Retirement Income Options
Self-Study Course # 2
RETIREMENT INCOME OPTIONS & THE NEED FOR PLANNING

In this self-study course, the student will learn about the following:

- The realities of Retirement Planning.
- The six steps of the retirement planning process.
- Some updated facts and figures about retirement and planning.
- The Baby Boomers and why planning for the future is important.
- Retirement planning in the early years – “The Early, Early Years.”
- Government sources of CPP, QPP, OAS and their planning features.
- Registered Retirement Savings Plans, Annuities, LIFs, LRIFs and RRIFs.
- Definition of earned income for retirement purposes.
- The many types of Corporate sponsored retirement plans and limits – IPPs, ESOPs, ESPPs,
- Advantages & disadvantages of various Corporate retirement plans.
- Mutual Funds (Investment Funds) and other Variable contracts.
- Mutual fund maturity benefits, limitations, death benefits, reset options, transfers, deferred sales charges, and management expense ratios.
- Segregated funds and how they work
- Tax-Free Savings Accounts. What they are and how they work.
- Life insurance as retirement funding vehicles such as RCAs, Split Dollar Arrangements and Salary Deferral Arrangements
- Taxation as it pertains to retirement income.

INTRODUCTION

The most important factor at play is Canada's baby boom phenomenon. Currently, about a third of the population is between their mid-30s and mid-50s--prime working years. This translates to about 12 ½ million people, or 1/3 of the population. Currently roughly 370,000 Canadians reach the traditional retirement age (i.e., 65) every year. By 2020, 425,000 Canadians will turn age 65 daily and in 2031, 1 in 4 will be over age 65.

To exacerbate this situation, the U.S. is experiencing a similar (albeit not as severe) demographic challenge. Our southern neighbours may look north for younger workers to fill the labour gap that has been left by their retiring employees.

There is some hope on the seemingly bleak horizon. Canadians are having families later in life and living longer. The desire or ability to stop working may decrease while children are still at home or in need of their parents' financial assistance with the cost of post-secondary education.
There is already some evidence of a growing trend towards working after traditional retirement years. According to Canadian author David Foot in Boom, Bust & Echo 2000, more than one million people over the age of 55 have come out of retirement in the U.S. since 1995.

The Baby Boomer Years

For the first time, seniors outnumber children in Canada, as the population experienced its greatest increase in the proportion of older people since Confederation, according to the latest 2016 census data.

There are now 5.9 million Canadian seniors, compared to 5.8 million Canadians 14 and under.

This is due to the historic increase in the number of people over 65 — a jump of 20 per cent since 2011 and a significantly greater increase than the five per cent growth experienced by the population.

The increase in the share of the oldest Canadians was even bigger — up 19.4 per cent for those over 85 and up 41.3 per cent among those over 100.

The result is the median age of the Canadian population in 2016 increased to 41.2 years, six months older than the median age just five years ago. (Median age is the point that separates an equal number of Canadians who are older and younger.)

The aging of the population is due to the first baby boomers turning 65 over the last five years, as well as the increasing life expectancy of Canadians and a low fertility rate.

Projections suggest the imbalance in the population will only grow.

By 2031, about 23 per cent of Canadians could be seniors, like Japan, the world's oldest country.

By 2061, there could be 12 million seniors to just eight million children in Canada.

"As people get older, they need more health care, more home care, and that puts increasing demands on government spending," says Dr. Frances Woolley, economics professor at Carleton University in Ottawa. "There are big challenges for the government coming on the fiscal side."

"As people get older, they need more health care, more home care, and that puts increasing demands on government spending," says Dr. Frances Woolley, economics professor at Carleton University in Ottawa. "There are big challenges for the government coming on the fiscal side."
But Canada is still younger than most of its G7 counterparts. Only the United States has a younger population among the world's biggest industrialized economies.

Nevertheless, the share of Canadians in the labour market (between ages 15 and 64) has decreased since 2011 to 66.5 per cent from 68.5 per cent.

The growth in the number of working Canadians was the lowest since 1851, making its share of the population the smallest in 40 years.

