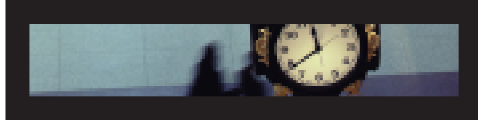
YOUR RETIREMENT SAVINGS PLAN

Securing financial freedom

NATIONAL BANK FINANCIAL



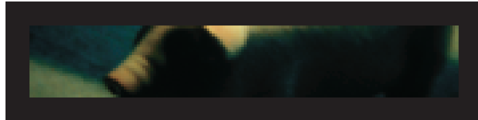
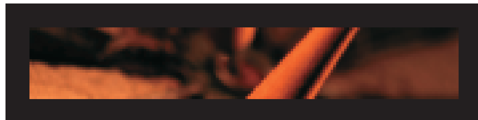
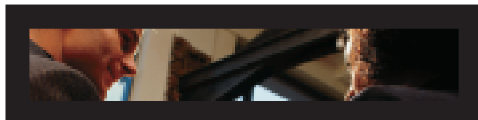
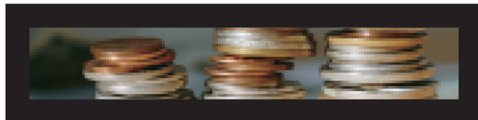
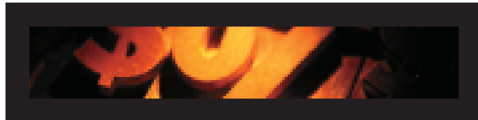
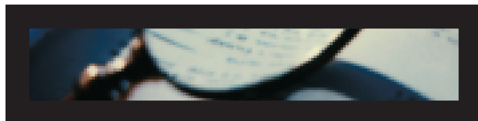
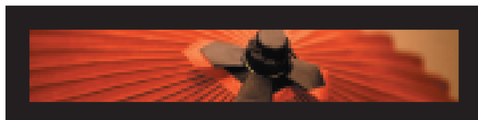








TABLE OF CONTENTS

Retirement Planning: A Top Priority **2**

The Basics of Retirement Planning **4**
- What you can expect from the government 4
- Supplementing the government plans 6
- Allowing for inflation 6

The RSP's Role in Retirement Planning **8**
- Immediate tax savings 8
- Tax-sheltered compounding 8
- Tax deduction + sheltered growth = more savings 8

Choosing the Right RSP **10**
- Three criteria for evaluating an RSP 10
- Four basic types of RSPs 12

The Hands-Down Winner: A Self-Directed RSP **13**
1. Professional guidance 13
2. Account consolidation 13
3. One size does not fit all 13
4. Objectivity 13
5. Capital safety 14
6. Superior long-term returns 14
7. International diversification 15
8. Greater involvement 15

Managing Your RSP Assets **16**

Eight Ways To Make the Most of Your RSP **18**
1. Start early 18
2. Contribute at the beginning of the year 19
3. Make the maximum contribution 20
4. Make use of spousal RSPs 20
5. Contribute securities 21
6. Use the cash accumulated in your RSP 21
7. Fund extended time off or a business start-up 21
8. Be your own mortgage lender 21

Do You Really Know the RSP Rules? **22**
- Contribution limits 22
- Calculating your RSP contribution room 23
- The definition of earned income 24
- Other amounts that may be added 25
  - Retiring allowances
  - Lump sums received from a registered pension plan
  - The cumulative $2,000 excess contribution
- Splitting a contribution between years 26
- Carrying RSP contribution room forward 26
- Eligible investments 27
- Foreign content limits 28
- Shares of eligible private corporations 28
- Partial withdrawals 28
- Interest-free loans 29
- Becoming a non-resident 29
- In case of death 30
- Converting your RSP to an income plan 31

Is Your RSP Protected? **32**

Why Choose National Bank Financial for Your RSP? **34**

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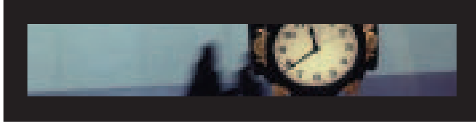

Retirement Planning: A Top Priority

*The combined forces of the retirement of the boomer generation, rising life expectancies and falling birth rates will seriously strain, and could possibly rupture, our retirement and health care systems in the next 30 years.**

Most people now realize it's important to prepare for retirement. But do you really appreciate just how important it is? Look around at today's retirees, and consider what lies ahead.

- Average life spans are increasing. In relative terms, those over 85 are the fastest growing part of Canada's population. If you're in reasonable health, you will likely live longer than today's typical retiree. And, you will likely retire earlier; Statistics Canada says few people now wait until 65. Consequently, your money will have to cover more years.
- Thanks to medical advances and lifestyle changes, you will likely have more years of good health than today's retirees. So, you will be able to enjoy more active pursuits. Think about what you would like to do in retirement – and what that would cost.
- You will get less government support. Cutbacks are already underway because key parts of Canada's social safety net – Old Age Security pensions, the Canada/Quebec Pension Plans and medicare – were designed during the 1960s using demographic and economic assumptions that made sense then, but which later proved to be flawed. Significantly, revenues from active workers were supposed to support retirees. There were 16 workers for each retiree as the first boomers entered adulthood in 1966. But boomers have had fewer children than their parents, immigration has not filled the gap and seniors are living much longer. As a result, there are now just four workers per retiree. And, that ratio is expected to fall to 2-to-1 by 2030, when all boomers will be at least 65. Meanwhile, the needs of an aging population are straining Medicare, which was designed before the development of today's costly drugs and high-tech treatments.
- There are fewer people in employer-sponsored pension plans. Membership peaked in 1991 and now covers just 39% of Canada's workers – many of whom will, no doubt, change jobs and leave their pension plans well before retirement.

** According to the Association of Canadian Pension Management, January 2000.*

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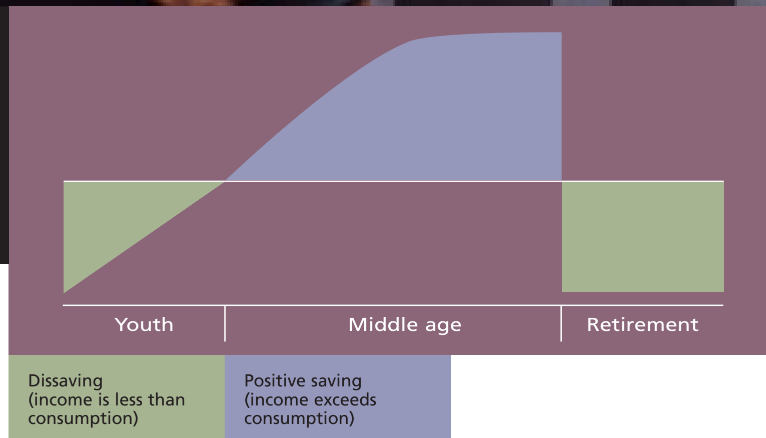
Economic life cycle



Federal officials recognized these trends in the 1980s and concluded that middle- and upper-income Canadians will have to rely more on themselves. So, they substantially increased retirement savings opportunities for those with less than top-notch pension plans. When the current rules were proposed in 1989, the Department of Finance said they were needed *"to encourage the increased private saving that is required now to meet pension needs later."* Providing for the future is not merely prudent; it's a social responsibility.

We urge you to make wealth accumulation for retirement one of your top investment priorities. The choices you make today will significantly affect your future ability to make choices about personal comfort and fulfillment. National Bank Financial prepared this booklet to help you better understand retirement planning and the vital role of a retirement savings plan (RSP). We hope you find it useful. Please don't hesitate to call your National Bank Financial Investment Advisor with any questions.

The Basics of Retirement Planning

No one can realistically hope to have an accurate picture of his or her financial needs 15, 20 or 30 years hence. There are too many uncontrollable variables. Nevertheless, a few projections can provide a rough idea of your future cash flows. You can then create a structured savings program and adjust your planning as the years go by.

What you can expect from the government

There are two main government pension programs: Old Age Security (OAS) and the Canada/Quebec Pension Plan (CPP/QPP). Their benefits are indexed for inflation and taxed as income.

OAS pays approximately $480 per month starting at age 65. These benefits begin to be phased out, however, for retirees with taxable income above the "clawback" threshold of approximately $58,000, and disappear once their annual income exceeds approximately $96,000. Conversely, there is a special tax-free supplement for low-income seniors. It's called the Guaranteed Income Supplement (GIS).

The maximum GIS payment is about $570 per month for a single retiree who has less than $13,700 in other income, including OAS. A couple could receive up to about $940 a month from GIS if they both receive OAS pensions and their joint income is less than approximately $17,900.

