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***TAX NEWS*** is a bimonthly publication of the Communications Services Bureau, California Franchise Tax Board. Its primary objective is to provide information to income tax practitioners about state income tax laws, regulations, policies and procedures.

**New process for Canadian retirement plans**

We recently received an inquiry about the taxability of the earnings and distributions from a Canadian Registered Retirement Savings Plan (RRSP).

After reviewing the characteristics of a RRSP, we have revised our internal procedures and will now treat a RRSP like a savings account, not a functional equivalent of an Individual Retirement Arrangement. As a result, California resident taxpayers' original contributions, made while a Canadian resident, are treated as a capital investment in the RRSP. California residents are required to include the earnings from their RRSP in their California taxable income in the year earned. After taxpayers pay tax on these earnings, the earnings will also be treated as a capital investment in the RRSP.

When taxpayers receive distributions from their RRSP, the amount consisting of the contributions and the previously taxed earnings is treated as a nontaxable return of capital. Please note that the federal election to defer taxation on the RRSP earnings until a taxpayer begins receiving distributions, as discussed in Revenue Procedures 89-45 and 2002-23, is only available for federal income tax purposes and is unavailable for California income tax purposes.

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*(Editor's note: It is very important to understand that various years' exchange conversion rates are to be used to compute taxpayer's original contributions – not the single rate when a taxpayer enters California. Also, income earned in a particular year includes capital gains on sales or transfers of mutual funds within the RRSP. Professional help with computations is recommended.)*