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Registered Education Savings Plan

While a post-secondary education is an invaluable personal asset, it is becoming increasingly more expensive. The good news is that over the years the Canada Revenue Agency (CRA) has significantly enhanced the Registered Education Savings Plan (RESP) rules. In addition to the tax advantages, there are increased savings limits and the Canada Education Savings Grant (CESG) which deposits up to $500 per year directly into your child's RESP. To obtain the maximum benefit from an RESP and the CESG, it makes sense to start your savings program early. At BMO Nesbitt Burns we can help you determine the best way to finance your child's education and work with you to develop a savings program that helps meet your educational savings goals.

Your RESP contributions are not tax deductible, nor are they considered taxable when withdrawn. The main reason for contributing to an RESP is that all of the investment income generated in the plan compounds on a tax-deferred basis. And, an RESP can remain opened for up to 35 years. Consequently, the tax-deferred compounding of income can result in substantial growth in the plan. When the income and CESG are paid out for education expenses, called Education Assistance Payments (EAPs), the funds are taxed in the student's and not the subscriber's hands (i.e., the individual who made the contribution), and presumably the student will be in a lower tax bracket.

Contributions

As of 2007, you may contribute a lifetime maximum of $50,000 per beneficiary. The number of years over which contributions can be made to the RESP is 31 years, and there is no minimum annual contribution limit that you must make.

Canada Education Savings Grant

The CESG was introduced in 1998 to help ensure students have enough money to fund their higher education. Under the program, the Government of Canada pays a grant of 20 per cent of annual contributions per beneficiary to an RESP, up to a maximum of $500 per beneficiary (up to $1,000 in CESGs if there is unused grant room from a previous year) into the RESP.

When an RESP contribution is made, the government pays the grant based on the child's available CESG contribution room. The grant is calculated as the lesser of:

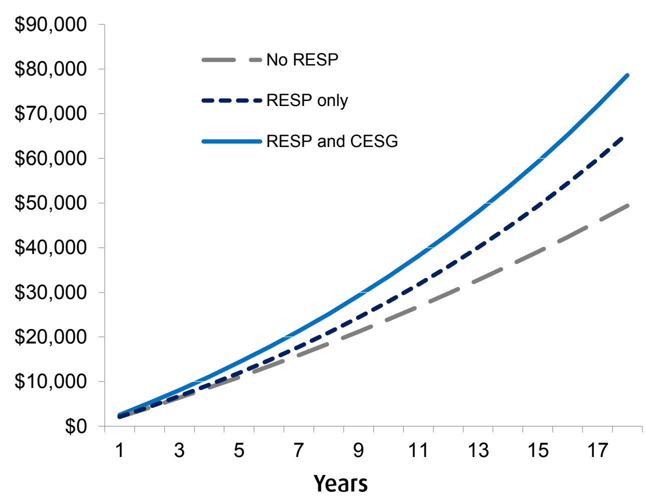
- 20 per cent of the RESP contribution amount;
- 20 per cent of available CESG contribution room; or
- $1,000 (20 per cent of $5,000 if there is unused grant room from a previous year).

Children born after 1997 (when the CESG was first introduced) are eligible for CESGs totalling $7,200 over the life of the RESP.

The following chart shows the benefit of using an RESP to save for your child's education and the additional benefit provided by the CESG.

If you are in a 46 per cent tax bracket and invested $2,000 per year, at six per cent for 18 years inside an RESP, you would accumulate $65,520 versus only $49,407 if the $2,000 was invested outside an RESP in a non-registered account. If the RESP received the CESG each year, the RESP would be worth a total of $78,624 after 18 years. By combining the benefits of an RESP with the CESG, you could accumulate almost 60 per cent more money than saving for your child's education outside an RESP.

Comparison of Growth Using an RESP Verus Non-Registered Account



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Multiple beneficiaries

If you have a family RESP for more than one child and one of those children does not pursue a post-secondary education, the other RESP beneficiary(ies) can receive the CESG, as long as they receive no more than $7,200 of grant money in total.

For example, let's assume a total of $8,000 of CESG was paid into a family RESP plan with two beneficiaries ($4,000 of CESG received for each beneficiary). If only one beneficiary pursues post-secondary education, $7,200 of grant money can be paid to that beneficiary, even if the beneficiary only earned $4,000 in grants. The remaining $800 would have to be repaid to the government; however, only the CESG would have to be repaid, not the income earned on the CESG.

Contributions and the CESG

Every child under age 18 who is a Canadian resident accumulates CESG contribution room, regardless of whether they have an RESP. Children accumulate $400 for each year between 1998 to 2006, and $500, from 2007 onwards, and unused CESG contribution room is carried forward for use when RESP contributions are made in future years.

Let's assume, a father has a daughter who was born in 2002 but he didn't open an RESP for her until 2009, when she turned seven. The child would have $3,500 ($400 for each year from 2002 to 2006 and $500 for 2007 to 2009) of CESG contribution room available. If the father contributed $5,000 to an RESP for his daughter in 2009, a CESG of $1,000 (20 per cent x $5,000) would have been paid into the plan. The child would still have $2,500 ($3,500 minus $1,000) of CESG contribution room available that could have been carried forward for use in a future year. If the father then contributed $5,000 to the RESP in each year between 2010, 2011, 2012, 2013 and 2014, additional CESGs of $1,000 would be paid into the plan each year. Since there would be no more CESG contribution room carried forward into 2015, even if the father contributes $5,000 in 2015; the CESG payment would be only $500.