If you've contributed to CPP/QPP while working, you will be due as much as approximately $830 in monthly benefits. The actual amount is based on your contributions. These benefits are paid as early as age 60, but on a reduced basis. For example, you get 30% less if you start at 60 instead of waiting for the full entitlement at 65.

So, not counting GIS, government programs should provide $5,760 to $31,440 or so in annual household income. That may not seem like much, but OAS and CPP/QPP are meant to be an anchor, not your entire support. Together, they were designed to replace no more than 40% of the average national wage.

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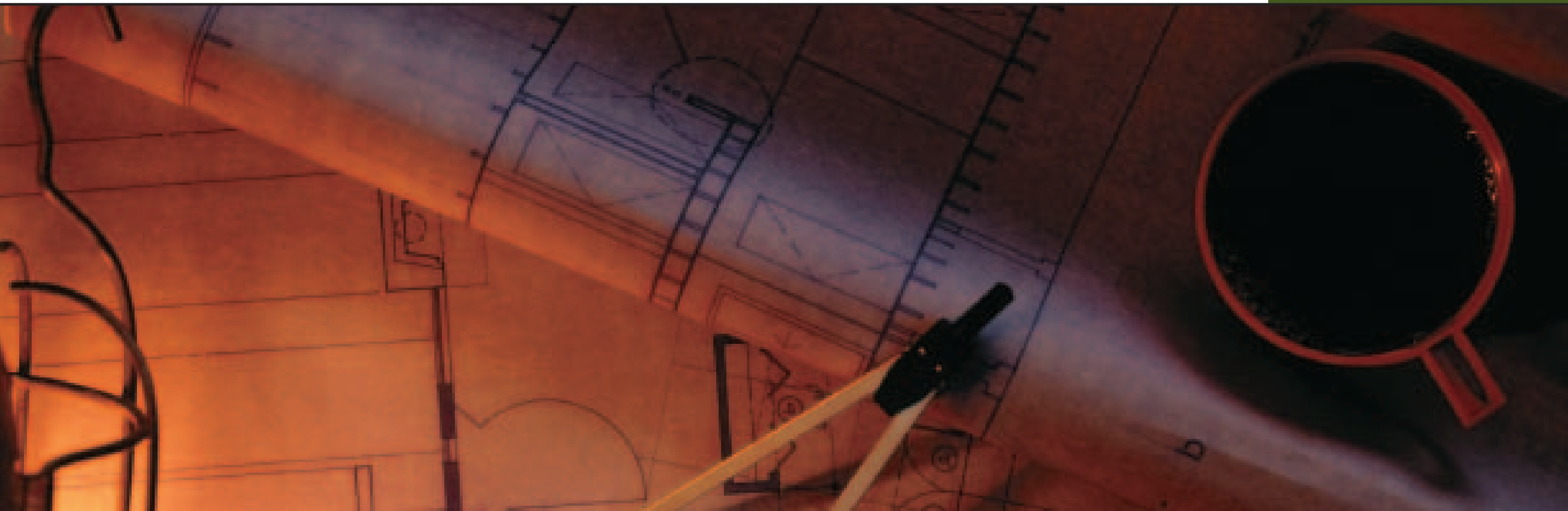


Government benefits

	Single without CPP/QPP	Single 1XCPP/QPP	Couple 1XCPP/QPP	Couple 2XCPP/QPP
OAS	$ 480	$ 480	$ 960	$ 960
CPP/QPP	0	830	830	1,660
Monthly income	480	1,310	1,790	2,620
Yearly income	5,760	15,720	21,480	31,440

Approximated from 2004 figures, maximum entitlement, excluding any GIS.

"OAS and CPP/QPP are meant to be an anchor, not your entire support. Together, they were designed to replace no more than 40% of the average national wage."

Supplementing the government plans

How much income will you need for the lifestyle you deserve after working so hard? Your house may be paid for. Your children will probably be grown, but you might be helping at least one parent well into your own retirement. You will no longer face work-related expenses, but may want to travel, start new hobbies or indulge a few whims. Also consider that while all Canadian provinces have Medicare plans, none cover 100% of your health-related expenses.

As a general rule, if you are now between 40 and 60 years old, 60–75% of your current household income is a good approximation of what you will need for a comfortable retirement.

Suppose, for example, that Richard and Suzanne currently earn $80,000, and would like to retire on 75% of that, or $60,000. Subtracting roughly $20,000 in government benefits leaves a $40,000 gap to be filled by their employer pension plans and personal savings. We'll refer to that $40,000 gap later in this discussion.

Allowing for inflation

OAS and CPP/QPP benefits are indexed for inflation, but your supplementary income estimate is not. You must adjust that part of your projection from "current" to "future" dollars to account for the inevitable loss of purchasing power. Even at relatively low inflation of 3% – the top target level set by the federal government and the Bank of Canada – one dollar 25 years from now will buy less than half of what it buys today. This table assumes inflation will average 3% a year. That's higher than the current rate, but lower than the average 4.8% rate prevailing over the past 40 years.

Equivalent income supplement required (3% inflation)

Annual income supplement required*	Annual income supplement required in...					
	10 years	15 years	20 years	25 years	30 years	35 years
$ 20,000	$ 26,878	$ 31,159	$ 36,122	$ 41,876	$ 48,545	$ 56,277
30,000	40,317	46,739	54,183	62,813	72,818	84,416
40,000	53,757	62,319	72,244	83,751	97,090	112,554
50,000	67,196	77,898	90,306	104,689	121,363	140,693
60,000	80,635	93,478	108,367	125,627	145,636	168,832

** Current dollars*

So, the $40,000 annual gap projected for Richard and Suzanne will actually be $72,244 when they retire in 20 years. Suppose they have no pension plans at work and expect to exhaust their savings over 25 years. How much retirement capital will they need?

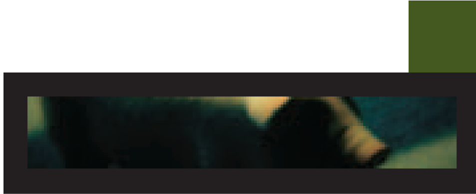
Richard and Suzanne figure they can continue to earn 6% on their money and want their withdrawals fully indexed for 3% inflation. This table shows the approximate capital needed to fund $1 of annual income. Find the point for 25 years, 3% indexing and 6% growth. You'll see it takes just over $18 in savings to fund each dollar of income. Multiply 18.10 by $72,244 and you'll find they need just over $1.3 million.

Capital required to fund $1 of retirement income

Years of income required	Level of annual indexing: No indexing		3%	
	Average annual growth of remaining money: 6%	8%	6%	8%
20	$ 12.16	$ 10.60	$ 15.44	$ 13.23
25	13.55	11.53	18.10	15.00
30	14.59	12.16	20.40	16.39
35	15.37	12.59	22.40	17.49

Assumes full withdrawal made at start of year.

"Even at relatively low inflation of 3% – the top target level set by the federal government and the Bank of Canada – one dollar 25 years from now will buy less than half of what it buys today."



The RSP's Role in Retirement Planning

The savings targets obtained by working with the preceding tables are staggering! Most of us would have little hope of amassing this much wealth without some kind of help. Fortunately, help is available through a retirement savings plan.

An RSP puts two powerful forces to work: long-term compound growth and tax deferral. Compounding means that each year's income is reinvested to earn still more money. RSP tax deferral provides two advantages: immediate tax savings plus tax-sheltered compounding of the plan's earnings. Basically, you are able to invest more than you would otherwise, and that extra money earns a lot more money over time.

Immediate tax savings

RSP contributions are tax-deductible. This means that every $1 you contribute can generate a tax refund of up to 50¢. So, a $5,000 contribution could cost as little as $2,500, with the government footing the balance. The exact amount will depend on your marginal tax rate.

Tax-sheltered compounding

Your RSP's investment earnings compound tax-free until they are withdrawn. While many people focus on the upfront tax deduction, tax-sheltered compounding plays an even more important role in building your retirement savings.

Consider what happens with a regular unsheltered investment. Tax takes as much as 50¢ from every dollar earned. You not only lose that money, but also the future compounding on it. So, the 6% you thought you were getting is really more like 3% after tax. And if inflation averages 3% annually, your capital isn't growing in "real" – post-inflation – terms. In an RSP, the same investment would truly earn 6%, and your capital would grow at 3% a year after inflation.

Tax deduction + sheltered growth = more savings

The chart to the right illustrates these two tax advantages. It compares a $5,000 RSP contribution made at the start of each year to a similar amount invested without tax sheltering. We assumed a marginal tax rate of 50% and a 6% return on both investments. Here's how they did after 30 years:

RSP	**$419,008**
Unsheltered investment	**$245,013**
Difference	**$173,995**

Remember, though, that each $5,000 RSP contribution generates a tax deduction. That's worth as much as $2,500, which could also be invested. We assumed it takes 12 months to actually receive that tax refund, and then invested it outside the RSP. It earns the same 6% as the RSP, but with no sheltering. That reduces the after-tax return to 3%. This builds an additional $116,439 over our 30-year savings period. Adding that to the difference above, we see that in this example the combined effects of the RSP tax advantages would put you ahead by more than $290,000!

