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ESTATEPLANNING

Hold Estate Taxes

Flow Your Wealth

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You probably know by now that Life Insurance proceeds flow to named beneficiaries tax-free. If you have accumulated wealth over time you should be aware that significant taxes will come due when you sell your investments or when you die. It's a cold fact, which takes many people by surprise, that more than 50 per cent of your assets can be taken away as taxes. The Canada Revenue Agency (CRA) rules say you have parted ways with your assets at the time of your death, known as a deemed disposition.

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Here's how it breaks down

When you die, the CRA calculates your taxes owing as if you'd sold all of your assets at the moment of your death. As such, any registered investments – those held in your Registered Retirement Savings Plan (RRSP) or inside your Registered Retirement Income Fund (RRIF), are treated as income in the year you die. This pushes many people squarely into the highest tax brackets. In Ontario, for example, 53.53 per cent of all that income will make its way to Ottawa. If you have large capital gains in an unregistered account, meanwhile, 50 per cent of those gains will also be included as income on your final tax return. In addition, trust and estate administration taxes, formerly known as probate taxes, will be levied at 1.5 per cent of the asset value. A $1 million non-registered investment portfolio or a $1 million home will attract $15,000 in probate fees. It may appear that the value of your accumulated assets is frozen like a solid ice jam. Fortunately, with proper planning, you can preserve more of your hard-earned money with a melt-and-cascade strategy so those assets can flow to your family and other beneficiaries with little to no taxes owing.

You may want to leave some of your wealth to charity. The melt-and-cascade method helps in this case too, streaming your RRSP and RRIF funds away from the CRA, and into your favourite charitable organizations. The strategy includes the use of Life Insurance in different forms, depending on your specific situation, and is sometimes an alternative to investing because the amount your beneficiaries will inherit after tax is substantially and dramatically less than if your assets were nested inside of a Life Insurance policy instead.

The five examples below illustrate the advantages of alternative investing and explain how the melt-and-cascade strategy was used to minimize or eliminate taxes on the registered assets (RRIFs and RRSPs) and non- registered assets of high-net-worth individuals. Alice is a 71-year-old widow whose husband left her a large estate that included a $1 million RRIF. Because she is turning 72, she needs to withdraw a minimum amount from her RRIF every

year - $54,000 in this case. That figure is also required to increase in subsequent years. If she leaves the money in her RRIF, taking only the minimum amount of income required, about half of the value remaining in her RRIF and one quarter of the appreciation in her other non-registered investments will become taxes payable when she dies. Because she doesn't need the RRIF income to pay everyday expenses and bills, we structured a $1 million Life Insurance policy on her, and used some of the RRIF income to pay the premiums. Upon her death, her beneficiaries will get that $1 million, with no taxes or probate fees payable.

Steve is 65 years old, a divorced, single professional with two grown children. He has accumulated almost $2 million in his RRSP. He would like to leave half to his children and the other half to his favourite charity. In this case, he is withdrawing from his RRSP to provide the funding needed to maintain a $2 million Life Insurance policy on his own life, naming his children and the charity as the policy's beneficiaries. When he dies, $1 million will be paid out to his children. The other $1 million will be paid out to the charity, which will also generate a charitable receipt of $1 million, saving his estate approximately $500,000 of tax. If you do the math, his children end up getting a $1.5-million benefit - $1 million from the policy, and $500,000 more remaining in his estate that would not have otherwise been there if he hadn't made the donation.

Please visit our new website WEALTHinsurance.com

Watch "The New Philanthropy", my recent "Ted Talk" at Moses Znaimer's ideacity conference http://bit.ly/MarkHalpern

Mark's corporate goal is the creation of $100 million in new charity each year working with clients, generous donors of non-profits and collaborating with allied professionals.

Helen and Leo, a married couple, own and operate a busy car dealership. They wanted to transfer money to the next generation without triggering any taxes. In this case, Leo used income from his non-registered investments to buy three Life Insurance policies, one for each of their three children. He is the policy owner. Helen is the contingent owner, and the children are tertiary owners. The cash value of the policies continues to build and remains tax sheltered within the Life Insurance policy. When a parent transfers a Life Insurance policy to their child, the cash value goes with it and so does the valuable risk protection. That insurance coverage on the children is especially important if, at some point in the future, they become uninsurable. The child can be named as a contingent owner. When the parents die, the policy will go directly to each child and the child can use it for their own estate planning. A Life Insurance policy purchased for one child can be transferred to a different child in the future for any reason. The cash value that is used by the child will be taxed at their own, respective rates versus their parents.

