THE GLOBE AND MAIL

CESTNICK

TAX MATTERS

RESP withdrawals take some planning, so be prepared

SPECIAL TO THE GLOBE AND MAIL
PUBLISHED SEPTEMBER 9, 2021

This week our youngest son starts his first year of university. We made the trek to the campus and helped him move into his dorm. While we were there, he struck up a conversation with an older student who was explaining to my son that the hardest course at the school is astronautical engineering. That's right – rocket science.

But I have to say that paying for an education by using a registered education savings plan is very likely more difficult to understand than a course in astronautical engineering. RESPs are a great vehicle for education savings, but making withdrawals can be confusing. Let me share with you some tips.

THE BASICS

One advantage of an RESP over other savings vehicles is that, as the subscriber (the person contributing to the RESP), your contributions may qualify for free money from the government in the form of the Canada Education Savings Grant (CESG), the Canada Learning Bond (CLB) and certain provincial grants where those are available. And so, the money inside an RESP is made up of the following three parts: your contributions to the plan, government grants and accumulated earnings on all of this money.

When money comes out of an RESP, there can be five types of withdrawals:

1. Withdrawals of your original contributions – called a return of payments (ROP);
2. Withdrawals of the government grants and accumulated earnings – called educational assistance payments (EAPs);
3. Payments to you, the subscriber, of the accumulated earnings in the plan – called accumulated income payments (AIPs);
4. Repayment of grants made to the plan (repaying the grants to the government is required in certain situations);
5. Transfers from one RESP to another.

As for the first two types of withdrawals, which are most common, an ROP is a tax-free payment out of the plan. As the subscriber, you can make this withdrawal for yourself at any time or allow those dollars to be paid to one or more of the beneficiaries of the plan when it's time for them to attend postsecondary school. The second type, the EAP, is taxable to the student when withdrawn.

As for the last three types of withdrawals, AIPs are subject to tax plus a 20-per-cent penalty and may take place if no beneficiary of the RESP attends postsecondary school. There are other options (such as transferring those amounts to your RRSP within limits) that may be available rather than paying the tax and penalties. If no beneficiary attends postsecondary school, or a beneficiary is not resident in Canada for tax purposes, then any government grants need to be repaid. As for transfers from one RESP to another, this can generally happen on a tax-free basis.

THE NUANCES

When our son started university this week, we made a withdrawal from the RESP we set up for our kids years ago. The rules say that the student must be enrolled full-time in a qualifying educational program (QEP), or is at least 16 years of age and enrolled part-time in a specified educational program (SEP – I won't get into defining a QEP or SEP today – but most programs will qualify.)

When withdrawals are made, you can generally specify what type of withdrawal it is (ROP, EAP, etc.). If there's more than one beneficiary on the plan you can also identify which beneficiary the withdrawal is for.

The most that can be withdrawn in the form of EAPs in the first 13 consecutive weeks of postsecondary studies is $5,000 ($2,500 for part-time students). This doesn't include withdrawals of your original contributions – which you can make at any time. After 13 weeks, any EAP amount can be withdrawn as long as the amount is for education costs (generally the financial institution, or promoter, of the RESP isn't required to verify the actual education costs being incurred or what the withdrawals are being used for).

In most cases, the best strategies for RESP withdrawals are these:

- Make the taxable EAP withdrawals when the student's income is the lowest. For my son, he plans to participate in his school's co-op program, which means he'll have decent income starting in 2023. So, we want his taxable EAP withdrawals to fall in 2021 and 2022 as much as possible.
- Many students had lower income in 2021 because of the pandemic, so this may be a good year to make EAP (as opposed to ROP) withdrawals from the plan.
- Grants must be repaid if they're not used, so it's generally best to withdraw EAPs (which include the grants) first during the student's years of study. The most that one student can receive in CESGs is $7,200 in a lifetime.
- Withdraw all RESP money by the time your children have completed their postsecondary education to avoid potential tax and penalties on AIPs.

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