Of course, RSP withdrawals are added to your income for the year and taxed accordingly. But those withdrawals will probably occur after you retire, when your income and marginal tax rate are likely to be lower. Also, you will probably spread your withdrawals, and the tax bite, over many years. Still, let's examine the worst-case scenario.

’s Role in ent Planning

Calculating the RSP advantage

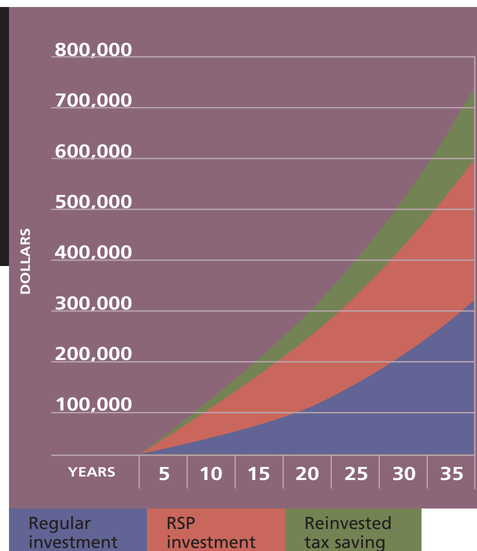
	RSP	Unsheltered investment	Difference
Value after 30 years	$ 419,008	$ 245,013	$ –
Tax due	- 209,504	Already paid	–
Net value after tax	209,504	245,013	- 35,509
Tax refunds invested	116,439	0	–
Total	**325,943**	**245,013**	**80,930**

Suppose you had to cash out the entire RSP in one year and pay 50% tax on its full value.

Collapsing the RSP in one year still leaves $209,504 after tax. Plus, you would have the $116,439 of invested tax refunds. So, even in an implausible worst-case scenario, the RSP still wins by more than $80,000!

RSP tax deferral and long-term compounding enable even modest contributions to become a sizeable retirement nest egg. This explains why RSP savings can consistently grow in real terms while unsheltered investments often do not.

RSP vs. regular investment



“Normally, people are advised to pay annual RSP administration fees directly instead of having them deducted from the plan. That keeps the maximum compounding on a tax-free basis. Consider reversing that when you are about to start tapping the RSP for income. Having the fees deducted from the plan is the same as a tax-free withdrawal.”

Choosing the Right RSP

Every January and February bring a bewildering array of advertisements touting the merits of all the different RSP products offered by a host of financial institutions.

Gathering enough information for an educated choice is an undertaking in itself. Even worse, you often have to deal with someone who has only a basic knowledge of RSPs. Perhaps that's why many people, especially those who look on the RSP as merely a tax deduction, wait until the last minute and go for the simplest, most convenient choices. Often that's a GIC, a money market fund or whatever mutual fund is hot at the moment. Over time, this can easily produce a mishmash of uncoordinated holdings that are probably not good choices for your long-term planning.

Stop and think. Your RSP is so important to your future well-being that it only makes sense to take the time to weigh all the options. Then, make your choice using the same criteria that apply to any other investment: rate of return, capital protection and flexibility.

Three criteria for evaluating an RSP

Rate of return

Thanks to the power of long-term compounding, even a small increase in average return can have a dramatic impact on your retirement accumulation. Suppose you are 30 years from retirement and contribute $5,000 annually to your RSP. If you average 6% in yearly growth, you'll accumulate $419,008. If you average 7%, you'll accumulate $505,365. That difference in performance of one percentage point yields 21% more.

Capital protection

One of the surest ways to build wealth over time is to minimize investment losses, even if that means sacrificing some upside potential. Check the table on page 11; if overly speculative investing wipes out 50% of your RSP, you will have to make 100% on the remaining assets just to break even. Determining your own risk/return ratio involves a compromise between maximizing returns and protecting capital. Don't be too daring, or too cautious. Prudently consider the alternatives and ask your Investment Advisor to recommend those vehicles that best suit your temperament and financial situation.

Growth of a $5,000 annual RSP contribution made at the beginning of the year

Number of years	Rate of return					
	4%	5%	6%	7%	8%	9%
10	$ 62,432	$ 66,034	$ 69,858	$ 73,918	$ 78,227	$ 82,801
20	154,846	173,596	194,964	219,326	247,115	278,823
25	216,559	250,567	290,872	338,382	394,772	461,620
30	291,642	348,804	419,008	505,365	611,729	742,876
35	382,992	474,182	590,604	739,567	930,511	1,175,624

ng the Right RSP

Capital protection: evaluating the cost of speculative investing

Percentage loss	Return required (%) to break even
10 %	11 %
30 %	43 %
50 %	100 %
60 %	150 %
80 %	400 %
100 %	–

Flexibility

It's best to adopt a portfolio approach for your retirement savings, holding a variety of investment vehicles to balance your exposure to inflation and market risk. As well, your investment emphasis should shift through your financial life cycle, from growth to capital protection and, ultimately, income. Flexibility means having the control and choice to make these shifts at appropriate times.

It can be dangerous to be locked into only one type of investment vehicle. Think back to 1981 when that year's Canada Savings Bonds were issued at 19.5%. How would you have felt if all of your money was tied up in GICs at 9%?

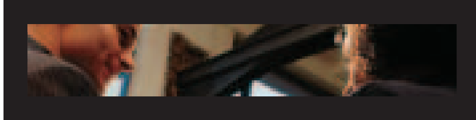
Conversely, high-yielding short-term investments can create a false sense of security. Average yields on short-term Government of Canada bonds averaged about 11% during the 1980s, and people who counted on that continuing were shocked when rates plunged over the next 15 years, and short-term bond average yields fell to around 4%. That's like getting a 60% pay cut. The same is true of equities. Since 1970, annual returns on Canadian common stocks, as measured by the S&P/TSX Index, have ranged from -26% to +45%.

Four basic types of RSPs

RSPs can be divided into four main types. Each one carries the same tax advantages; the difference lies simply in how your contributions are invested. This table summarizes their characteristics. Look for your best combination of potential long-term return, safety of capital and flexibility.

Type	Investment vehicle	Offered by	Advantages	Disadvantages
Savings account RSP	▪ Demand deposits ▪ Interest calculated monthly or daily	▪ Banks ▪ Trust companies ▪ Credit unions	▪ Easily cashed in ▪ Guaranteed investments	▪ Low real return after inflation ▪ Risk of capital erosion from inflation
Term deposit RSP	▪ Deposit certificates with terms to maturity of 1 through 5 years	▪ Banks ▪ Trust companies ▪ Insurance companies ▪ Credit unions	▪ Higher yield than savings account RSPs ▪ Guaranteed investments	▪ Funds are generally locked in for the term of the deposit ▪ Usually no possibility of realizing a capital gain by selling the deposit at a profit ▪ Risk of earning a below-market return when interest rates rise ▪ Some deposits are linked to the performance of a stock or bond index, but can be hard to understand and as a worst case, end up earning no return whatsoever
Investment fund RSP	▪ Money market funds ▪ Fixed income funds ▪ Balanced funds ▪ Canadian equity funds ▪ Foreign equity funds* ▪ Real estate funds	▪ Investment dealers ▪ Investment fund distributors ▪ Insurance companies ▪ Some banks and trust companies	▪ Higher potential return than savings account or term deposit RSPs	▪ Higher potential risk than guaranteed investments – these risks are related to prevailing interest rates, markets and economic conditions ▪ Risks related to the nature of the fund and the competence of the fund manager ▪ Annual administration fees
Self-directed RSP	▪ Investment portfolio composed of GICs, treasury bills, bonds, investment funds, Canadian and foreign* shares	▪ Investment dealers ▪ Some banks and trust companies	▪ Highest potential return ▪ Very flexible ▪ Portfolio can be adapted to the specific needs of the planholder	▪ Planholder must participate in managing the plan ▪ Annual administration fees ▪ Inflation, interest rate and market risks, which can be eased by using a portfolio approach

* *Subject to applicable foreign content limits.*



The Hands-Down Winner: A Self-Directed RSP

We feel a self-directed plan represents the best choice for those who have accumulated $50,000 or more in their RSP, or who will reach that level within a few years. Need convincing? Here are eight good reasons.

1. Professional guidance

Most financial institutions offer several types of plans. Unfortunately, though, they are not always able to deliver informed, objective advice. Financial markets and the RSP rules become more complex each year. When you set up a self-directed RSP, you usually team up with a qualified Investment Advisor who is responsible for providing ongoing service. Professional guidance – aimed at helping you make the most of your RSP – is never more than a phone call away.

