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Tax Increases Ahead

Protect Yourself Now

Mark Halpern, CFP, TEP, MFA-P

As businesses slowly begin to reopen, we see the start of new beginnings. I say "new" because we know life will never be exactly the way as it was. COVID-19 caught us like a deer in the headlights. We are sure to see more people working from home, more shopping online, and virtual doctors' visits. Until a reliable vaccine is developed, travelling for pleasure on crowded flights will remain a fond memory.

Financial support from federal and provincial governments has helped many (not all) Canadians get through all of this in part by providing direct support and loans to Canadians. In doing so, they helped crystallize the importance and significance of good health care, mortality and estate and tax planning.

The tab for direct support so far is $145.6 billion. But the real costs are much higher when you add in measures to protect Canadians' health and safety, provide business and tax liquidity support as well as the direct support for individuals, businesses and different sectors. That number is estimated at more than $817 billion.

There are also tax deferrals and credit and loan guarantee programs that cover emergency wage subsidies for businesses so they don't have to lay off people, as well as the emergency relief benefit (CERB), interest-free loans of up to $40,000 for qualifying businesses, along with $5.5 billion in GST credits, financial aid to students, farmers and seniors.

Vast shutdowns have jeopardized businesses, large and small, forcing many to shut down shop permanently because, with zero revenues, they are unable to pay their rent, wages and other expenses. Charitable organizations have suspended (hopefully temporarily) many important programs while universities struggle to determine how they can afford to issue widespread refunds to students whose final terms were cut short.

Those expensive government programs are essential, not just for our economy but to our everyday lives and peoples' sense of self-worth.

Preserve, preserve and preserve

Unfortunately, Canadian taxpayers will be asked (compelled) to foot the bill. It will be up to you and a seasoned financial advisor, to determine how to best preserve hard-earned savings for the benefit of your family, loved ones and the charities you care about. Not the Canada Revenue Agency.

Not long ago, the federal government increased revenues by introducing a new top tax rate for people with an annual income of more than $220,000. The tax rate rise by four percentage points, from 29 per cent to 33 per cent.

Despite not having a crystal ball, I believe there's a very strong possibility that other taxes will also be raised. Some are the capital gains tax, which will likely go from 50 per cent to 75 per cent, private equity, investment real estate, and appreciated securities taxed at

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Mark Halpern is a Certified Financial Planner (CFP), Trust and Estate Practitioner (TEP), Master Financial Advisor - Philanthropy (MFA-P) and one of Canada's top life insurance advisors. He is CEO of WEALTHinsurance.com® and illnessPROTECTION.com®, with special expertise for business owners, entrepreneurs, medical professionals and high-net worth individuals and their families. He can be reached at 416-364-2929, toll-free at 866-566-2001 or mark@WEALTHinsurance.com.

27 per cent of gains. Money in holding companies could be taxed at more 50 per cent.

We don't currently have an inheritance tax in this country, nor do we pay taxes on profits from the sale of our principal residences… but those may be up for grabs as well.

Even if the top one per cent of taxpayers were taxed at one hundred per cent, we would still not eliminate or greatly reduce our growing national debt.

There isn't much left on the table when it comes to non-taxable money. Only four remain: principal residences, TFSAs, lottery winnings, and life insurance.

No one, including the insurance industry, was prepared for the pandemic we are now experiencing. A lot of death benefits will be paid out earlier than expected, and the health of many insured Canadians will be impaired.

With the benefit of almost 30 years' experience in this industry, I confidently predict life insurance premiums will continue to rise as prevailing record-low interest rates persist. One major insurer recently announced rate hikes on life insurance products of up to 27 percent.

Anticipating those changes ahead, we have been meeting with clients and their families on Zoom and Skype, settling nerves for some, and opening eyes for others with advice on how to better manage their finances and preserve wealth. The best outcomes are obtained by asking the right questions followed by thorough planning.

The Rogers

The Rogers family recently met with us virtually. The parents, in their 70s, worried about the financial hit their $40-million real estate portfolio would take when they die. Heavily invested in commercial real estate, many of their commercial tenants have closed shop during the pandemic, and the underlying values of their properties have diminished considerably.

