



RESPs – No longer just for kids

When most people think of Registered Education Savings Plans (RESPs), they think of an educational savings plan for children. Did you know that RESPs are a great savings plan for adults?

In fact, self-funded RESPs are a smart investment for individuals who are planning on going back to school (i.e. for a change in career or retirement studies), or can even be used as an income splitting tool.

It's a common misconception that Registered Education Savings Plans (RESPs) are only useful for parents saving for their child's post-secondary education. With a little financial savvy, an RESP can not only provide an effective means of funding an adult's education, it can also provide an income splitting opportunity as well.

Generally, investments that qualify for an RRSP, qualify for an RESP with the added benefit of no foreign content restrictions. Unlike RRSPs however,

contributions to an RESP are not deductible; which allows the contributor to withdraw their original capital at any time on a tax-free basis.

In addition, you are not forced to withdraw the funds from the RESP at age 69 and incur an income inclusion, which provides some deferral against income related clawbacks like Old Age Security.

RESP FOR ADULTS - HOW DOES IT WORK?

By opening a non-family RESP and naming yourself both the subscriber and the beneficiary, you can contribute up to \$4,000 per year, and up to \$42,000 total over the life of the plan.

You can invest in a wide array of investments including equity and bond funds, and the investment can compound tax free until withdrawn. You can withdraw your contributions at any time without penalty. However, the RESP has a limited life – it must be terminated within 26 years of its initiation.



WHAT ARE THE RULES FOR WITHDRAWING FUNDS?

You can withdraw your original capital at any time free from taxes. Once you have enrolled in a qualified postsecondary institution, you can begin receiving Educational Assistance Payments (EAP).

An EAP is a distribution to a beneficiary of the RESP's accumulated investment income (and Canada Education Savings Grant (CESG) amounts where applicable) which are taxed in the beneficiary's hands in the year of receipt.

In order for a beneficiary to qualify for an EAP they must be enrolled full-time in a post-secondary level program at a qualifying educational institution in Canada that requires at least 10 hours a week of work or instruction for at least 3 consecutive weeks.

For an educational institution outside of Canada, the course must last at least 13 consecutive weeks.

The amount of the EAP is limited to the lesser of \$5,000 and the amount of the actual expenses for the first 13 consecutive weeks, with no limit on the amount of the EAP afterwards.

The attraction lies in the fact that you are eligible for the EAP regardless of whether you attend or pass the class, and that correspondence classes qualify. In addition, you would be eligible for the education tax credit of \$400 per month of full time enrollment and the tuition tax credit.

Non-family RESPs allow adults to be both the subscriber (contributor) and beneficiary.

Although RESPs for adults are not eligible for the Canada Education Savings Grant, (a qualified 20% top-up paid by the Federal government), they still represent one of the few investments that allow assets to grow on a tax-deferred basis, which is particularly valuable if you don't have any RRSP contribution room.

WHAT IF I DON'T GO BACK TO SCHOOL?

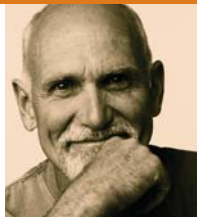
If you don't enroll at a qualifying institution, and the plan has been open for more than 10 years, you can qualify for an Accumulated Income Payment (AIP). An AIP represents the investment earnings in the RESP, and not your original contributions (or CESG amounts where applicable).

Unlike the EAP, which are withdrawals of the investment earnings after you have enrolled at a qualifying institution, an AIP withdrawal is subject to a penalty tax of 20% in addition to the taxes payable when taken into income. It is important to note that the RESP must be terminated prior to March 1st of the year after the first AIP payment is made. If you have contribution room left, you can transfer up to \$50,000 into your RRSP or to a spousal RRSP. This will allow you to avoid the 20% penalty tax (12% for Quebec residents), while generating a tax deduction from the contributions made to the RRSP.

HOW CAN I USE AN RESP TO SPLIT INCOME?

The opportunity for using an RESP to split income arises if you decide not to attend a post-secondary institution.





If you name your spouse as a joint subscriber to the RESP, and your spouse has contribution room left in their RRSP, the AIP can be transferred to your spouse's plan regardless of who made the contributions.

This option is particularly attractive if your spouse is in a lower tax bracket since the taxes paid on the eventual withdrawal will be reduced. It's important to note that if you are going to contribute an AIP payment to an RRSP or spousal RRSP, the contribution must be made in the same tax year, or within the first 60 days of the following year, in which the AIP payment is received. If the RRSP deduction is not claimed within the same tax year, the 20% penalty tax will apply.

If you don't have a joint RESP, you may still be in luck if the RESP allows for joint subscribers by simply adding your spouse as a subscriber and then transferring the AIP to your spouse's RRSP (assuming of course that your spouse has sufficient RRSP contribution room).

ARE THERE OTHER WAYS TO AVOID THE 20% PENALTY TAX?

If neither you nor your spouse has contribution room left within your RRSPs and you still want to avoid the 20% penalty tax, you will have to go back to school.

If you find yourself in this situation, try finding a qualifying post-secondary program with minimal costs and that lasts for more than 13 consecutive weeks. This will allow you to withdraw more than the initial \$5,000 limit described above.

Once the 13 weeks have passed, you can withdraw the money for anything you want and for whatever reason (i.e. to purchase a car). And remember that there is no requirement for you to attend or pass the requirements of the program. That said, you will still have to claim EAP payments as income during the year they were withdrawn.

IDEAL CANDIDATES

- Individuals seeking to return to post-secondary education
- Individuals seeking additional tax deferred investment opportunities
- Individuals who have a spouse in a lower marginal tax bracket and are interested in income splitting

TAKE ACTION

- Complete an RESP application (Form #03285E), and
- Ensure your spouse is named a joint subscriber to preserve the ability to split income

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