2. Account consolidation

RSPs are often opened at the last minute based on clever advertising or because an institution has a nearby branch. The result: a hodgepodge of uncoordinated GIC or mutual fund plans, a multitude of statements, many maturity dates to monitor and no idea of the overall return earned on your retirement savings. A self-directed RSP lets you consolidate all of your existing plans into one easy-to-manage account.

3. One size does not fit all

A 40-year-old who plans to work another 20 or 25 years should take a different approach to saving than a 60-year-old who looks forward to retiring fairly soon. Your self-directed RSP can be tailored to your particular situation; you won't have to settle for anything less than a perfect fit.

4. Objectivity

RSPs offered by banks, other financial institutions and insurance companies are typically limited to that particular vendor's products. Self-directed RSPs are most commonly available at investment dealers, which are not tied to any one product line. For instance, National Bank Financial Investment Advisors have access to a wide variety of investment products from many sources – and are free to recommend the most suitable selection for you.

"When you set up a self-directed RSP, you usually team up with a qualified Investment Advisor who is responsible for providing ongoing service."

5. Capital safety

A self-directed RSP can offer GIC and bond holders protection well beyond the $60,000 coverage from the Canada Deposit Insurance Corporation (CDIC) or the Quebec Deposit Insurance Board (QDIB).

Suppose your current RSP consists of one GIC or term deposit worth $80,000. If the investment's issuer fails, you would get just $60,000 (capital and interest) from CDIC or QDIB. You could, of course, protect the full $80,000 by dividing it between two financial institutions, but would then have two accounts to worry about. Or, you could move your money into a self-directed RSP and then divide it between GICs from two or more institutions. As before, the full $80,000 would be insured, but you would have just one convenient account. Alternatively, a self-directed RSP can hold a wide range of treasury bills, savings bonds and bonds issued by the federal and provincial governments as well as certain Crown corporations. If you hold until maturity, those investments are all 100% government-guaranteed, with no limit on the amount protected.

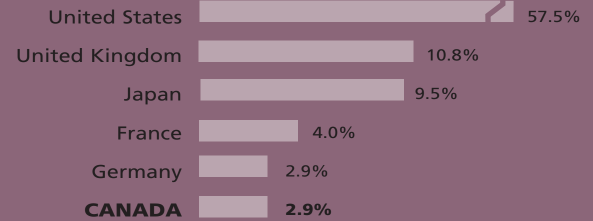
Were you aware that CDIC and QDIB only insure GICs and term deposits running no more than five years? What if interest rates are high and you wish to lock in for a longer term? Bonds issued by the federal and provincial governments, as well as their Crown corporations, run as long as 30 years. And they even come in various foreign currencies. So, a self-directed RSP lets you protect far more than $60,000 with just one account, lock in rates for up to 30 years and even diversify by currency.

6. Superior long-term returns

Diversification has always been the cornerstone of a sound investment strategy. By dividing your capital among several asset classes, you can smooth the volatility of your portfolio and increase your long-term return. For example, over the last 40 years, equities have been the top-performing Canadian asset class 18 times, bonds 13 times and money market instruments 9 times. If your RSP restricted you to only one type of investment, you would have been in the right place a little less than 50% of the time – at best.

All major pension funds base their investment strategies on asset mix and there is no reason why your personal retirement savings should be treated differently. A self-directed RSP is the only type of plan that offers both the flexibility and choice of vehicles necessary for proper diversification.

Canada represents less than 3% of the world's stock markets



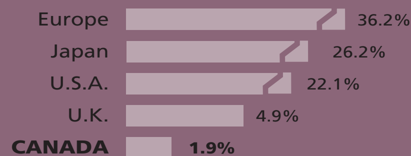
Source: MSCI World Index – country composition

7. International diversification

You can diversify by geographic region as well as by asset class. Research has convincingly shown that geographically diversified portfolios offer higher, less volatile long-term returns than portfolios that concentrate assets in any one country – especially Canada, which offers less than 2% of the world's stock and bond investment opportunities when measured by market capitalization. Conscious of this, the federal government increased RSP foreign content limits to 30% in 2001.

Regular savings account and term deposit RSPs offer no international diversification. Certain mutual fund RSPs do offer foreign exposure, but at the expense of flexibility. The self-directed RSP is really the only type of plan that allows you to take full advantage of the many attractive investment opportunities outside of Canada.

Canada represents less than 2% of the world's bond markets



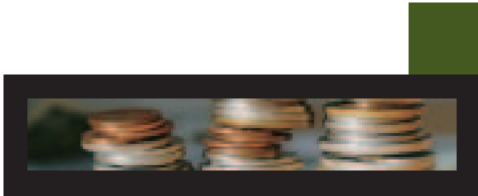
Source: J.P. Morgan World Bond Index – country composition

Effectively, there is no foreign content limit for self-directed RSPs, since there are several ways of investing up to 100% of this type of plan's assets in foreign securities. See the table of RSP-eligible investments on page 27 and our discussion on the foreign content rules on page 28.

Consider your desired retirement lifestyle in setting your own foreign content level. Suppose you hope to spend every winter down south. Keeping 25–50% of your plan in U.S. dollar stocks and bonds, or mutual funds that hold them, would help protect your future ability to buy goods and services in the U.S., the Caribbean and Latin America.

8. Greater involvement

Many people embrace the challenge of managing their own money. Others have no interest at all. A self-directed plan can accommodate the full spectrum. Even though you can make many decisions with such a plan, you don't have to. You might do nothing more than make one annual contribution and put it into a GIC, a bond or a balanced mutual fund. You could also have your self-directed RSP managed on a fully discretionary basis using one of the many products available at National Bank Financial designed to accomplish this. Regardless of how much you do delegate the actual investment management of your RSP, we think that taking an active role in your retirement planning is a very good thing. *Don't forget that your Investment Advisor is there to help you every step of the way.*



Managing Your RSP Assets

Some experts say an RSP should only hold interest-bearing investments that would otherwise be fully taxed. They prefer to keep stocks and equity mutual funds outside the plan in order to benefit from tax breaks for capital gains and Canadian-source dividends. Others insist an RSP should include such equity investments because they are likely to provide the best long-term growth.

If your resources allow you to have both an RSP and a regular investment account, manage them as one large portfolio, weighted according to the asset mix recommendations that our specialists publish quarterly. Then, tax considerations make it advantageous to concentrate interest-bearing securities in the RSP and hold equities in your regular account. However, if your RSP is the bulk of your financial assets, ignore the tax considerations mentioned above and focus instead on RSP investments that will earn the highest return consistent with the amount of risk you are comfortable assuming.

Take your total financial situation into account. For instance, if much of your wealth is invested in your own business, you already have a growth-producing asset. Your RSP should therefore be run more conservatively to balance your financial exposure. If, on the other hand, you are in a defined benefit pension plan, you already have the equivalent of a substantial fixed-income investment, and would likely be well-advised to run your RSP more aggressively with growth-oriented investments such as stocks, equity funds and long-term bonds.

Your definition of risk should also change with your time horizon. Your greatest short-term risk is market volatility since fluctuating stock and bond prices mean your retirement savings may briefly decline in value. However, your greatest long-term risk is inflation because it erodes the purchasing value of your savings year by year. So, money for the near future should be oriented toward guaranteed investments, which ensure capital preservation. Money that won't be needed for many years should generally be placed in growth-oriented investments to counteract the impact of inflation. The key is to properly define your time horizon.

Obviously, the younger you are, the more growth-producing assets you can, and should, hold. Meanwhile, conventional wisdom suggests that as you approach retirement, you should switch to highly liquid, low-risk investments. Consider, though, that someone retiring at 65 stands to live for at least another 20 years. That is certainly a long-term investment horizon. So, even as a retiree, it makes sense to keep at least some of your savings in equities as a hedge against inflation. That's yet another reason to have a self-directed RSP. You can convert this type of plan to a self-directed retirement income fund (RIF) without disrupting your holdings.

ng Your RSP Assets

There is a word of caution, however, if you intend to convert to an annuity. Your investment horizon would then correspond to the time left until your planned conversion. As that date approaches, we recommend switching into short-term investments to minimize the volatility risk of stock and bond markets.

Managing your self-directed RSP portfolio may seem rather daunting, particularly if your investment experience is limited. But remember, you are in good hands. Your Investment Advisor will help translate your situation, resources and objectives into a personalized investment strategy designed to optimize your future financial well-being.

