, the grant application must be submitted between August 15, 2016 and August 14, 2018.

The **Saskatchewan** government has provided the Saskatchewan Advantage Grant for Education Savings (SAGES). However, the SAGES grant program has been indefinitely suspended by the province effective Jan 1, 2018. There is a small window of opportunity to take advantage of SAGES before Dec 31<sup>st</sup> 2017. Existing clients may receive grants for existing eligible contributions, by completing a SAGES grant form.

Eligible beneficiaries may receive a grant of 10% on annual RESP contributions up to \$250 a year per beneficiary. The lifetime maximum is \$4,500.

To qualify, the beneficiary must:

- be a Saskatchewan resident when the RESP contribution was made
- named a beneficiary of the RESP
- all beneficiaries of a family plan must be siblings of one another
- the contributions must be made by December 31 of the year the child turns 17

In 2007, **Quebec** introduced the Quebec Education Savings Initiative (QESI) to encourage saving for children and grandchildren. It is a refundable tax credit, paid directly to an RESP on behalf of the beneficiary, equal to 10% of the annual contributions up to a maximum of \$250. Contributions can accrue and be recoverable up to a maximum of \$250, based on additional RESP contributions.

To qualify, the beneficiary must be:

- less than 18
- a beneficiary of the RESP
- a resident of Quebec on December 31<sup>st</sup> of the tax year

The maximum lifetime QESI is \$3,600.

**Consider any other government funding that is linked to the RESP you have established. Are you in one of the provinces that offers extra assistance. Speak with your TD advisor about the potential implications for your named beneficiar(ies)?**

### Impact of non-residency

A **beneficiary** must be a Canadian resident for tax purposes when contributions to the plan are made; however he or she could attend a qualifying institution outside Canada. However, non-resident beneficiaries cannot receive CESG payments. If the plan has received any CESG, the funds must be repaid. Income received

from RESP by a non-resident beneficiary will be subject to withholding tax. The income may also be taxed by the beneficiary's country of residence. A subscriber must be a Canadian resident when the RESP is opened. If he or she subsequently becomes a non-resident, the plan can remain open.

**Have you become a non-resident of Canada after subscribing to an RESP for a child? Has the child decided to attend a foreign institution? Speak with your TD advisor and tax specialist about any government assistance and tax obligations.**

### Funding an RESP

Choosing how to fund an RESP will involve consideration of a number of factors. What are your goals and priorities? What is your cash-flow? How many children do you have, or wish to benefit from an RESP?

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What is your timeline, i.e., how old are your children, *and* how much time do you have to save for their education and your retirement? How much mortgage debt are you carrying? Let's look at an example where you have \$2,500 and are looking at an accelerated payment on your mortgage versus the potential outcomes of contributing to your RRSP or an RESP:

1. If you put the \$2,500 in a mortgage with an interest rate of 2.5%, you would be saving \$62.50 in interest in the next year.

2. If you deposit the funds into an RESP, assuming a return of 4%, you would receive \$500 in Canada Education Savings Grant (CESG) plus the \$3,000 total that is invested would earn \$120 during the next year for a total gain of \$620.
3. If you contribute the \$2,500 into your RRSP, obtain a tax refund of \$1,000 and put it in an RESP, it would attract a CESG of \$200. Assuming a return on the combined \$1,200, the RESP will have earned another \$48.

Next, assume you can only make the basic monthly mortgage payment but are looking at whether to contribute to your RRSP and/or an RESP. Note that you would have to put \$208.33 a month into an RESP to contribute \$2,500 a year, and get the maximum annual \$500 in CESG. To maximize the total amount of CESG that can be collected over a child's youth (before he or she reaches 18) you need to contribute at least \$2,500 annually for 14.4 years to obtain the full \$7,200 of CESG available per child (i.e.  $14.4 \times \$2,500 \times 20\%$ ). Consider starting when your child is young to improve the ability maximize the CESG.

Taking into account these factors, here are a few common RESP funding strategies:

- You fund an RESP straight from your cash-flow;
- You contribute to your RRSP and use the ensuing tax refund to contribute to an RESP. Assume for example that you are able to contribute \$6,250 to your RRSP. Assuming you are in the 40% tax bracket, you would reduce your tax payable by \$2,500 which could be contributed to an RESP.
- If you receive the Canada Child Benefit (CCB) then you can simply deposit that amount into the child's

RESP. The CCB is a tax-free monthly payment made to eligible families to help them with the cost of raising children under 18 years of age. The amount of the benefit changes based on the number of children who live with you, their ages, your family net income, and a child's eligibility for the child disability benefit. (You can find detailed information on the CCB on the Canada Revenue Agency website.)

**Look at your overall financial plan and review the factors that will affect your ability to contribute to an RESP with your TD advisor. Understand the maximum contributions that need to be made, per child, to get the maximum amount of CESG. Consider the options available to you to contribute to an RESP as much as you are able.**

### Taxation of an RESP

As noted previously, RESP contributions are not tax-deductible, but the income and growth/gains within the RESP are sheltered from tax until funds are withdrawn from the plan. If the plan is used as intended, the funds (income and grant portions of the plan) are generally taxed as income to the beneficiary.

The type of investment held within the RESP does not have any bearing on how the beneficiary is taxed. The CRA will not consider whether it is capital gains, dividends or interest income. It is simply taxed as "other income." However, since the student-beneficiary generally has little or no other income, the taxes may be minimal, if any.

**Speak to your TD advisor about the post-secondary education costs of your beneficiary and ensure you make the maximum use of an RESP.**

## Now you have information to assist you to:

- **Establish an RESP for a child**
- **Choose the appropriate plan type**
- **Become informed about the potential government — federal and provincial — assistance available to your beneficiary**



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