RESPs Part One: Starting an RESP

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Planning Ahead for Education

In essence, an RESP or Registered Education Savings Plan is an investment account designed to assist contributors, in setting aside funds for their beneficiaries, towards post-secondary or higher education tuition and expenses. In most cases, this is parents saving for their children. These savings accounts are considered to be tax-advantageous in the sense that no investment gains in the account will be subject to income taxes. RESPs are a powerful education savings tool for parents.

How Does an RESP Work?

It is important to note that parents are not the only group of people that are eligible to open up an RESP for a child. In fact, these savings accounts can be opened by a number of different contributors such as grandparents, common-law partners, family friends, or even child-care agencies.

Once an individual has chosen to open up a savings account, they must select a plan provider. RESPs can be opened at most financial institutions such as banks, credit unions, and wealth management firms like Qube. Your wealth manager will work with you to evaluate the three different types of RESPs offered and choose the right type for your specific situation.

1. Family Plan

These plans are ideal for those who have more than one child. The family plan allows contributors to select one or more children to receive the funds. These beneficiaries **must be related to the plan contributor** by either blood or adoption. Children, stepchildren, grandchildren, adopted grandchildren, would all be considered blood relationships and therefore covered under the plan. Nieces, nephews, aunts, uncles, and cousins are not considered to be blood relatives.

It is important to note here that a contributor may also open an RESP for their brother or sister.

One of the main advantages of the family plan is its flexibility in allowing earnings to be shared among more than one individual. Additionally, this RESP type allows all beneficiaries named under the plan to use the Canada Education Savings Grant (CESG). This grant essentially allows the government to add funds into the RESP up to a lifetime maximum of $7200. The CESG is available until the end of the calendar year that a child turns 17. Individuals from middle- and low-income families may qualify for additional government contributions depending on the adjusted income level of their primary caregiver.

2. Individual (Non-Family) Plan

This plan type proves most beneficial when used for a child that is **not related to the plan contributor.** As opposed to the family plan, only one beneficiary can be named under the individual plan. Although you have the ability to open this type of plan for an adult (or even yourself), you will not reap the benefits from government grants as adults are over the age eligibility for both the CESG as well as the Canada Learning Bond (CLB). The CLB is an alternative grant designed to support children from low-income families.

3. Group Plan

The group plan is designed to allow contributors to name a single child, regardless of whether they are related or not. In this type of plan, **the savings of one individual are combined with those of other contributors.** In essence, the amount that a beneficiary receives upon withdrawal is dependent on the total value of the group account as well as the number of beneficiaries that are enrolled in the plan.

Group plans are typically provided by dealers and are considered low-risk investments. However, as with any other investment tool, individuals considering signing onto these plans must evaluate and understand the rules set out by the plan administrator. For example, these types of plans typically ask contributors to commit to making regular payments over a certain period of time. Individuals may be subject to fees if these regular payments are stopped.

I Have Selected a Plan Type. What Now?

Once contributors have selected the type of RESP that works best for them, they can then proceed to open an account. A Social Insurance Number (SIN) must be provided for both the plan contributor as well as all beneficiaries. If you do not already have a SIN for either yourself or the child, one can be acquired through Service Canada. Obtaining a SIN is free, however additional documents such as birth certificates may be required.

The next step is to choose an RESP provider—this can be any financial institution such as a bank, group plan dealer, or wealth manager. Once a contract has been signed and an RESP has been opened by a financial institution, the CRA will register the account and review the plan eligibility. The typical wait time for RESP approval is 90 days.

Contributing to the RESP

Now that your RESP is open, you can go ahead and begin contributing to the plan. Similar to TFSAs (Tax-Free Savings Accounts), RESPs are tax-advantageous accounts. Capital gains, dividends, or income are not subject to tax. However, unlike TFSAs, withdrawals from an RESP for education funding are subject to income tax at the beneficiary's rate. For more information on TFSAs, read the Qub[Ed] article on RRSPs vs. TFSAs.

Since every RESP is different, the required frequency of contribution is completely dependent on the plan specifics. Some plans may ask for specified monthly amounts, some may require minimum deposits, and others may let you contribute on an ad hoc basis. As with all other types of investments, the earlier you begin to fund the RESP, the sooner you will earn interest in the account.

While there are no annual contribution limits for RESPs, there is a savings strategy that will optimize the government grants received each year. The government will match 20% of the contributions, up to a maximum of $500 per year. Therefore, in order to maximize the grant, it is suggested to make annual payments of it is suggested to make annual payments of $2,500 instead of a one-time lump-sum. There is also a lifetime limit of $50,000 for each beneficiary. If a contributor deposits an amount that exceeds this lifetime limit, they will be subject to a tax of 1% per month on the share of the over-contribution until it is withdrawn. In addition to the dollar maximum amount for these savings accounts, contributions to RESPs must also be completed within a 31-year period. However, there is no requirement for the account to be drained by that time. In fact, there is a 4-year grace period until the RESP must be fully paid out or collapsed (i.e., by the 35th year since the plan was established).

To learn more about withdrawals from RESPs as well as plan termination, read RESPs Part Two: When it is Time to Withdraw.

In Conclusion...

When implementing an RESP, it is vital for contributors to seek advice from industry experts like those at Qube that possess extensive knowledge on proper plan administration, tax expertise, and CRA guidance. The decision on how to determine contribution amounts maximums, as well as plan eligibility, requires substantial expertise. If plans are implemented without proper consideration, contributors could put themselves at risk with the CRA and be subject to tax restitutions.

Individuals who are seeking to utilize an RESP in funding their beneficiaries' education will benefit from the services of an Investment Counsellor. Unencumbered by alternative motivations, Qube will work with you to delve deep into your unique, personal circumstances and investment preferences, consider your specific financial goals, risk tolerance, and ongoing needs. Our team at Qube is committed to providing you with a holistic, diversified, and personalized investment experience. If you would like to learn more, reach out to us by email or call (780) 463-2688.