

TAXADVISOR

Over the Limit

Withdrawing RRSP overcontributions

COURT REPORT

BY JAMIE GOLOMBEK



With the 2006 RRSP season soon drawing to a close, it's inevitable that one or two of your clients may have inadvertently got themselves into an RRSP overcontribution situation.

The most common source of overcontributions arises from clients who have a group RRSP program

in which their employer makes contributions on your clients' behalf throughout the year. In RRSP season, a frazzled client then calls you in a panic, as the March 1st deadline approaches, looking to "top up" their RRSP contribution since the employer doesn't fully fund up to the client's maximum allowable RRSP limit.

A calculation is done, the client makes a last-minute RRSP contribution and then discovers, a couple of months later when their 2005

tax return is filed and assessed, that they accidentally overcontributed to their RRSP. What to do?

The first step is to ascertain that an overcontribution has really occurred. After all, on Jan. 1, 2006 new contribution room opens up in respect of 2005 earned income so the client may not be in an overcontribution situation. If it is determined that despite the new room the client has still overcontributed, the situation can easily be rectified.

The fastest way to get the money out is to request a withdrawal of amount overcontributed directly from the RRSP issuer. This amount will be subject to withholding tax, which can later be recovered by your

client when she files her 2006 tax return with a copy of the Canada Revenue Agency's Form T746 entitled "Calculating Your Deduction for Refund of Undeducted RRSP Contributions."

To avoid withholding tax, the client can complete CRA's Form T3012A, "Tax Deduction Waiver on a Refund of Your Undeducted RRSP Contributions." Once it has been "certified," the client can submit this to the RRSP issuer and withdraw the overcontributed amount without being subject to the withholding tax.

A question often posed by advisors is whether the withdrawal of the overcontributed amount

must come from the same account that gave rise to the overcontribution.

A tax case decided almost exactly two years ago (*Vale v The Queen*, 2004 TCC 107; 2004 DTC 2362) dealt specifically with this question. On January 5, 2001, Barbara Vale made an inadvertent \$10,000 overcontribution to her RRSP at CIBC. Once she became aware of that, Vale withdrew most of the overcontribution. (Since taxpayers are allowed to overcontribute \$2,000 to an RRSP without penalty, she didn't need to withdraw the full amount to avoid the 1% monthly penalty tax).

The reason she ended up in Tax Court was that the withdrawal was made partly from her CIBC RRSP to which she originally made the overcontribution and partly from another RRSP at TD Canada Trust. The question that the court had to decide was whether a withdrawal from an RRSP that is different from the one to which the overcontribution was made still qualifies for this deduction.

The CRA only permitted her to deduct the amount withdrawn from the CIBC plan. Vale objected and took the matter to court.

The judge, in analyzing the issue, referred specifically to the *Income Tax Act*, which states that a deduction is permitted for a withdrawal of inadvertent RRSP contributions as long as the taxpayer "can reasonably be regarded as having received a payment from a registered retirement savings plan... in respect of such portion of the undeducted premiums."

The CRA argued that the withdrawal from the TD Canada Trust plan did not qualify for the deduction because the withdrawal did not "relate" to the overcontribution.

The judge disagreed and felt that the "broad language used in (the act) suggests that Parliament did not intend to require a strict tracing of the withdrawal and overcontribution."

This finding will be helpful to advisors as it provides them with the flexibility to choose from which of a client's accounts an RRSP overcontribution should be withdrawn. Considerations may include the portfolio mix and asset allocation in each account as well as possible cost considerations if fees may be incurred to dispose of an asset within the account, as opposed to simply transferring it out "in-kind." **AER**

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