BUDGET 2015: RRIF WITHDRAWAL REQUIREMENTS ADJUSTED TO BETTER REFLECT CURRENT REALITIES

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As widely predicted, Budget 2015 proposes to reduce the amount that annuitants are required to withdraw from a Registered Retirement Income Fund ("**RRIF**") in 2015 and subsequent taxation years.

Under the existing rules in the *Income Tax Act* (Canada) (the "**Tax Act**"), a Registered Retirement Savings Plan ("**RRSP**") must either be used to purchase an annuity or converted into a RRIF by the end of the year in which the RRSP holder turns 71 years of age. Once the RRSP is converted into a RRIF, contributions are no longer permitted and the RRIF holder is required to withdraw a minimum amount from the RRIF annually starting the following year. The minimum amount required to be withdrawn is calculated based on a percentage withdrawal factor that corresponds to the RRIF holder's age, multiplied by the value of the assets in the RRIF at the beginning of the year. The same percentage withdrawal factors are also used to determine the minimum amount that must be withdrawn annually from a defined contribution Registered Pension Plan ("**RPP**") and a Pooled Registered Pension Plan ("**PRPP**"). At the time of establishing the RRIF, the holder also has the option to base the minimum withdrawal factor amounts on the age of his or her spouse or common-law partner.

The annual RRIF withdrawal factors are currently set at 7.38% in respect of RRIF holders that are 71 years old and increase to a maximum rate of 20% for RRIF holders 94 years of age or older. In Budget 2015, the Government announced its intention to lower the applicable withdrawal factors to 5.28% in respect of RRIF holders that are 71 years old, increasing to a rate of 18.79% for RRIF holders that are 94 years of age. The withdrawal factor would remain at a rate of 20% for RRIF holders (or their spouse or common-law partner) that are aged 95 or older.

Generally, the RRIF withdrawal factors are intended to operate in a manner that delivers an annual source of income to retirees and ensures that the Government begins to recoup tax revenue on tax-deferred savings from RRSPs. The existing RRIF rules were developed on a basis that would provide a regular stream of payments to RRIF holders from age 71 to 100, assuming a 7% nominal rate of return on RRIF assets and an indexing factor of 1% annually. The new withdrawal factors proposed in Budget 2015 are predicated on an assumed 5% nominal rate of return on RRIF assets and a 2% indexing factor. These assumptions are more in line with long-term historical rates of return on investment portfolios and expected inflation.

The new withdrawal factors will allow for better capital preservation by allowing RRIF holders to keep more of their retirement savings in their RRIFs for a longer period of time, while continuing to take advantage of the tax deferral provided on earnings within a RRIF. The proposals are the federal Government's response to extensive lobbying by investment industry and seniors' groups that argued that the current RRIF withdrawal factors were not being adapted to meet the increased life expectancies of Canadians. Seniors were concerned that their RRIFs were being liquidated too quickly, and that they ran the risk of outliving their savings. The existing RRIF withdrawal factors were designed in 1992, when interest rates were much higher and, therefore, envisioned a level of return on retirement savings that would no longer be possible in the context of the current interest rate environment.

The Government has suggested that the reduced RRIF withdrawal factors, coupled with the increase to the annual TFSA contribution limit that was also announced in Budget 2015, will give seniors an "increased flexibility to manage their savings in a tax-efficient manner". The Government estimates that, with the new withdrawal factors, a RRIF holder will preserve almost 50% more capital from the time the RRIF is created (at age 71) to the time that the holder is age 90 than that same holder would have preserved under the existing withdrawal factors. The Government also estimates that the RRIF changes announced in Budget 2015 will save Canadian seniors $670 million in federal taxes between 2015 and 2020.

As a result of the proposed changes, an individual with a high asset value in his/her RRIF will run the risk of a higher tax liability on death, as funds not taken out of a RRIF during the RRIF holder's lifetime will generally be taxed at the applicable marginal tax rate in the RRIF holder's terminal tax return (subject to the availability of certain spousal or other rollovers). However, if an individual is already subject to income tax at the top marginal tax rate during their later years, allowing funds to accumulate in a RRIF may not lead to a higher ultimate cumulative tax liability.

Finally, Budget 2015 provides, as a transitional measure, that RRIF holders who withdraw more than the newly reduced minimums from their RRIFs at any time in 2015 will be permitted to re-contribute the excess amount to their RRIFs until February 29, 2016. The re-contribution amount will be limited to the reduction in the minimum withdrawal amounts provided for in Budget 2015. Re-contributions will be deductible by a RRIF holder when computing his/her income for the 2015 taxation year (the objective of such permitted deductions being to offset the required income inclusion arising from the initial excess withdrawals from the RRIF). Similar rules with respect to re-contributions will apply to individuals receiving annual payments from a defined contribution RPP or a PRPP.

For reference, Budget 2015 included Table A5.2 below, which compares the existing and new RRIF withdrawal factors.

Table A5.2

Existing and New RRIF Factors

Age (at start of year)	Existing Factor %	New Factor %
71	7.38	5.28
72	7.48	5.40
73	7.59	5.53
74	7.71	5.67
75	7.85	5.82
76	7.99	5.98
77	8.15	6.17
78	8.33	6.36
79	8.53	6.58
80	8.75	6.82
81	8.99	7.08
82	9.27	7.38
83	9.58	7.71
84	9.93	8.08
85	10.33	8.51
86	10.79	8.99
87	11.33	9.55
88	11.96	10.21
89	12.71	10.99
90	13.62	11.92
91	14.73	13.06
92	16.12	14.49

93	17.92	16.34
94	20.00	18.79
95 & over	20.00	20.00