JEWISH FOUNDATION of GREATER TORONTO

*Professional Advisor's Newsletter*

GIVING Advice

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***RRSPs, and RRIFs Need Protection Too***
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A 70-year-old, unmarried client came to see me recently worried about an issue that's common to many affluent Canadians. He had accumulated $2.8-million in a RRIF and was now concerned about what will happen to his hard-earned nest egg when he passes away.

I had to deliver the bad news: when that day comes his estate will face a tax bill of about 53% that will cut his RRIF savings by more than half. The government will collect almost $1.5 million in taxes.

If he was married he could leave behind the entire $2.8 million to his wife with no tax consequences at that time, but as a single person his estate will instantly diminish to only $1.3 million - a sizeable amount to be sure, but nothing like the $2.8 million.

It was time for me to help him protect his RRIF.

Divorced people, older unmarried individuals, widows and widowers need to know about this situation, and find ways to protect their savings.

You decided to protect your financial future when you started buying RRSPs or RRIFs. Now is the time to think about protecting your accumulated registered funds.

Many Canadians actively squirrel away money into an RRSP every month or make an annual contribution (usually at the RRSP deadline) in order to build up a healthy retirement package. Since the money is in a registered plan it will be subject to tax only when it is removed from the plan. That's because when you originally bought your RRSP you received tax relief as an incentive to put money away to fund your retirement (a good move on your part considering Ottawa does not want you to rely solely on the federal government for your retirement income).

Over the years that money has accumulated income tax free. The hope is that when you retire and start taking the money out, you will be in a lower tax bracket than when you made the RRSP deposit so the tax bite will be lower (or at least no higher) than the tax saved on the original contribution. That explains why many people withdraw only the prescribed minimum from their RRIF while the balance continues to accumulate tax free.

**Other Risks to your Retirement Savings**

Aside from ultimate tax liabilities, protecting retirement goals can be very difficult if certain unexpected and usually unfortunate life events occur along the way. You have probably heard real stories about people getting sick without insurance and being off work because of an injury, or an entrepreneur or self-employed person who gets sick and has no company benefits.

Treating and coping with a serious illness brings significant and unexpected costs often not covered by government or employee health plans anyway. Consider just the lost income resulting from time away from work for both patient and caregivers.

But you still need money – to eat, pay bills like children's education or cover everyday expenses. Since most Canadians have their money in two main areas, their RRSPs and their homes, if they become ill or unable to work chances are they will dip into their retirement savings versus dipping into their house. As soon as you remove money from a registered plan two important things happen:

1. You will be taxed on this amount whether you are ill or well.
2. It has taken years to build up your RRSP. You may not have time to replenish it.

**Defensive Strategies to Protect your Registered Investments**

People should consider long term disability insurance, critical illness insurance or long term care to insure their retirement savings against sickness or injury. Long term disability allows someone to insure their earned income in case of any illness, injury or sickness. It is paid after a waiting period, usually 90 days, is generally tax-free and replaces your "lifestyle" expenses allowing you to focus on getting better instead of worrying about money.

A critical illness insurance policy can pay up to $2 million following the diagnosis of a heart attack, stroke, cancer or any one of more than two dozen conditions. A healthy individual now contributing $500 a month into an RRSP might consider reducing the monthly deposit to $400 and use the $100 difference to fund a critical illness insurance policy as a defensive retirement strategy. It won't make a big dent in a retirement "pot" but will make a huge difference if someone gets sick along the way.

Another defensive strategy is a long term care policy to pay the expenses of home care or facility care if the insured is unable to do some basic daily living activities or if they suffer a cognitive impairment like Alzheimer's or dementia.

**Protecting your Retirement Savings from the Tax Department**

Married people should consider inexpensive joint-and-last-to-die life insurance to fund the tax that will be due on second death. It is a great way to use the money that normally would be going to taxes to ensure that all or most of your RRSP/RRIF savings go to your children and/or your favourite charities.

**Be Remembered for Charity, not your Tax Bill**

People who want to leave a sizeable portion of their estate to a charity should consider a charitable legacy. If you have made arrangements for your non-registered assets or insurance to go to your children, consider designating a charity as beneficiary for all or some of your RRSP/RRIF. Most people would prefer to be remembered for leaving $1 million to charity instead of 'donating' over $500,000 to the government via taxes. If there are additional estate taxes due, the charitable receipt will reduce or eliminate those costs too.

People may also want to consider buying a life insurance policy that names a charity as the owner and beneficiary of the policy. As an example, a person can take out an additional $50,000 a year from their RRIF or RRSP and use that money to buy an insurance policy valued in the millions of dollars. The $50,000 from the RRIF that is used to pay the premiums is considered a charitable donation. That charitable donation will eliminate the person's taxes on the RRIF withdrawals. Therefore, not only is that person clever by withdrawing RRIF amounts tax-free, he or she will also be remembered as a philanthropist who left money to a worthwhile cause instead of leaving it to the government.

My personal favourite reason to make a charitable bequest is that it instills in our children and grandchildren charitable values as they can become the "board of directors" who decide where your gifts are distributed each year in perpetuity.

There are many strategies available to help protect your retirement funds and reduce your final taxes in order to leave more to your loved ones or favourite charities. The best time to do this is when "the sun is shining" and you are healthy. Get good advice from an experienced professional with knowledge and expertise to get started.

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