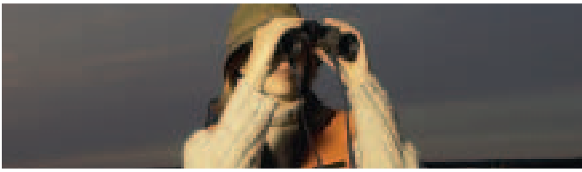
The Tax Protector

A wealth preservation strategy

RBC Dominion Securities



Life insurance is most commonly used to provide financial security to your family and other beneficiaries in the event of your death. However, life insurance can also be used to protect the full value of your estate from taxes. At death, your assets often trigger significant tax obligations, which are frequently met by liquidating the assets of your estate. A life insurance benefit can cover your tax obligations and leave your estate intact.

How can the Tax Protector help you?

The Tax Protector can help you:

- Leave a lasting legacy for your family
- Lessen the burden on loved ones during a difficult time
- Keep family heirlooms in the family
- Give more to your favourite charity

Planning for the tax bill on your registered assets

Are you aware that almost half of your retirement savings are payable to the government at death? Often, the top marginal tax rate is applied to all remaining funds in your RSP or RIF when they are taken into income in your final T-1 tax return, or that of your surviving spouse. On a $300,000 RIF account, up to $150,000 in taxes will be payable to Canada Revenue Agency, depending on which province you live in. Are you and your family members prepared for this tax liability?

Life insurance may be the least costly method of compensating for the taxes that are payable at that time. Even better, you can design your plan to specifically pay a benefit on the death of the last remaining spouse, which is when the taxes are due. This is called "Joint Last-To-Die" insurance coverage and comes at a lower premium cost than the equivalent individual coverage.

Should you consider the Tax Protector?

The Tax Protector can benefit you if you own substantial assets that you want to protect from taxes. These include:

- Registered plans, such as an RSP or RIF
- Shares in private or publicly traded corporations
- Collectibles, such as art, jewellery and antiques
- Real estate

Reducing your capital gains tax

At death, your assets can be transferred to your spouse without triggering any taxation. But on the death of your spouse, your assets are deemed to have been sold at current market value for tax purposes—even if they have not been sold. This can result in taxable capital gains.

After the cost base has been subtracted from the current market value of these capital assets, 50% of the gain must be claimed as income in your or your spouse's final tax return. Often, these assets must be sold in order to create enough cash to pay the taxes.

The Tax Protector allows your heirs to retain these assets, since the proceeds of the life insurance policy will cover the tax liability. This can help avoid an untimely disposition.

Leave a lasting legacy for your family

Case scenario

Tax liability projection at age 85 (rounded to the nearest $1,000)

In this example, a wife and husband are both 65 years old. With their total current assets valued at $2,785,000, they will owe $777,490 in taxes if the last spouse dies at age 85 (assuming a 46% tax rate).

AGE	ANNUAL RIF WITHDRAWALS (minimum)	BALANCED AT YEAR-END (8% growth)	TAX LIABILITY AT DEATH
65	$0	$318,000	$146,280
70	$19,170	$387,270	$178,140
75	$28,570	$357,220	$164,320
80	$28,540	$317,170	$145,900
85	$28,480	$275,690	$126,820

CAPITAL ASSETS

1. **Shares of a private company (purchased 1980)**

Current value of shares	$1,745,000
Future value (2% growth)	$2,593,000
Less total capital invested	$100,000
Gross capital gain	$2,493,000
Taxable capital gain (50%)	$1,246,500
Tax payable at death	$573,390

2. Cottage (purchased 1973)

Current value	$240,000
Future value (2% growth)	$356,600
Less purchase price	$20,000
Gross capital gain	$336,000
Taxable capital gain (50%)	$168,000
Tax payable at death	$77,280

3. Registered Assets

Current RSP value	$300,000
Age	65
Assumed growth rate	6%
Annual withdrawal	RIF minimum
Marginal tax rate at death (top marginal rate in Ontario)	46%

U.S. Estate Taxes

The following discussion applies only to Canadian residents who are not U.S. citizens or U.S. green card holders.

If upon your death you own any assets considered to be U.S. situs property (shares of U.S. companies, U.S. real estate, etc.), your estate may be required to pay U.S. Estate Taxes to the Internal Revenue Service based on the fair market value of these holdings at your death.

As much as 50% of the value of U.S. assets may be payable in taxes when you die. However, U.S. Estate Tax will not be payable if your worldwide assets at death are less than $1.2 million US, and you do not own any U.S. real estate. If you do own U.S. real estate, you will not be subject to U.S. Estate Tax if your worldwide assets at death are less than $1 million US.

Individuals investing in the U.S. should note that life insurance proceeds generally factor into the calculation of worldwide assets. However, the Tax Protector may still be the most cost-effective way of addressing this issue.

The above information is subject to change. Ask us for further information on U.S. Estate Tax.

How will your final taxes be paid?

Your executor will have several options to choose from:

CHOICE 1: Your estate can pay the tax liability with cash

Cash must be readily available when the tax bill is due.

CHOICE 2: Your estate can pay the tax liability from other liquid assets

Cash can be made available by selling the more liquid assets. However, that may not be a preferred choice as it can result in a "fire sale" (i.e., the sale of goods at extremely low prices) of all your assets. You should also consider how quickly your assets can be sold, if you can get full value for them and if they would be enough to pay the bill.

CHOICE 3: Your estate can borrow the funds to pay the taxes

With this option, you should consider whether credit would be readily available when the time comes, and if your estate would have adequate assets to provide the security required for both the loan and the interest that would have to be repaid.

All three of these options involve the erosion of the final value of your estate, as well as considerable expense and inconvenience for your heirs. The following option effectively eliminates these drawbacks and allows your assets to be transferred intact.

CHOICE 4: Purchase life insurance now to pay your taxes later

Since the taxes are not payable until the death of the last remaining spouse. Joint Last-To-Die insurance coverage can be purchased in order to provide the appropriate amount of cash upon death of the last spouse. Often, the cost of such coverage is only 1% to 3% of the future liability, depending on your age. You can either pay those costs annually, or take advantage of tax-exempt coverage, such as Universal Life, to prepay your premiums over five or 10 years.

In the case study above, it would cost $10,336** annually to buy enough insurance to cover the anticipated taxes, which is roughly 1.3% of the total liability. That is less than 0.4% of total taxable assets.

Protect your estate from taxes
To find out how you can benefit from the Tax Protector, call us† today.

** Effective May, 2005, Manulife Term to 100 rates.

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