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TAXSTRATEGY

Financial planning can be a lot like sports. Find a good coach and…

Play to win

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From the NHL to Wimbledon to the recent World Cup FIFA extravaganza, the world of sports offers a wide variety of seemingly unrelated athletic endeavours.

And yet, many similarities can be found among these sports. Not only that, a number of interesting comparisons can be made between these contests and your own financial plan.

For example: in virtually any sport (all the ones I can think of anyway) there are offensive and defensive plays, each with its own risks. The same holds true in financial planning.

In any sport, whether it's a competition between teams or individuals, the players have a coach. And all winning athletes, professional or amateur, will tell you that they would not have been able to reach the heights they have without help from their coach/mentor, teammates, parents or friends.

The same correlation exists with the estate planners, tax professionals, accountants and lawyers involved in a good financial plan.

When it comes to creating a winning financial plan, offence seems to always stand out as your major priority.

This is especially true today as the government starts to scale back its contributions. Seniors' benefits like Old Age Security and defined benefit pension plans are falling by the wayside every day.

To play the game effectively, you need to look at both the investment side (offence) and the health and benefits side (defence) of your life.

Playing offence

Taking the offence involves looking at risk (and diversification) in a way to help fend off that same risk.

Short-term interest rates currently range anywhere from zero to four per cent interest before tax.

That's a risk considering Canada's consumer price index hit 2.3 per cent in May, the first time in more than two years that the inflation figure has been above the two per cent level – meaning that even a four per cent interest rate no longer goes the same distance it did even 10 years ago.

A better strategy is to have access to funds in case of emergencies or opportunities. This will allow you to take advantage of high(er) rates when possible and acknowledge that risk should be in longer-term investments.

A good offensive strategy will also allow you to pass on a bigger estate to your family or to charities to cut down on taxes.

The taxman taketh

Many people are still unaware of how high a tax liability they can have at death. Many business owners, professionals, retirees and high-net-worth families can really find themselves in a significantly reduced financial situation if these tax liabilities are not looked after ahead of time:

✓ The federal government

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takes $460,000 of every $1 million of retirement savings after the second death of both spouses.

✓ The government gets $320,000 of every $1 million of investment holdings on the second death of both spouses.

✓ It will also collect about $1 million of every $5 million of investment growth (such as accumulated capital gains from investments, real estate and business equity) on the second death of both spouses.

And that's just the way it is right now.

Another risk to think about is that governments change their minds on funding and taxes all the time. None of us has a crystal ball as to what governments will give or take away in the future.

However, as the taxpayer pool shrinks and there is greater demand on health care, especially for the older population, the odds are in favour of taxes going up (not down).

In addition, there could well be an inheritance tax. (Currently, there is no such tax in Canada.) While whatever is in place now may be grandfathered, any new taxes or tax hikes will be in effect afterwards.

Another way to help cut down on the tax burden is to be generous and gift securities directly to a charity through a planned giving strategy.

You will not only reduce taxes on your estate, and thereby leave your beneficiaries a bigger inheritance, you will also be giving to a worthwhile organization and setting a good example to younger people as to how to use their income.

Here's another offensive strategy: buy personally-owned life insurance rather than mortgage protection from your bank. With bank mortgage insurance, coverage decreases as the mortgage decreases but the cost of premiums stays the same.

Effectively, the cost per $1,000 of coverage increases because bank mortgage insurance will only pay the balance of the mortgage outstanding at death.

However, a personal life insurance plan payout remains fixed throughout the term and can be used for any purpose whatsoever.

That includes a mortgage, yes, but perhaps the biggest thing for the surviving, working parent is to ensure there is some financial help for their children's university educations.

The main thing here is that YOU get to decide who gets the money.

As well, bank mortgage insurance is subject to provincial sales tax – but personally-owned life insurance is not.

Life insurance also passes directly to beneficiaries, meaning there is no probate tax on it either.

Long-term care insurance, aka the Rodney Dangerfield of insurance policies, doesn't seem to get the kind of respect it deserves. Few people buy it, and even fewer advisors sell it. But that certainly doesn't mean you don't need it.

Like the government tax example above, you can never tell what's going to be in the future. But that's what insurance is all about. Someone once told me you don't buy house insurance hoping your home will burn down, but you have it, just in case.

The "just in case" this time around is that the odds of living past 100 increases every year. In fact, forecasts for Canada indicate the centenarian population will reach 78,300 by the time the 1961 crest of the baby boom wave reaches age 100 in 2061 – that's up from the 2011 census that showed there were 5,825 people in Canada aged 100 or older.

But if you are in need of long-term health care during this time, including nursing care, rehabilitation and therapy, help with dressing, eating and bathing or homemaking services, costs not covered by regular health care can range between $4,000-$10,000 per month.

Then there is critical illness coverage. This coverage provides a lump-sum, tax-free payout of up to $2 million on the diagnosis of around two dozen illnesses, including cancer, Alzheimer's disease, deafness, heart attack, loss of an independent existence, Parkinson's disease, stroke, and a list of other illnesses. These are funds that can go to helping look after a loved one.

Above all, don't forget to make a will – and then look at it every year to make any updates if necessary.

Make sure the people looking after you and your estate are people you trust, and make it all legal by having up-to-date powers of attorney: one for personal health and another for personal property.

The easiest way to go about this is to get organized with a free Estate Planning Toolkit (available at www.illnessPROTECTION.com/estateplanning-toolkit.php). This is a multi-part kit that includes:

☛ putting together an estate directory (where you will outline where your estate can find all your important financial papers);

☛ an estate planning check-list , which will help you organize your estate efficiently and eliminate taxes;

☛ executor duties checklist, which you should put with your will to ensure your executor knows what to do; and

☛ business owners planning guide, which will help you develop a contingency plan to ensure continuity in your business.

Always use a certified financial planner, accountant, lawyer and professional trust and estate practitioner who knows the ins and outs of financial plans and can help make you a winner – no matter what happens on the field. ❐