While unused CESG contribution room may be carried forward for use in future years, RESP contributions made in one year that exceed the available CESG contribution room cannot be carried forward and applied to a future year. For example, if the subscriber makes a $3,500 RESP contribution this year and the child has $2,500 of CESG contribution room available, a $500 ($2,500 x 20 per cent) CESG payment will be paid into the plan. Next year, if a$1,500 RESP contribution is made, a CESG of $300 ($1,500 x 20 percent) will be paid into the plan. The extra $1,000 contributed to the RESP in the prior year cannot be carried forward to help qualify for the full CESG payment in a future year.

Year	RESP Contribution	Acutal CESG Paid to the RESP	CESG Room Available at Year End
2009	$5,000	$1,000	$2,500
2010	$5,000	$1,000	$2,000
2011	$5,000	$1,000	$1,500
2012	$5,000	$1,000	$1,000
2013	$5,000	$1,000	$500
2014	$5,000	$1,000	$0

Contribution requirements for beneficiaries who are 16 or 17 years old

Since the CESG has been designed to encourage long-term savings for post-secondary education, there are specific contribution requirements for beneficiaries who attain 16 or 17 years of age. RESPs for beneficiaries 16 and 17 years of age can only receive the CESG if at least one of the following two conditions is met:

- A minimum of $2,000 of contributions has been made to, and not withdrawn from, the RESP for the beneficiary before the year in which the beneficiary attains 16 years of age; or
- A minimum annual contribution of at least $100 has been made to, and not withdrawn from, the RESP for the beneficiary in any four years before the year in which the beneficiary attains 16 years of age.

This means that you must start your RESP savings for your child before the end of the calendar year in which the beneficiary reaches age 15, in order to be eligible for the CESG.

Enhanced benefits for RESPs

Canada Learning Bond

The Government of Canada introduced a Canada Learning Bond (CLB) for children born after December 31, 2003 in families entitled to the National Child Benefit (NCB) supplement for their child. The CLB is a grant that is paid into the child's RESP. It consists of an initial sum of $500 and, for subsequent years, annual payments of $100 for up to 15 years for each year the family is entitled to the NCB supplement for the child.

Enhanced CESG

The 20 per cent CESG may be increased to 30 per cent on the first $500 of contributions for families with less than approximately $88,000 of annual income, and up to 40 per cent for families with less than approximately $44,000 of annual income. These annual income amounts are adjusted yearly based on the rate of inflation.

RESPs and your Will

An RESP can be held by a single subscriber or joint subscribers (generally a parent or parents). Since the RESP is the property of the subscriber(s), this asset belongs to the subscriber(s). If there is only one subscriber, upon his/her death, the RESP becomes the property of the subscriber's estate. If there are two subscribers (joint subscribers), upon the first death, the RESP becomes the property of the surviving subscriber, subsequently falling to the estate of the second subscriber upon their passing.

Upon death, the RESP assets are subject to the terms of the deceased subscriber's Will. Ideally, where there is only one subscriber, the subscriber's Will would appoint a successor subscriber to maintain the RESP. If the maximum RESP contribution limit has not been reached, the succeeding subscriber can continue the RESP contributions.

Joint subscribers are encouraged to have mirror RESP clauses in their Wills, directing how the RESP is to be dealt with upon the surviving subscriber's death. Of course without a contract between the joint subscribers, the surviving subscriber is free to change the RESP clause in his or her Will since the RESP is property that belongs to the subscriber.

U.S. citizens and RESPs

If you are a U.S. person (U.S. citizen or Green Card holder) living in Canada, you are required to file annual U.S. income tax returns, in addition to your Canadian income tax return. It is important to consider the U.S. income tax consequences of your investment and savings strategies – including setting up an RESP for your child. A U.S. citizen parent contributing to an RESP should be including the income earned within the RESP as taxable income for U.S. tax purposes. However, for Canadian income tax purposes, the RESP income is generally only taxable to the child when withdrawn from the RESP for education purposes, and is therefore not included as taxable income to the contributor. This mismatch in the timing of the taxation (and taxpayer) between Canada and the U.S. may result in double taxation.

Depending on the specific terms of the RESP, if the contributing parent is not a U.S. person, but the beneficiary is, the accumulated income may be included in the child's income for U.S. tax purposes upon withdrawal from the RESP. Ultimately, the withdrawals from the RESP that include accumulated income may also be subject to significant interest charges in addition to the U.S. income tax that results from any RESP withdrawal.

In addition to U.S. income tax considerations, annual U.S. information reporting requirements should be considered, as RESPs may be treated as foreign trusts for U.S. income tax purposes.

If you or your child is a U.S. person, the U.S. tax filing and reporting obligations associated with a Canadian RESP should be discussed with a cross-border tax advisor to determine the feasibility of establishing (or maintaining) an RESP.

Start your education savings plan today

With the increasing cost of a post-secondary education, it's important to have an educational savings plan in place. For more information about RESPs and other planning strategies to help you meet your family's education funding needs, please contact your BMO Nesbitt Burns Investment Advisor.

BMO Nesbitt Burns Education Savings Calculator

To get an idea of how much your children's future education costs will be – and if your current education saving plan will be enough – use our **Education Savings Calculator.**

www.bmo.com/nesbittburns/financial-calculators

After reviewing the results, you can make changes to key assumptions to see the impact on your plan. The calculator's printable report summarizes your results and can be used for further discussion and planning when meeting with your BMO Nesbitt Burns Investment Advisor.

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The information presented herein is neither a comprehensive review of the subject matter covered nor a substitute for specific professional advice. Because of the complexity and evolving nature of cross-border taxation, and the potential for significant penalties, consultation with a cross-border tax specialist is recommended to review the applicable US and Canadian tax consequences and to co-ordinate the tax implications in both jurisdictions.

The comments included in the publication are not intended to be a definitive analysis of tax law. The comments contained herein are general in nature and professional advice regarding an individual's particular tax position should be obtained in respect of any person's specific circumstances.

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