"Labour-sponsored venture capital funds, or labour-sponsored investment funds (LSIFs), have become popular RSP investments because they generate tax credits that equal 15–35% of their purchase price, depending on the province. That's on top of the normal RSP tax deduction. Ever stopped to think why you get this generous tax treatment? It's the government's way of rewarding you for accepting to do venture capital financing with your retirement savings. This is not exactly for the faint of heart, so don't be seduced by the tax credits, and make sure you fully understand what you are investing in before committing your capital. It's also easy to fritter away those tax credits because they put, or keep, money in your pocket only when you file your tax return. When making an LSIF investment, make a note to invest the tax credits – ideally in a more conservative vehicle that will offset the risk you've assumed through the LSIF's venture capital investing."

Eight Ways To Make the Most of Your RSP

The RSP is an invaluable tool for building your retirement capital. We suggest the following eight strategies to help you to get the most out of it.

1. Start early

Even if retirement seems light years away, open your RSP as soon as possible so you can maximize the combined benefits of deductible contributions and tax-sheltered compounding.

Consider this comparison. George contributes $5,000 per year to his RSP from age 20 through 30 inclusively. His contributions total $55,000. Carol starts contributing $5,000 yearly when she reaches age 31, and continues through age 65. Her contributions total $175,000. Assuming an average annual return of 6%, George will have accumulated $609,888 in his RSP, while Carol will have $590,604. Carol contributes more than three times as much to her RSP than George, but he ends up with a larger nest egg. Why? Because George's funds compounded for 11 additional years.

This table shows how a delayed start can significantly reduce the capital available at retirement.

$5,000 annual contribution, 6% return

Savings start at age	Years of compounding	Cumulative contributions	Value at age 65	Growth per $1*
30	35	$ 175,000	$ 590,604	$ 3.37
35	30	150,000	419,008	2.79
40	25	125,000	290,782	2.33
45	20	100,000	194,964	1.95
50	15	75,000	123,363	1.64
55	10	50,000	69,858	1.40

* *Overall average amount of growth for each dollar invested.*

2. Contribute at the beginning of the year

You can make an RSP contribution anytime up to 60 days after the end of the year. But it doesn't pay to wait.

- You are more likely to maximize your savings if you contribute at the start of the year – or even on a systematic monthly basis – than if you rush around at the last minute.
- Contributions made at the beginning of the year benefit from up to 14 months of additional tax-free compounding. In the example below – which assumes a 6% average annual return – both contributors put in the same total amount, but one does so at the beginning of each year while the other waits until the end. The result: 30 years later, the early bird ends up with an additional $33,000 accumulated in his/her RSP.

Remember, too, that cash held outside your RSP typically earns a low rate of interest that is fully taxed. Cash put into your RSP can be invested with a longer-term mindset, so it will likely earn more – and those earnings will compound tax-free until withdrawn.

Obviously, the higher your contribution, the more there is to gain from putting it into the RSP as soon as possible.

$5,000 annual contributions made at beginning of year vs. end of year

After	Start-of-year accumulation	Last-minute accumulation	Difference
10 years	$ 69,858	$ 65,904	$ 3,954
15 years	123,363	116,380	6,983
20 years	194,964	183,928	11,036
25 years	290,782	274,323	16,459
30 years	419,008	395,291	23,717
35 years	590,604	557,174	33,430

3. Make the maximum contribution

You are generally best off making a full RSP contribution, even if you have to borrow. This formula will help you calculate what your maximum contribution could be, based on the amount of cash you have available:

Say your marginal tax rate is 50% and you have $3,000 of available cash. You could borrow another $3,000 and contribute $6,000 to your RSP. Then, use the resulting $3,000 tax refund to pay back your loan. Interest on an RSP loan is not tax-deductible, but the RSP's other advantages will generally more than compensate for the interest cost.

How much? A simple formula

How much can you afford to contribute?

$$\frac{\textbf{Available cash}}{\textbf{100 \% – (your marginal tax rate)}}$$

4. Make use of spousal RSPs

Whether legally married or common-law, you are allowed to contribute to an RSP in your spouse's name. You get the tax deduction, but the contributions will belong to your spouse. This is a long-term strategy for couples with unequal incomes or savings. It's aimed at reducing future tax by dividing retirement income between the couple instead of concentrating it in one spouse's hands. Also, if both spouses have eligible retirement income, they can each claim the pension income tax credit.

Making a spousal contribution does not increase your contribution limit; you simply put part or all of it into your spouse's plan – without affecting his or her own contribution limit. For example, suppose David and Louise each have $5,000 of contribution room this year. The combined $10,000 of contributions may go entirely into David's plan, Louise's plan, or be split in any way between the two.

If you are going to make spousal contributions, your spouse should consider having two RSPs if there is a possibility of he or she making withdrawals prior to retirement – one plan for his or her own money and one for the money from you. That's because spousal contributions face a holding period that runs two years from the end of the year in which the last deposit is made. For example, the holding period for a spousal contribution on January 2, 2005 will run until December 31, 2007. As the contributor, you – not your spouse – will be taxed on withdrawals during that time. This attribution rule would not apply, however, to the other RSP in which your spouse puts only his or her own contributions.

The attribution rule is also waived for withdrawals made while you and your spouse are living apart due to a marriage breakdown, or if one of you becomes a non-resident.

Note that you may continue making spousal contributions even after you have passed the age of 69, when you can no longer have your own RSP. That's if you have qualifying income or unused contribution room and your spouse is 69 or younger. What if your spouse has to turn that RSP into income? There are special rules:

- If the RSP is converted to a retirement income fund (RIF), the attribution rule will apply only to withdrawals above the minimum amount that must be taken from the plan each year.
- If the RSP is converted to a registered annuity, the attribution rule will apply only if that annuity can be cashed out as a lump sum within three years.

Many people automatically assume that a higher-income spouse should be the one who makes spousal RSP contributions. But that's not always the best choice. Remember that the goal is to balance income in retirement. Here are three situations in which it might be better for today's lower-income spouse to make the spousal contributions:

- The lower-income spouse has a good pension plan while the other has a poor one or none at all.
- Through better saving or investing, the lower-income spouse currently has a much larger RSP.
- The lower-income spouse is in line for a large inheritance that can be invested for retirement.

5. Contribute securities

A self-directed RSP is the only form of plan that can accept contributions other than cash. The dollar amount of your contribution equals the fair market value of the securities you put in. There are, however, tax considerations. You will face capital gains tax if the transfer value of the securities exceeds their cost. Unfortunately, though, you are not entitled to apply the loss against taxable capital gains if the securities are worth less than you paid. In that case, first sell the holdings so you can use the capital loss, and then make your contribution in cash.

You could use this cash you contribute to the plan to repurchase the same securities – but only if you wait at least 30 days. The "superficial loss" rules require investors to wait at least 30 days before repurchasing a security on which a capital loss is claimed. There is, however, a wrinkle for mutual fund investors. Your RSP could immediately buy the fund you just sold, but in a different version. Many mutual funds are available in separate versions as RSP "clones" and in corporate class structures. You might then wish to switch back to your original choice after 30 days because the alternative versions typically have somewhat higher built-in management fees. Note that the 2004 federal budget closed a loophole that enabled investors to realize a capital loss outside their RSPs and immediately have their plans buy the very same security. The thinking was that the RSP was legally a separate "person," so the 30-day rule did not apply. The 2004 budget stipulated that an RSP is, in fact, affiliated with its owner and subject to the superficial loss rule.

6. Use the cash accumulated in your RSP

Perhaps you would like to swap eligible investments owned outside your RSP for cash built up inside the plan. That's easily done with a self-directed plan, and generally speaking, there are no tax consequences since this amounts to an exchange. Note, however, that if the fair market value of the securities held outside the plan exceeds their purchase price at the moment the swap is made, this will give rise to a taxable capital gain.

7. Fund extended time off or a business start-up

Your RSP can be used for more than retirement. It's a perfect way to save for periods when you expect to give up employment income in return for time off. For example: a maternity leave, a sabbatical year, unpaid leaves of absence or extended vacations. You will likely be in a fairly low tax bracket if you're on unpaid or low-paid leave. So, your RSP withdrawals would attract little or no tax. Some entrepreneurs live off their RSPs while getting a new business off the ground.

8. Be your own mortgage lender

A self-directed RSP allows you to hold your own mortgage as an investment – just as you would a bond, treasury bill, stock or mutual fund. The RSP provides cash for your home purchase and you pay it back at the same rate as you would to a conventional lender. This can be an attractive RSP investment since mortgage rates are usually up to two percentage points higher than yields on fixed-income securities of similar term. The tax rules require your RSP to charge the same mortgage rate as a commercial lender would. To maximize the growth of your RSP, shop the mortgage market for the highest rate that applies to your desired term, not the lowest. That will mean higher mortgage payments now, but greater tax-sheltered growth for the future. Note, though, that additional fees make this worthwhile only for RSPs that can fund a mortgage of at least $50,000.

Do You Really Know the RSP Rules?

Although it has many excellent features, the RSP is governed by a set of relatively complex rules and provisions. We summarize the main ones below.

