

The following two articles are reprinted with the permission of the author. They appeared in News North.

TAX BREAK

Financial Assistance for Disabled Canadians

Part 1

Here's a no-brainer. You should participate in the new Registered Disability Savings Plan (RDSP) introduced by the federal government in 2008 if you or your child has a severe disability.

The RDSP, copied after the current Registered Education Savings Plan program, has benefits you can't afford to pass up either. It's a chance to set money aside and allow the investment income to grow tax-free while receiving generous government grants and bonds. The goal of the RDSP is to allow you to accumulate a large pool of funds for yourself or your disabled child.

Let's follow the cash to see how an RDSP works. There are four incoming streams of funds into an RDSP- your contribution; income earned in the plan; federal grant and the federal bond.

Your contributions to an RDSP are not tax-deductible. However, it isn't taxable when it is withdrawn either. The maximum contribution is \$200,000, with no annual limit. Here's a neat feature - anyone can contribute to the plan, including relatives, friends and community groups. Contributions to a RDSP can be made until the end of the year the disabled beneficiary reaches age 59. Only the disabled person – the beneficiary of the RDSP - can withdraw the contributions.

Your contributions attract generous matching federal grants. If your (or the disabled child's) family income is more than \$75,000, the government fully matches the first \$1,000 of contributions. Therefore, even high-income families will receive the minimum grant of \$1,000 annually, if they contribute at least \$1,000 annually to an RDSP.

If the family's income is less than \$75,000, the grant goes into serious overdrive. The marching grant is 300% on the first \$500 contribution, or \$1,500! On the next \$1,000 contribution, the grant is 200%, or \$2,000. Therefore, a family with total income of less than \$75,000 receives total grants of \$3,500 annually, if they contribute a minimum of \$1,500 annually. These grants are payable until the beneficiary reaches age 49 with a lifetime limit of \$70,000.

And that's not all. Families with very low incomes, of less than \$20,900, receive a bond of \$1,000, paid to the RDSP annually. Low-income families with annual incomes of between \$20,900 and \$37,200 will receive a reduced annual bond of \$500. Get this - the bonds are automatically paid into the RDSP annually even if no annual contributions are made to the RDSP. A qualifying RDSP will receive the bond until the beneficiary reaches age 49. The maximum lifetime bond is \$20,000.

The final stream of funds into the RDSP will come from investment income earned by the money from contributions, grants and bonds. This income grows tax-free until the beneficiary withdraws the money.

Anyone who qualifies to claim the Disability Tax Credit (<http://www.cra-arc.gc.ca/E/pub/tg/rc4064/README.html>) can set up an RDSP with their financial institution of choice. The BMO Bank of Montreal is the first major bank to offer the RDSP starting on December 22, 2008. Because of this late starting date, the federal government announced last week the 2008 RDSP registration deadline is extended to March 2, 2009 to enable you to take advantage of the 2008 grants and bonds.

If the disabled individual is a minor (under age 18), a parent, grandparent or guardian can create the RDSP with the disabled child as the beneficiary. If you are a disabled adult, you or a legal guardian creates the RDSP.

For RDSP info: <http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/rdsp-reei/menu-eng.html>

Andy Wong, CGA, CFP, is a tax consultant at Mackay LLP, Chartered Accountants, in Yellowknife. He can be reached at AndrewWong@Yel.MacKay.ca

TAX BREAK

New financial aid for the Disabled - Part 2

The previous TaxBreak looked at the nuts and bolts of the innovative Registered Disability Savings Plan (RDSP) that provides long term financial aid to disabled Canadians starting in 2008.

This follow-up article discusses why you should set up an RDSP and the BIG trap for the unwary. But first, a quick recap. You put money into an RDSP to support yourself or a disabled child in the future. Your contributions, while not deductible to you, are matched by federal grants. Low income families also receive an additional bond. Altogether, an RDSP could receive up to \$70,000 in grants and \$20,000 in bonds.

Any Canadian who qualifies to claim the Disability Tax Credit can set up an RDSP. If the disabled individual is a minor (under age 18), the parent, grandparent or guardian sets up the RDSP with the disabled child as the beneficiary. If you are a disabled adult, you set up your own plan and are the beneficiary.

Setting up an RDSP has no downside and a huge upside because of the generous grants and bonds. As well, the investment income in the plan grows tax-free, and your disabled child (not you) pays tax when the grant, bonds or investment income are withdrawn. The contributions can be withdrawn tax-free.

Here's how the plan works. We assume a family with total income (Mom's and Dad's) of \$100,000, making annual contributions of \$1,500 to an RDSP for their disabled 10-year old son, James. We also assume James goes on to earn an annual income of \$20,000 as an adult (age 18 on) and does not marry.

Under this scenario, during the first 7 years while James is a minor, the RDSP grows slowly from the accumulation of annual contributions of \$1,500, annual grants of \$1,000 and investment income earned in the plan. The RDSP receives no bonds due to the family's high income.

Things start to pop when James becomes an adult at age 18 because at that time his income, not his Mom's and Dad's, is used to calculate the federal grants and bonds. . As a result, the annual federal grant jumps to \$3,500 (from \$1,000) and the plan also receives an annual bond of \$1,000 because of James's low income. (If James marries or lives common-law, his spouse's income gets counted and would reduce his annual grants and bonds).

The annual grants and bonds is payable until the beneficiary (James) reaches age 49, provided the \$1,500 annual contributions are made. In this example, if you invested the contributions, grants and bonds over the 40 years period, assume a modest 5% return, the value of the RDSP would grow to about \$600,000 when James reaches age 50. All that from the contribution seed money of \$60,000 (\$1,500 x 40 years)!

There is one catch, not surprisingly. As soon as James makes a withdrawal, the last ten years of grants, bonds and associated investment income is repaid to the federal government. That's punitive but with a good reason and there is a simple way to avoid it.

The harsh 10-year claw back is there to ensure the RDSP is used to promote long-term retirement savings, i.e., James won't cash out at age 20, etc. It also discourages James from making withdrawals to fund contributions to get more grants and bonds.

If James starts his withdrawals at age 59 (and not earlier), the 10-year clawback won't apply because the federal grants and bonds stopped 10 years ago, when he reached age 49.

You can set up an RDSP at your bank or call your investment broker.

Andy Wong, CGA, CFP is a tax consultant at Mackay LLP, Chartered Accountants, in Yellowknife. He can be reached at AndrewWong@Yel.MacKay.ca