Our analysis determined their estate would face a $10-million tax bill when the parents die, an amount they were unaware of. To get that $10 million into family hands to pay the tax bill would require $20 million before tax.

We showed them a tax-exempt life insurance strategy that would require a total cost of $4 million to mitigate the entire tax liability instead of the $20 million pre-tax requirement.

The Smiths

This family had a net worth of $25 million that will shrink to $20 million because $5 million will be eaten up in taxes. In this case, they needed $10 million pre-tax to pay the $5 million tax bill.

We showed them a strategy that cost only $2 million instead of the $10 million pre-tax by restructuring their investments in a secure and tax-friendly way.

The Jones

Then there were the Joneses. They have a net worth of $50 million, but $12 million is in appreciated securities that could face $1.5 million in capital gains tax. The father also had a donor advised fund (DAF). We suggested he move $600,000 a year of the appreciated securities, pay no capital gains and get a charitable donation for $600,000, which would then save him $300,000 in annual taxes. He could then use the $600,000 we moved to his DAF to acquire a life insurance policy inside his foundation, with premiums payable for 10 years only. Using this strategy, he would go from having $1.5 million eaten up in capital gains taxes to saving $300,000 annually in personal taxes and creating an additional $8 million for his charitable foundation.

The above examples illustrate just a few ways that tax-exempt life insurance can preserve and grow your wealth cost-efficiently.

Immediate Financing Arrangement (IFA)

We often meet successful people who are asset rich and cash poor. They embrace our strategies but don't have the cash flow available to pay life insurance premiums. Sometimes they are simply reluctant to tie up their own money.

Many of our clients use an Immediate Financing Arrangement (IFA) as a leveraging strategy to acquire their life insurance. Basically, they pay the premiums and immediately borrow back those funds. This lets them get life insurance at what is just a fraction of the true premium cost, without reducing cash available for their use. In the end, they enjoy tax benefits and increase their estate values.

There is a cash surrender value (CSV) that builds up in an exempt whole life insurance policy that can be used to reduce your net, out-of-pocket costs to buy a policy. This allows you to keep your money in the form of borrowed premiums working for you in whatever investment you want.

Using the IFA, you use your

insurance policy as collateral for a line of credit with a Canadian chartered bank or life insurance company. Every year, you pay interest only on the line of credit, and can deduct the collateral insurance costs and the interest expense against personal or corporate income.

As you pay the ongoing premiums for the policy, you are eligible to borrow back up to 100 per cent with sufficient collateral. Using the line of credit lets you inject the capital into cash flow, acquisitions, investments and other business purposes.

Of course, the loan has to be repaid and it can be done in many ways. Most commonly, the loan is repaid using the death benefit, and remaining proceeds get paid out to beneficiaries. Some people prefer to repay the loan as their income grows, they dispose of other assets or their cash flow increases.

These planning strategies require development well ahead of time by experienced professionals who can help you through the entire process, including the determination of which financial institution is right for you. Bear in mind that a policy loan will be considered a disposition of assets and could trigger taxes if the loan exceeds the adjusted cost base of the policy. Again, please use a professional for this issue.

Proper estate planning is a process, not an event, that requires customized solutions – and every situation is different. The key here is in the planning, completing proper diagnostics before developing appropriate solution to meet a family's needs.

And before you ask: Yes, I do need a haircut, my older kids are itching to get back to school with real live teachers and I have many dear friends and relatives who I would like to hug. This may take time, but hopefully, when it's all behind us, we will all be thankful that we did the best we could. ❑

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, who are already challenged for time, through the complex process of ensuring the people and organizations they care about are taken care of.
If you are like his other successful business owner clients, you are looking to reduce your tax obligations, preserve your wealth and leave a legacy. Incompletions rob us of energy. Mark collaborates with your professional advisory team to achieve your desired outcomes. His approach is simple. He makes sure what is important to you gets done. He gets you organized, provides a big picture view of your financial affairs, determines your strategy and helps you take action. He will simplify the complicated, so you and your family can rest easy. He can be reached at 416-364-2929, toll-free at 1-866-566-2001 or Mark@WEALTHinsurance.com.
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