- **Contribution limits**

RSP contribution limits – technically called "deduction limits" – are based on your previous year's income. Each spring or summer, the Canada Revenue Agency – formerly Revenue Canada – prints your limit on the Notice of Assessment it sends after processing your tax return for the previous year. That's convenient, but the information arrives too late for those who recognize the benefits of contributing early. Here, we explain how to determine your own limit. Your Investment Advisor will gladly help you apply this to your own situation.This table shows maximum deductible limits currently planned, plus the income required to qualify for them. The government revises the contribution rules from time to time, so we encourage you to check with your Investment Advisor or consult our annual publication, *The RSP Express.*

You are also allowed to exceed your limit by $2,000 without penalty, as discussed on page 25. That is a cumulative lifetime limit; you do not get $2,000 of extra contribution room each year. Excess contributions beyond that limit face a penalty tax of 1% per month.

Yearly contribution limits

Year	Maximum yearly contribution	Previous year's earned income required to be able to contribute the maximum amount
2004	$ 15,500	$ 86,111
2005	16,500	91,667
2006	18,000	100,000
2007	Indexed	Indexed

From 2007 on, the RSP limit will be indexed to growth in the average national wage.

Really Know Rules?

Calculating your RSP contribution room

Your annual RSP contribution room is based on a three-step formula.

First, take 18% of your previous year's "earned income," subject to the limits cited on the previous page. Earned income consists of more than your pay from work; check the list on page 24.

Second, subtract the Pension Adjustment factor (PA) that appears in box 52 of your T4 slip for the prior year. The PA reflects the value of benefits you accumulated in your employer's registered pension plan or deferred profit-sharing plan. Your PA will be zero if your employer has no such plans. You might also have a Past Service Pension Adjustment (PSPA) covering retroactive pension plan improvements. That reduces your RSP contribution room. Or, you might have a Pension Adjustment Reversal (PAR) if you've left a defined benefit pension plan before retirement age. A PAR allows you to contribute more to your RSP by restoring part of the RSP room you previously lost through the PA calculation.

Third, add any unused contribution room from as far back as 1991. That amount is on the Notice of Assessment for your most recent federal tax return. Or, call the Canada Revenue Agency's computerized telephone service. The number is in your telephone directory's blue pages.

Yearly contribution room		
		18% of previous year's earned income, subject to the contribution limits on page 22
	PLUS	Unused contribution room carried forward from previous years
	PLUS	Pension Adjustment Reversal (PAR), if any
	MINUS	Your previous year's Pension Adjustment factor (PA)
	MINUS	Past Service Pension Adjustment (PSPA), if any

The definition of earned income

Your RSP contribution limit is based on earned income for the previous year. As shown below, that involves more than regular salary. For example, net rental income counts. So do alimony payments received. Perhaps you are paid a director's fee for serving on the board of your condominium or a family business. That's included too as "net income from an office." Note, though, that you cannot include pension income, interest, capital gains, dividends or distributions from limited partnerships.

ADD:

- Net income from an office or employment
- Net income from self-employment
- Employee profit-sharing plan allocations
- Disability benefits received from the Canada or Quebec Pension Plan
- Supplementary unemployment benefits – not regular EI benefits
- Royalties from any work or invention you created
- Research grants, net of certain related expenses
- Net rental income from real property
- Canadian-source business or employment income earned while a non-resident
- Alimony and maintenance payments received

SUBTRACT:

- Union and professional dues, and deductible employment-related expenses
- Refunds of salary, wages and research grants
- Current-year net rental losses on real property
- Current-year losses from running a business
- Deductible alimony and maintenance payments

Be aware that everyone who reports earned income generates RSP contribution room. Perhaps your young children earn money from delivering newspapers, mowing lawns or baby-sitting. Or, your teenager might have a regular part-time job. Have the child file a basic tax return reporting that income. It's unlikely that he or she earns enough to owe any tax. Even so, the tax department will allocate RSP room. That means your child can have an RSP and his or her savings can start compounding on a tax-deferred basis. Consider that $100 invested at age 15 and compounding on a tax-deferred basis would be worth almost $2,000 at age 65, assuming 6% average annual growth. If the child owes no tax now, there's no point in claiming a tax deduction for the contribution. Instead, the child can put the money into the RSP now, but wait to claim the deduction until he or she earns enough for it to generate meaningful tax savings. That's handled by filing Schedule 7 with the child's tax return.

Other amounts that may be added

Certain amounts may be added to an RSP without affecting your regular contributions.

Retiring allowances

A retiring allowance may be due at retirement to recognize long service, or it might be a severance payment for a loss of office or employment. Payments for service through 1995, even if they are made after 1995, qualify for transfer to your RSP, subject to the limits shown below. This entitlement is based on service with the employer you are leaving plus any related organizations. This transfer can be extremely beneficial for an entrepreneur who is selling or retiring from an incorporated company he or she created many years ago.

Retiring allowance rollover	
	$2,000 per year of service prior to 1996 with the company paying the retiring allowance
PLUS	
	an additional $1,500 per year of service prior to 1989 with the same company for which you did not accrue benefits under the company's pension plan.

Lump sums received from a registered pension plan

If you leave an employer's registered pension plan before retirement age, you can transfer the present value of your benefits to a locked-in RSP or locked-in retirement account (LIRA). These plans work just like regular RSPs except that withdrawals are generally prohibited. Some provinces do allow early access in cases of financial hardship or health problems. At a certain point – usually the earliest retirement age for the pension plan you left – you can start regular withdrawals by converting the plan to a life income fund (LIF) or, if your province allows, to a locked-in retirement income fund (LRIF). LIFs and LRIFs are similar to a retirement income fund (RIF), but have maximum as well as minimum annual withdrawal limits. A LIF that holds pension money under federal jurisdiction must be converted to a life annuity when you are 80 years old. LIFs under provincial jurisdiction no longer face this requirement, or can be converted at age 80 to an LRIF, which does not require annuitization. Ask your Investment Advisor for complete details.

The cumulative $2,000 excess contribution

The PA calculations – done by your employer – are so complex that federal officials created a penalty-free RSP overcontribution zone to allow for errors. It's available to everyone aged 19 or older. You are allowed to put as much as $2,000 extra into your RSP without penalty. That's a cumulative lifetime limit, not an annual amount.

This overcontribution is not tax-deductible when it goes into the plan, but is fully taxed when it's withdrawn. So, be careful in how you use it. Here are two ways:

- Make the overcontribution and forget about it. Just manage it as you would a normal contribution. That can pay off if the money stays in the RSP long enough for tax-free compounding to more than cover the tax due on withdrawal. For example, assuming 6% average annual growth, breakeven would take about 24 years if your marginal tax rate were 50% at both time of contribution and withdrawal.

- Treat the overcontribution as an advance contribution. Put in the money now and wait for a distant year when you have RSP contribution room but are short of cash. For instance, people in their first year as retirees often find that their lifestyle expenses have not yet dropped as much as their income. You could then have the tax department count your overcontribution against the normal limit you are unlikely to use, and get a tax deduction for it.

Splitting a contribution between years

Contributions made during the year's first 60 days can be applied to your deductible limit for the current year or the previous one. To maximize the value of your deduction, go for the year when your marginal tax rate is higher. For example, suppose your marginal rate is 50% for one year and 48% the next. A $5,000 RSP contribution saves $2,500 in tax at a 50% rate, and $2,250 at a 48% rate.

You can also make your normal RSP contribution, but delay claiming your deduction until you are in a much higher tax bracket. You would submit your contribution receipt with the tax return for the year in which the contribution was made, but also include Schedule 7 which lets you indicate how much – or how little – of the associated deduction you wish to claim. The tax department will then track your undeducted contributions. This is different than an overcontribution in which you put in more than you're allowed. Here, you're using your allotted room but simply not claiming the deduction for it. Understand, though, that this means you lose use of your tax savings until the deduction is claimed. Consider this only if your income will rise substantially over the next few years.

Carrying RSP contribution room forward

If you do not make a maximum RSP contribution, your unused limit will automatically be carried forward so you can catch up later. That provides great flexibility, but you are generally better off using all of your contribution room as it becomes available. Here's why:

- The longer you wait, the more tax-sheltered compounding you give up. At 6% average annual growth, a five-year delay would reduce your accumulation by about one-quarter.
- New contribution room will be added to your unused balance each year. So the longer you wait, the harder it will be to muster enough cash to take full advantage of the RSP's tax-saving opportunities. Ultimately, the accumulated room could become so large that you can never make full use of it.
- The value of the tax deduction for your RSP contributions depends on your tax bracket. A large catch-up contribution could easily drive you down by one, two or even three or more levels. Each time your taxable income drops through a level, that part of your deduction falls in value. Suppose someone with $65,000 of taxable income makes a $40,000 catch-up contribution. The contribution's top $5,000 saves about $2,500 in tax while the bottom $5,000 saves only about $1,250.

