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WealthHealth

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Pension Plan Strategy for Physicians

You know your personal RRSP is a fundamental part of your financial planning, but do you know how an individual pension plan (IPP) can work for you too? Now, with the recent changes to passive investment income for private corporations, IPPs are getting more attention than ever before. As an incorporated professional, an individual pension plan is another effective strategy you can use to save more for retirement. Unlike an RRSP, which is personal, you can also use an IPP to shift tax-deductible funds from your corporation to a pension where the dollars can be invested on a tax-deferred basis until your retirement.

An IPP essentially serves two purposes for incorporated professionals. It's a defined benefit pension plan (for one person) that allows greater tax-deferred contributions than an RRSP. And, at retirement, it gives you an annual pension income that takes into account your years of employment and level of T4 income.

DESIGNED FOR YOU

Individual pension plans were designed specifically for high-income incorporated professionals and business owners just like you so they're worth consideration. Some key objectives and benefits:

- Higher contribution limits
- Flexibility
- Creditor protection
- Manage passive investment income

HIGHER CONTRIBUTION LIMITS

In most cases where an incorporated professional earns sufficient income, the **corporation** can contribute more each year to an IPP than can be contributed to an RRSP – as much as 65% higher than you're allowed under RRSPs (depending on your T4 income and years of service). This can translate into a big difference in your ability to save for your future versus an RRSP.

You can generate more tax-deferred income, resulting in modestly more assets in your IPP at retirement compared to the strategy of contributing to an RRSP and investing retained earnings in your corporation (as many physicians currently do).

Let's look at an example of a 55-year-old physician who's been incorporated for 10 years.

Assumptions:

- 55-year-old physician professional corporation owner
- Incorporated 10 years
- Saved $285,714 in her RRSP and makes maximum contributions to age 65
- Rolls this amount into an IPP (maximum allowed); 7.5% return on investment

If this physician stays in RRSPs, she'll generate a total of $1,570,905 by the time she's 65. If she invests in an IPP instead, and makes the higher annual contributions, she'll have $2,272,001 at age 65. That's a **difference of $701,096 or 45% more** than if she'd continue to use her RRSP until retirement.

IPPs have a special subaccount, called the additional voluntary contribution account. You can use this account to transfer any RRSP assets into your IPP and take advantage of tax deduction of fees and the creditor protection of assets under a pension plan.

FLEXIBILITY

Using Canada Revenue Agency (CRA) rules, you can decide each year whether your IPP pension benefit will be accrued using a defined benefit plan method or the more traditional defined contribution plan method. (In contrast to defined benefit plans, defined contribution plans do not provide a fixed amount of funds at retirement. With defined contribution plans, what's "defined" is the amount you put into them.) This flexibility allows you to switch each year between the two kinds of plans depending on your business cash flow needs. Less cash flow means you can switch to the defined contribution plan, making lower contributions.

CREDITOR PROTECTION, ADDITIONAL DEDUCTIONS

Unlike RRSPs, IPP assets are protected from creditors by provincial legislation (Ontario). An IPP also offers several tax deductions for your corporation, including investment and administrative fees. IPP contributions can be made within the employer's taxation year or within 120 days after year end.

MANAGE PASSIVE INVESTMENT INCOME

Recent tax changes for private corporations take effect for the 2019 tax year and include a $50,000 threshold for passive, taxable investment income within a year. An individual pension plan may be a strategy your corporation can use to diversify investments and keep investment income under $50,000. By having your corporation make contributions to an IPP, you're shifting tax-deductible funds from your corporation to a vehicle where your money can be invested on a tax-deferred basis until your retirement.

OTHER CONSIDERATIONS

While individual pension plans offer many benefits for physicians, there are other administrative factors to consider before you set one up.

- Set-up requires a trustee.
- An IPP is governed by both pension and income tax legislation. You can't withdraw funds from an IPP as you would from an RRSP and you must use your IPP to fund regular pension payments after retirement. Investment criteria for pensions apply.
- If you start an IPP, be prepared to submit annual tax filings and to pay higher annual administration costs than for an RRSP. You'll also need to file a tri-annual actuarial report (usually managed by the actuaries of the IPP).
- An IPP is more expensive to create and maintain than an RRSP.
- IPPs can be subject to audit.

YOUR PERSONAL RETIREMENT NEEDS

Whether we care to listen or not, we're all constantly being reminded to rely less on government benefits in the future and take more personal responsibility for our retirement needs and any possible special needs like assisted living and special care. As we continue to live longer lives, these costs could be expensive over time.

You've worked hard in your career as a physician caring for others, so it's wise to take care of yourself and your family's future by doing all you can now to save for your future. A CMA Network advisor can help you review your current RRSP strategy within your whole financial security plan to determine if an individual pension plan is right for you.

Suite 1501
1111 West Georgia Street
Vancouver, British Columbia
Canada V6E 4M3