



Individual Pension Plan

If you are a business owner saving for retirement, you have an additional alternative to the traditional Registered Retirement Savings Plan (RRSP). It's called an Individual Pension Plan (IPP).

IPPs have been available for over ten years but were rarely seen in practice because of high administration costs and low pension limits. Now, IPPs are offered at much lower cost and the government is finally increasing the limits for tax-sheltered pensions. The combination of these factors has sparked renewed interest in IPPs.

An IPP is a registered defined benefit pension plan similar to those offered by many large employers and government organizations to their employees. The main difference is that an IPP generally has only one member: the business owner-manager.

With an IPP, your company contributes to the plan and receives a tax deduction. The amount of each contribution depends on your age and salary. The plan is designed to provide you with an indexed pension equal to a percentage of your earnings, subject to an upper limit set by the legislation.

If you are over age 40, the contributions will normally exceed the maximum RRSP limit that would otherwise apply to you. This is the major benefit of an IPP – annual contribution limits can significantly exceed RRSP limits, particularly for older employees.

Your company can also make a potentially large past-service contribution when the plan is initially set up.

A further benefit of IPPs is that, unlike RRSPs, the IPP fund assets are creditor-proof. Similarly, you own any

surplus remaining in the plan once the benefits are paid. This means that the value of the plan is not lost if you die or your employment is terminated.

If the IPP's investment performance is poor, your company is required to fund the deficiency, and will receive a tax deduction for doing so. In contrast, RRSPs prevent you from making extra tax-deductible contributions to cover investment losses.

Your company can deduct IPP investment management fees. With RRSPs, there is no deduction for these fees.

Additionally, IPP benefits are eligible pension income that qualifies for pension income splitting. This will allow the recipient to transfer a maximum of 50% of the income to their spouse. As well, the pension received is eligible for the \$2,000 pension credit, which is also available to the spouse on splitting the income.

With all of these advantages, it might appear that IPPs are a "must have" for most owner-managers. But there are some disadvantages of which you should be aware.

The greatest drawback is a lack of flexibility in the timing of retirement benefits. IPP benefits are firmly locked in until retirement and the benefit amounts are pre-defined. With RRSPs and RRIFs, you can access some or all of the funds any time you wish.

Another potential concern is the requirement of mandatory funding. With RRSPs, contributions can be skipped if cash flow is a problem. IPP contributions, however, must be made, regardless of the profitability of the business. Well-established and profitable businesses that can comfortably afford these

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contribution obligations are therefore best suited for IPPs. Unlike the case with RRSPs, if a company borrows to make an IPP contribution, the interest on the loan is tax-deductible.

A further contrast between IPPs and RRSPs is that, if the IPP investment performance exceeds expectations, your company's contribution obligation is reduced or eliminated. This could lead to a situation where contribution limits to the IPP fall below what could otherwise be contributed to an RRSP.

As well, IPPs will not allow you to build up a pool of retirement assets for a lower-income spouse. You can do this with a spousal RRSP, whereby one spouse contributes to the plan and receives the tax deduction, but the other spouse pays the tax on the eventual withdrawals, with the expectation of paying a lower tax rate. There is no such thing as a spousal IPP. However, a similar result can be achieved with the pension income splitting option discussed previously.

Finally, IPPs have higher administration costs than do RRSPs. There are set-up costs, annual administration fees, and mandatory actuarial valuations. These costs, however, are tax deductible to your company, reducing the effective cost.

A typical "good fit" candidate for an IPP is an owner-manager, over 45 years old, who has been drawing an annual salary of \$100,000 or more for several years. To determine whether an IPP is right for you, please contact your Collins Barrow tax advisor.

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Our Tax Team Members are:

Robert Rock, CA, CFP is a Partner of the firm and brings over 25 years of professional expertise providing income tax, executive compensation planning commodity tax, business reorganization and succession and financial planning advice to a wide range of clients. Contact Rob at: rock@collinsbarrow.com

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Why Collins Barrow Ottawa LLP

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