Eligible investments

The RSP rules allow a self-directed RSP to hold an incredibly wide range of investments.

Eligible investments

Asset class	Canadian content	Foreign content	Foreign exposure counted as Canadian content
Cash and equivalents	■ Canadian dollars ■ Federal or provincial treasury bills ■ Bankers' acceptances ■ Government of Canada and provincial Savings Bonds ■ Canadian money market investment funds	■ Foreign money market investment funds ■ Foreign government-issued treasury bills ■ Foreign-currency denominated deposits*	
Fixed-income	■ Canadian bank/trust company GICs and term deposits ■ Negotiable bonds and debentures issued by the Government of Canada, the provinces, municipal bodies and Crown corporations ■ Bonds of corporations listed on Canadian exchanges ■ Bonds issued by unlisted Canadian public corporations ■ Mortgages on Canadian property ■ Bond or mortgage investment funds	■ Foreign government-issued bonds with an investment grade rating ■ Bonds issued by foreign corporations that are listed on prescribed stock exchanges ■ Foreign bond investment funds	■ Negotiable bonds and debentures issued in foreign currency by the Government of Canada, provincial governments, municipal bodies and Crown corporations ■ Negotiable bonds issued by certain supranational organizations such as the World Bank ■ Investment funds that hold foreign currency bonds from Canadian and supranational issuers
Equities	■ Shares of corporations listed on Canadian exchanges ■ Canadian equity investment funds ■ Shares of eligible Canadian private corporations (See page 28) ■ Shares in provincial venture capital corporations	■ Foreign stocks listed on prescribed exchanges ■ Foreign equity investment funds	■ Derivative-based investment funds
Multi-class or special	■ Balanced investment funds ■ Certain warrants, rights and options ■ Real estate investment trusts and royalty trusts	■ Limited partnership units listed on a Canadian stock exchange	■ Index-linked GICs

Ineligible investments

An RSP is not allowed to hold:

- Precious metals such as gold and silver bars
- Futures contracts
- Works of art, jewellery or other collectibles
- Employee stock options
- Uncovered call options
- Real estate

Nevertheless, certain items on this list – such as precious metals and real estate – may be held indirectly through investment funds, investment trusts and royalty trusts.

* *Note that although the Income Tax Act now allows foreign-currency deposits as an eligible investment under the 30% foreign-content allowance, to date no financial institution has developed the capability of holding more than one currency in an RSP account.*

Foreign content limits

The 2000 federal budget increased the RSP foreign content limit to 30% for 2001 and subsequent years. Foreign content above this limit faces a penalty tax of 1% per month. Here are some other points you should know:

- Foreign content is measured in terms of the RSP's "book value," not its market value. Book value basically reflects the cost of the plan's investments and changes periodically. Your National Bank Financial Portfolio Statement clearly indicates your current level of foreign content, calculated using book values. Be careful if you are near your limit and hold foreign investment funds. Your RSP could be penalized if the reinvestment of distributions or allocations from any of those funds pushes the plan over the limit.
- Your foreign content position is not affected by your investments' market value. So, there is no problem if your foreign holdings appreciate faster than your Canadian ones.
- Foreign content is determined on a plan-by-plan basis, not on your total RSP assets. It therefore makes sense to consolidate all your RSPs into one self-directed plan to maximize your allowable foreign content.
- A wide range of bonds and derivative-based mutual funds offer 100% foreign exposure, yet qualify as Canadian content.
- Depending on the country and the type of investment, a foreign government may collect non-resident withholding tax on dividends or interest paid out to Canadian RSP accounts.
- Your RSP is granted $3 of extra foreign content room for every $1 it puts into shares of an eligible private corporation or a labour-sponsored venture capital fund, subject to a limit of 20% of the plan's book value. This can increase the plan's foreign content limit to as much as 50% of book value. Consider, though, that private companies and venture capital funds carry extra risk. Evaluate each one on its own investment merits, not simply as a way to boost your allowable foreign content.

Shares of eligible private corporations

Your RSP may hold shares of an eligible private corporation as long as you are not a "connected shareholder" of that company. That means you and your close relatives, singly or together, cannot control 10% or more of any class of the corporation's shares. This 10% determination applies to both options and directly held shares, but is waived if the book value of the shares involved is less than $25,000.

"Your foreign content position is not affected by your investments' market value. So, there is no problem if your foreign holdings appreciate faster than your Canadian ones."

The definition of what constitutes an "eligible" private corporation is complex. If you are interested in holding such shares, we ask that you obtain a written opinion from that corporation's legal counsel stating that the shares are indeed RSP-eligible, and that you are not a "connected shareholder" if the value of your investment exceeds $25,000.

Partial withdrawals

You can withdraw cash or securities from an RSP at any time, but there are tax consequences. The amount withdrawn will be added to your income for the year and taxed accordingly. Part of that tax will be collected at the time of withdrawal. The withholding rate ranges from 10% to 31% depending on the amount and the province in which you reside.

Withholding tax on RSP withdrawals

Amount withdrawn	Quebec residents	Residents of other provinces
Up to $5,000	21%	10%
$5,001–$15,000	26%	20%
More than $15,000	31%	30%

Interest-free loans

Two special programs let certain people take interest-free loans from their RSPs:

- **Home Buyers' Plan (HBP):** You can borrow up to $20,000 to buy a principal residence if neither you nor your spouse owned one in the past five years. Your spouse can also borrow up to $20,000 from his or her RSP. The money must be repaid within 15 years starting 2 years after the withdrawal.
- **Lifelong Learning Plan (LLP):** You can tap your RSP or your spouse's if enrolling full-time in a recognized educational program of at least three months. You can borrow up to $20,000 over four years, taking no more than $10,000 in any one year. The RSP must be repaid within 10 years starting 5 years after the first withdrawal.

The disabled get special eligibility concessions.

Each program requires a minimum annual repayment. If you miss any, the amount is considered an RSP withdrawal. It's then taxed as income for that year and can't go back into your plan.

An HBP loan can be useful if you need just a bit more cash to avoid expensive default insurance. The LLP is better than the straightforward RSP withdrawals done by many students, because LLP withdrawals are not taxed and go back into your plan. Otherwise, think very carefully before using these programs; this is not free money. Your cost is the growth your RSP gives up while the loan is outstanding – plus all future compounding on those earnings. The younger you are, the greater the potential cost. If repayment takes the full 10 or 15 years, the lost compounding could easily make this far more expensive than a conventional loan. Your cost will be even higher if the repayments – which are not tax-deductible – take so much cash that you can't afford full RSP contributions in future years.

Note that, to prevent quick flips, you lose the tax deduction on RSP contributions made within 90 days of an HBP or LLP withdrawal.

Becoming a non-resident

You do not have to close your RSP if you leave Canada. Your capital and its ongoing earnings will remain sheltered from federal and provincial tax. You should, however, consult a tax expert to determine if your new country of residence will tax the plan.

You can even continue to make RSP contributions if you have Canadian-source income or unused contribution room from previous years. Of course, the related deductions are usable only on a Canadian income tax return.

RSP withdrawals made before leaving Canada are considered taxable Canadian income subject to the regular withholding rates. Withdrawals after your departure are subject to non-resident withholding tax. This tax rate is set at 25%, but might be lower if your new country of residence has a tax agreement with Canada. If you convert your RSP into an annuity, Canada will deduct non-resident withholding tax from your annuity payments. Check with your new country of residence to see if it will tax those payments as well.

In case of death

You are entitled to designate a beneficiary for your RSP. This beneficiary may be a person, your estate or a registered charity. The designation can be conveniently made on the RSP contract form, if your province recognizes that, or in your will.

If you die without designating a beneficiary, the RSP will be closed, its full value will be paid to your estate and that amount will be taxed as part of your final year's income.

Recent years have seen several major changes in the RSP beneficiary rules. The table below summarizes your options.

If you have a spouse, your will should also authorize your executor(s) to make two other payments to his or her RSP:

- A spousal RSP contribution if you have not used up your contribution room. This must be done within 60 days of the end of the year of death, and will be deductible on your final return.
- A non-deductible overcontribution to the extent that you have not used your cumulative $2,000 overcontribution cushion. Since there is no tax deduction, this is advisable only if your spouse can let the money remain tax-sheltered long enough to more than offset the tax due when it is withdrawn from his or her RSP.

Some older people buy life insurance to replace the income tax due on their RSP or RIF at death. That maximizes the estate left to their heirs. Your National Bank Financial Investment Advisor can help arrange such coverage through our exclusive insurance brokerage, NBF Financial Services. Due to the way that insurance is priced, this can often work well for couples who buy a policy that pays off only on the second death. Whether it's worthwhile for a single person will depend on his or her specific situation. Ideally, the heirs should pay the insurance premiums since they will be the ones to benefit.