Alex is a 53-year-old accountant in a second marriage, a very common situation. He took money out of his RRSP (melt) to fund a Life Insurance policy (cascade). When he dies, the benefit from that policy will be paid into a testamentary trust for his second wife, who will have access to the income during her lifetime. The children from his first marriage will act as the trustees of the trust, so when the second wife passes away, whatever remains in the trust will revert to those children, tax-free.

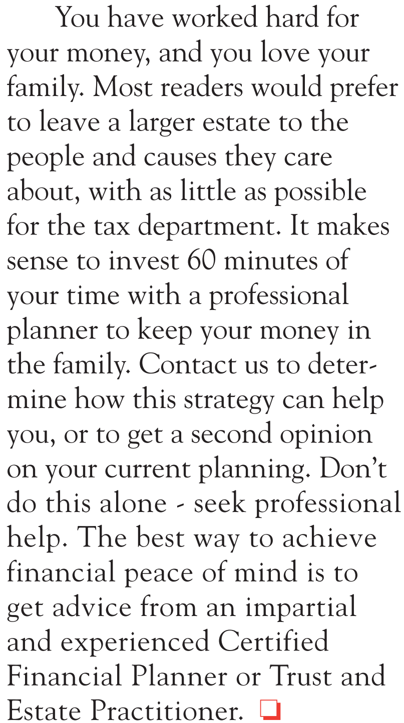
Ralph, a 73-year-old retiree, was receiving about $120,000 a year in taxable income from his RRIF and losing half of it to taxes. The melt-and-cascade strategy works especially well with charitable giving. He used the $120,000 RRIF income to pay the premiums on a new $2-million Life Insurance policy. The policy is owned by his charitable foundation, which is also the beneficiary, so the $120,000 premium is treated as a charitable donation. Having the policy owned by the charity helps offset the $120,000 of RRIF income. The proceeds paid on death will generate a $2 million charitable gift for which he is recognized during his lifetime.

No Going Back

The melt-and-cascade strategy doesn't have to begin with tax-sheltered funds. In fact, many clients who have maxed out their RRSP and RRIF contribution use the proceeds from the disposition of bonds, stocks and GICs - even segregated funds - to pay the Life Insurance premiums. This is even more effective when done within a corporation or holding company, as you can pay premiums with your corporate assets, and the proceeds on death flow out of the company tax-free

through the company's Capital Dividend Account ("CDA").

You should also know there is no reverse cascading – at least not without attracting taxes. So, for example, if a parent cascades a Life Insurance policy to an adult child and for some reason the child transfers ownership back to the parent, a policy gain is triggered, and tax must be paid. Life Insurance is one of the best ways to ensure that your family, loved ones and favourite charitable causes quickly and easily receive your last gift. As you can see, there are many ways you can use funds already on hand to finance the premiums. The unmatched flexibility, tax-free benefits and ability to designate any beneficiary is what distinguishes Life Insurance from any



other investment.

You have worked hard for your money, and you love your family. Most readers would prefer to leave a larger estate to the people and causes they care about, with as little as possible for the tax department. It makes sense to invest 60 minutes of your time with a professional planner to keep your money in the family. Contact us to determine how this strategy can help you, or to get a second opinion on your current planning. Don't do this alone - seek professional help. The best way to achieve financial peace of mind is to get advice from an impartial and experienced Certified Financial Planner or Trust and Estate Practitioner. ❑

Mark Halpern is one of Canada's top life insurance advisors, a Certified Financial Planner (CFP), Trust and Estate Practitioner (TEP), Master Financial Advisor-Philanthropy (MFA-P) and CEO of WEALTHinsurance.com

He guides successful business owners, professionals, and affluent families through the complex process of ensuring the people and organizations they care about are taken care of. If you are like his other clients, you are looking to reduce your tax obligations, preserve your wealth and leave a legacy.

Mark collaborates with your professional advisory team to achieve your desired outcomes. His simple approach makes sure what is important to you gets done. He will suggest appropriate strategies to get your financial affairs meticulously organized, help you take action, and simplify the complicated so you and your family can rest easy.

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