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## Pensions: Income Splitting and Related Matters

### Pension Income Transferred from Spouse or Common-Law Partner

Income splitting with your spouse or common-law partner is generally not allowed. However, one exception applies — to pension income. You and your spouse (or common-law partner) can agree to split up to 50% of your spouse/partner's eligible pension income. If your spouse/partner is 65 years of age at the end of the taxation year, all their pension income is eligible, and up to 50% of it can be transferred to you. If your spouse/partner is not 65 at the end of the year, only their income eligible for the \$2,000 pension income credit ("qualified pension income") is eligible income for purposes of the income splitting election.

There are two possible benefits to splitting income. First, if you are in a lower tax bracket than your spouse/partner, as a couple your tax will be lower overall. That is, your spouse/partner's income taxed at the higher rate will be reduced, and your income taxed at the lower rate will be increased. Provincial tax will also have a bear-

ing on the tax savings involved, but generally speaking the federal rate brackets will determine whether the election is beneficial in terms of tax rates.

Second, if you are 65 or over at the end of the taxation year for which you are splitting pension income, you may include the transferred income along with your own pension income in claiming the \$2,000 pension income credit. Thus, to the extent you do not already have \$2,000 of pension income of your own before the transfer, you can increase this credit. To the extent your spouse/partner has more than \$2,000 of eligible pension income, this will increase the credit available to you as a couple. If you are not yet 65 at the end of the relevant taxation year, you may still claim the credit in respect of "qualified pension income" transferred from your spouse or common-law partner. Essentially, this is your spouse or common-law partner's private pension or annuity income, not including RRSP, RRIF, or DPSP income, plus certain amounts received as a consequence of the death of your spouse/partner's (former) spouse/partner.

These two benefits should each be considered in deciding how much (if any) pension income should be transferred. If you are both in the same income bracket and both fully using the \$2,000 pension credit, there is typically not much point to the transfer. If your spouse/partner is in a higher income bracket, you will, as a couple, benefit from a transfer, at least to the point where you are both in the same bracket. Even if you are both in the same bracket, there may be an advantage to receiving at least enough pension income to fully utilize the \$2,000 credit, assuming you do not have \$2,000 of pension income of your own.

The following amounts received in the year qualify as “eligible pension income” for the purposes of pension income splitting.

For people 65 or older before the end of the year, eligible pension income is the total of:

- (1) “Pension income”, which includes
  - (a) life annuity payments under a pension plan (other than a PRPP), including bridging benefits under an RPP, or an SPP (Saskatchewan Pension Plan),
  - (b) an annuity payment under an RRSP, DPSP, or PRPP,
  - (c) payments under an RRIF,
  - (d) periodic payments under a money purchase provision of an RPP to the extent that such payments are not already included,
  - (e) annuity payments purchased by a DPSP trustee as a payout of the taxpayer’s vested interest,
  - (f) the income element of annuity payments, and
  - (g) amounts included in the individual’s income in respect of certain life insurance policies;
- (2) The lesser of:
  - (a) the total of all amounts paid
    - (i) out of or under an RCA that provides benefits that supplement the benefits provided under an RPP, and
    - (ii) in respect of a life annuity that is attributable to periods of employment for which

benefits are also provided to the individual under the RPP, and

- (b) the amount by which
  - (i)  $35 \times$  the defined benefit limit for the year (i.e.,  $35 \times \$3,420$  for 2022 = \$119,700) exceeds
  - (ii) the total of all amounts included under (1) above; and
- (3) The lesser of:
  - (a) the total of all amounts received on account of
    - (i) a retirement income security benefit payable under Part 2 of the Veterans Well-being Act (“VWA”; prior to April 1, 2018, this was the Canadian Forces Members and Veterans Re-establishment and Compensation Act), and
    - (ii) effective April 1, 2019, an income replacement benefit paid in respect of a Canadian Forces veteran for the months following the month in which the veteran attained (or would have attained) age 65, and
  - (b) the amount by which,
    - (i)  $35 \times$  the defined benefit limit for the year (i.e.,  $35 \times \$3,420$  for 2022 = \$119,700) exceeds
    - (ii) the total of all amounts included above under (1) and (2) above.

For people under 65 at the end of the year, eligible pension income is the total of:

- “qualified pension income”, which consists of,
  - item (1)(a) above, and
  - items (1)(b) to (g) above, if received by the individual as a consequence of the death of a spouse or common-law partner; and
- item (3) above.

Item (2) in the list above is only available to those individuals 65 or over at the end of the year. It is also the only portion that qualifies for pension income splitting but does not qualify for the pension credit.

The following do not qualify as eligible pension income for pension income splitting:

- any pension or benefit under the Old Age Security Act or similar provincial plan;
- Canada/Québec pension plan benefits;
- death benefits;
- any portion of any payment that would otherwise qualify which is specifically deductible under another provision of the Income Tax Act;
- any payment received from a salary deferral arrangement, an RCA, an employee benefit plan, or employee trust; and
- lifetime pensions payable under an unfunded supplemental employee retirement plan (excluding those payable under the legislative arrangements established for federally appointed judges and Lieutenant Governors).

The election is made on form T1032, Joint Election to Split Pension Income for 2022. You must report on your return your share of the income transferred, and form T1032 will show you the pension amount you can claim (both on your own account and on account of the transfer).

### **Election To Split Pension Income on Death**

The legislation clearly contemplates that the election can be made in the year of death of either party by joint election with the legal representative of the deceased, provided the deceased was resident in Canada immediately before death.

Where the survivor does not survive until December 31, or where the transfer operates from the deceased to the survivor, the question arises as to the length of the taxation year of the deceased. That is, does the taxation year of a decedent terminate on the date of death or at the end of the calendar year?

Where a transfer is from the deceased to the survivor, the amount that can be transferred is

half the pension income received (or accrued) to the date of death. Similarly, where the survivor transfers an amount to the deceased but the survivor dies before the end of the year, the numerator of the pension proration would be the number of months of the marriage/partnership and the denominator would be the number of months to (and presumably including) the month of the survivor's death.

### **CPP and Divorce/Separation**

For married or common-law spouses, the Canada Pension Plan ("CPP") allows for the splitting of CPP benefits between a taxpayer and a former spouse. This permits divorced persons to apply for a share of the CPP credits of their former spouses, which results in equal sharing of pension credits accumulated while the taxpayers were married. The credits earned by both spouses during the marriage will be aggregated and split equally. Generally, there is no time limit on this application, except that where a spouse has died there is a 36-month time limit.

CPP entitlements can also be divided on separations of common-law partners if they have lived together for at least one year, and application for division is made within four years of the commencement of separation.

In the case of a legal divorce you do not have to apply for a division of benefits; the CPP simply needs to be notified that the divorce occurred and given certain information (with documentation), such as the length of time you lived together. In all other cases, an application is required. There appears to be a distinction without a difference. In either event, you should obtain from Service Canada form package ISP 1901, which contains much useful information as well as the requisite forms.

Separated parties can divide CPP "unadjusted pensionable earnings" by agreement or court order, but the order or agreement must specifically refer to "sections 55 or 55.1" of the CPP to be binding.