Summary of your options

Beneficiary option	Considerations
Your estate	This designation provides the most flexibility, but only if your will authorizes your executor(s) to make any allowable transfers, considering tax efficiency and need. They would file income tax form T2019. This lets them assess your tax position and optimize the use of tax-free transfers and taxable payouts. Be aware that your province may levy probate fees when the money is paid to your estate. Those fees, however, may prove minor in comparison to the potential tax savings for your family members.
Your spouse, married or common-law	This is the most common designation. The money can be transferred tax-free to your spouse's RSP or RIF, or be used to buy an eligible annuity in his or her name.
Dependent children and/or dependent grandchildren	If the beneficiary is physically and mentally healthy, your RSP money can be used, tax-free, to buy an annuity that pays regular income until the child turns 18. Each annuity payment will then be taxable for the child. If the beneficiary is physically or mentally infirm, your RSP money can be used to support the child for life. It can be moved to an RSP in the child's name. Or, it can be used to buy a life annuity for the child or a fixed-term annuity that makes payments until age 90. In each case, tax applies to the child's periodic income, not the initial transfer. Before the 1999 federal budget, this option was available only if there was no surviving spouse.
Registered charities	Your RSP's value can be paid, tax-free, to the named organization(s). Your estate would face tax on that withdrawal, but gets an offsetting charitable donation tax credit. This direct designation was provided for in the 2000 federal budget.

Converting your RSP to an income plan

You may convert your RSP to an income plan at any time, but must do so no later than the end of the year in which you turn 69. RSPs were designed to provide retirement income, not a permanent tax shelter. Note that the "maturity" deadline is December 31 of your 69th year, not your actual birthday. Also, you can make contributions right up to that point.

There are four options in closing your RSP. Any or all of them can be combined.

- Make a lump sum cash withdrawal or transfer out the securities intact. The full value will be taxed as income, which makes this option less attractive than those below.
- Transfer the RSP assets to a retirement income fund (RIF). You maintain control over your savings and take income until the plan is exhausted. You must make at least one annual withdrawal, based on a schedule of minimums that rise as you age. This withdrawal need not be in cash; you can take out securities that equal or exceed the required withdrawal amount. There is no maximum withdrawal limit, but you should carefully manage your plan so it does not run out too soon. To maximize the tax shelter, you can base your required withdrawals on the age of your spouse if he or she is younger. You can also set up a RIF just before the maturity deadline and delay your first withdrawal until the end of the following year.
- Use the funds to buy a life annuity, providing regular income. A single life annuity guarantees income for as long as you live. A joint annuity will run until you and your spouse both die. There is no estate value unless you arrange for a minimum number of payments and death occurs within that guaranteed period.
- Use the funds to purchase a fixed-term annuity that provides regular income until age 90, and pays out a lump sum if death occurs before then.

Ask your National Bank Financial Investment Advisor about our *Portfolio* RIF, a self-directed plan, as well as the various types of annuities we offer. We can also arrange for guaranteed deposit-based RIFs from a variety of financial institutions. You will find more details in the National Bank Financial publication entitled *Your Retirement Income – The Road Ahead.*

Many 69-year-olds have earned income from property rentals, director's fees, business ownership interests, royalties and other sources. That creates RSP contribution room for the next year even though they can no longer have an RSP. Here is how that room can be used:

- If your spouse still has an RSP, you can make spousal contributions to his or her plan. You get the tax deduction.
- Consider a last-minute overcontribution that equals the room you will get in the new year. Suppose you have $30,000 of earned income this year. That would create $5,400 of RSP contribution room. Make a $5,400 overcontribution in December, just before closing your plan under the age-69 maturity rules. You will face a 1% overcontribution penalty for that month, costing $54. On January 1, the system will create $5,400 in new room and legitimize that overcontribution. You will face no more penalties, and you will get a $5,400 tax deduction.

Is Your RSP Protected?

Financial markets – and the financial industry itself – are undergoing incredible change. Change is often accompanied by uncertainty, so it's important for you to be aware that your nest egg benefits from sound protection.

National Bank Financial: A century of proven strength

It should go without saying, but it's still important to keep in mind – your money's first line of defense is in the solidity and credibility of your financial institution. Since 1902, National Bank Financial has developed sound business practices to adapt to continually evolving economic environments.

With every investment decision comes the notion of risk, and as such, a personal tolerance level with respect to market volatility is one of the most important decisions you will make. However, your choice in the financial institution with which to invest your money should always be a sure thing. National Bank Financial clients are particularly fortunate in this regard. Our century-long history speaks not only to NBF's vast investment expertise, but also to our ability to maintain financial solidity, credibility and trustworthiness in any circumstance. Today, each branch of NBF's coast-to-coast network has inherited this enviable tradition.

Canadian Investor Protection Fund: Solid coverage

Client accounts at National Bank Financial and all other members of the Investment Dealers Association (IDA) of Canada are protected by the Canadian Investor Protection Fund (CIPF). This fund safeguards the public from the insolvency or bankruptcy of an IDA member firm. Your general accounts are protected for up to $1 million. Together, your retirement plans – RSP, RIF, LIRA, LIF and LRIF – also have $1 million of coverage.

As well, education savings plans are insured separately to $1 million. For more details, ask your National Bank Financial Investment Advisor for a copy of CIPF's official information leaflet or contact the CIPF directly.

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RSP Protected?

Other forms of protection

Please note, also, that cash balances of up to $60,000 in registered plan accounts are covered by traditional deposit insurance – as these amounts are held by our registered plan trustee.

Furthermore, fixed-income securities, such as bonds, strip bonds and treasury bills, enjoy their own guarantee as far as yield and maturity value are concerned. This guarantee is unconditional and unlimited for securities issued by a government or one of its agencies. However, the value of other securities, such as common stocks or investment funds, is dependent on market fluctuations and is in no way guaranteed. Lastly, as National Bank of Canada and National Bank Financial are separate corporations, the securities offered by the latter are not guaranteed by the former, with the exception of certain of those issued by the Bank itself.

Why Choose National Bank Financial for Your RSP?

National Bank Financial and its predecessor firms have been serving Canadians since 1902. Today, through 86 branches and more than 750 Investment Advisors, we counsel close to 300,000 individual investors all across Canada.

Why have these people entrusted us with $42 billion of their money – and more than $14 billion of that in retirement plans?

Strength

National Bank Financial is not only one of Canada's largest brokerage firms, but also a solid, well-capitalized subsidiary of the National Bank of Canada, one of the country's six largest chartered banks.*

Service

With more than 100 years of experience, we take immense pride in the enduring relationships we have had with successive generations of Canadian families – and in the quality of the advice and service we have provided them.

Significantly, our mandate is not to be Canada's biggest retail brokerage, but rather one of the best. Corporate commitments to objective, professional conduct and industry leadership in technology enable our Investment Advisors to deliver the old-fashioned personal service on which our business was built – but with the speed, depth and accuracy that the 21st century demands. Today's Investment Advisor must do more than recommend securities. He or she must be able to help you analyze your total situation, devise a suitable plan, answer your questions and address your concerns as they arise, and provide the detailed information required to manage your investments year after year. Whether it's a performance report, portfolio analysis, cash-flow projection or what-if modelling from our exclusive planning software applications, the data you need is just a few keystrokes away. More importantly, you get more than numbers – you get a personalized explanation of what they mean.

** National Bank Financial and National Bank of Canada are separate entities. Securities sold by National Bank Financial are not guaranteed by National Bank, with the exception of certain of those issued by National Bank itself.*

hoose National Bank
al for Your RSP?

Scope

Year after year, institutional investors surveyed by Brendan Wood International give National Bank Financial top marks for the quality of its investment research. Meanwhile, the media regularly look to our Economics and Strategy team for insights on social and political developments that affect both domestic and international markets. These research reports and commentaries are readily available to National Bank Financial clients. Clients also automatically receive our quarterly *Investment Strategy* newsletter, which reviews market trends and updates asset mix, sector rotation and bond duration recommendations.

The effort you put in today will greatly affect your personal comfort and fulfillment for many years to come. Speak to a National Bank Financial Investment Advisor about your retirement planning. You'll find we'll gladly take the time to talk to you. If you don't already have a National Bank Financial account, you can locate our nearest office by visiting us at www.nbfinancial.com.

What our clients say:

"You reach a point in your life when you have to start thinking seriously about financial security and providing for the future. You want an advisor you can trust, a plan that makes long-term sense and strategies that work. That's why I transferred my investments to National Bank Financial."

"I find it reassuring that, unlike many financial institutions, National Bank Financial does not have its 'own' stocks, bonds or funds. They don't have any vested interest in recommending one thing over another."

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