Dispelling the Myths - #3: RDSP Withdrawals

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There are several common misunderstandings about withdrawals from RDSPs. It is, however, a critical thing for a contributor to understand. After all, at some point the idea is to use the funds for the beneficiary.

That people are confused about withdrawals is understandable; withdrawals are one of the most complicated features of RDSPs and, because the RDSP is a long term savings plan, few people are making withdrawals. This means that few people in the financial institutions have had to deal with withdrawals, yet.

The most common misunderstandings are:

- Withdrawals can't begin until the beneficiary is 60
- Once money has been in an RDSP for ten years it can be withdrawn without penalty
- The worst thing that can ever happen to someone is that they have to give money back to the federal government.

Let me look at each of these misunderstandings but, first things first, withdrawals from RDSPs are usually referred to as payments.

Withdrawals can not begin until the beneficiary is 60 years of age.

NOT TRUE!

What is actually a definite rule is that withdrawals MUST begin at 60. Withdrawals can begin anytime from any RDSP but there are important implications.

Implications

1. If federal government contributions are greater than personal contributions, then the amount that can be withdrawn in a given year is limited to the amount calculated by a formula (known as the Lifetime Disability Assistant Payment – LDAP – formula), unless it is a specified year. It's a complicated formula but it is approximately the total amount left in the RDSP divided by the number of years before the beneficiary turns 83.

For example, if the beneficiary is 53, then it is the total amount in the RDSP divided by 30 (83 minus 53). The following year it will be the total amount divided by 29, and so on.

If personal contributions exceed federal government contributions, withdrawals are not limited by the formula.

What is a specified year? If a medical practitioner certifies that a beneficiary is not expected to live more than five years, then any amount can be withdrawn from the RDSP in that year and in the following years. Note: The holdback amount/ten year rule still applies.

2. If an RDSP receives funds from the federal government and the beneficiary makes a withdrawal within ten years of the last government contribution, then all funds received from the federal government in the past ten years. This is known as the holdback amount. More about this in the next section.

3. If Lifetime Disability Assistance Payments are begun at any age they must continue thereafter. Lifetime Disability Assistance Payments are regular (at least annual) withdrawals. Disability Assistance Payments do not need to continue each year; they may be a one-time withdrawal. Note that not all financial institutions are required by law to offer Disability Assistance Payments.

Once money has been in an RDSP for ten years it can be withdrawn without penalty.

False, generally.

The "10 year rule" requires that the beneficiary wait until ten years after the LAST government payment to make a withdrawal or pay a penalty. The penalty is the holdback amount, which is the total amount that the government contributed in the previous 10 years.

Suppose the federal government contributed $1,000 a year to an RDSP and those contributions ended in 2020. In 2021, the holdback amount would be $10,000 ($1,000/year times 10 years). In 2026, the holdback amount would be $5,000 and in 2031, the holdback amount would be $0.

The only time the above statement would not be false would be when referring to personal contributions made in the same year as the last government contributions. Ten years after that contribution is made, it could be withdrawn without penalty.

More importantly, where people utilize twenty years to receive all government contributions, they must wait an additional ten years to make withdrawals that are not penalized. That means that contributions in the first year must wait 30 years before being withdrawn.

The worst thing that can ever happen to someone is that they have to give money back to the federal government.

I added this one because I can't count the number of people who have said they would rather opt out of receiving government contributions because they don't want to have to pay it back in case they make a withdrawal prior to 10 years after the last government contribution.

I don't understand the logic. First, a beneficiary gets to keep the interest no matter what. Second, if life does permit the beneficiary to wait for ten years after the last government contribution then they get to keep all of the government contributions, which could be as much as $90,000. If a person is planning for a relative, then an option is to set aside enough to get through the time until the beneficiary is able to use the funds (e.g. a trust). Finally, where an RDSP has received the full complement of government contributions over twenty years, the RDSP could be worth as much as $400,000. In this instance, paying

$5,000 or $10,000 back to the federal government would seem to be a small penalty to pay to get access to the funds.

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