According to Woolley, younger people are increasingly struggling to find well-paid, stable employment. When young workers are not earning an income, they do not pay taxes. This has the potential to decrease the amount of tax revenues going into government coffers just as retiring older Canadians start to dip into their savings — which, if they are Registered Retirement Savings Plans, are taxed.

"Retirees don't want to crack open their nest eggs and share it with the federal government. It makes it politically harder for governments to collect tax revenue going forward."

Woolley calls it a "slow-motion train wreck. People respond quickly and effectively to emergencies and natural disasters, but not to longer-term trends. This conversation has been going on for decades."

André Lebel, a demographer with Statistics Canada, says that if the labour activity rate and productivity increase, that could counteract some of the effects of the aging population. Increasingly, older Canadians are staying in the workforce.

"Just because someone reaches the age of 65, that doesn't mean they aren't active anymore."

In the new millennium, baby boomers want it all – successful careers and a rewarding family life, but as they look ahead they also want financial security in their "golden years".

Baby boomers want financial products that meet any current and future needs. Therefore, life insurance products such as Universal Life and Segregated funds fit so well into their portfolios.
In addition, conservative investments that are liquid are particularly needed by baby boomers, as they may not have the will power to leave the money in place for 20 or so years if it is readily available.

The “Early” Early Years

Throughout the years, retirement planning has always had a different definition with the working public. At the beginning of the century, the average worker was too busy working, making a living to worry about the future. They certainly were not concerned about retirement or where the money to fund their retirement years was going to come from. It usually was accepted that the workers would set aside what they could, when they could. The reality of it was that many workers would work until their deaths.

When Registered Pension Plans became popular, the onus was put more on the company than the individual. The pressure of retirement was lifted a bit, but the selection of plans and the various benefits that made up these Pension Plans were limited.

Then came the boom years of the 1950’s. Along with these times, came the Canada Pension Plan as well as the need to fund “The Retirement Years”. Another factor that helped the sudden increase of Retirement Plans and future planning by the Life Insurance industry was the emerging Investment industry led by what we know today as Mutual Funds.

In the Income Tax Act of 1957, the provision for the introduction of the Registered Retirement Savings Plans was put into place. This springboard would launch a whole new industry of Retirement Planning.

Over the next 25 years, we would experience interest rates that would climb and fall just as fast. Inflation would also take its toll on the prevailing interest rates of the time. The good news is that we got through the first couple of decades, and as a result, Retirement Planning gained in the popularity that we see today.

The Reality

Throughout your lifetime, there will be several distinct and important events that will bring you face to face with your financial well-being: your education, your marriage, your first child, your first house, perhaps even starting your own business, and sending your children to university.
Financial planners for years have been saying that even though the above events are important and can be costly as *the largest single most expense that we will have in our lifetime is our “RETIREMENT.”*

**Canada’s Aging Population and Implications for Government Finances Highlight the Need to Plan for Retirement**

Despite broad public awareness that our society is aging, very little has been done by governments across the country to prepare for the marked aging that has already begun. This study examines the fiscal pressures, specifically the demand for greater spending on seniors-related programming coupled with a weakened ability to generate tax revenues, that governments will face for the foreseeable future from an aging population.

Similarly, unlike most of the period from the early 1970s through to 2010 (or so), labour force participation is now expected to decline. Indeed, expectations are that labour force participation will return to its pre-1970s level by mid-century. More specifically, from 2017 to 2063, Canada’s labour force participation rate is expected to fall from about 65 percent to 61 percent. This decline is akin to millions of fewer Canadians participating in the labour force.

This decline in labour force participation will adversely affect growth in per-capita income. Per-capita income grew, on average, by 1.3 percent between 1981 and 2016. However, expectations for the 2017 to 2045 period are that per-capita income will grow by only 0.9 percent, and almost the entirety of this decline in growth is expected to be due to lower labour force participation. The lower rates of per-capita income growth will mean the economy in general will grow more slowly, making it harder for government to collect revenues compared to its current capacity.

This slowdown in per-person income and economic growth more broadly comes at a time that governments will face pressure for higher spending on a wide range of programs. This study examines both health care spending and income transfer programs to seniors.

Health care spending on a per-person basis is heavily skewed towards a person’s first year of life (birth and related) and their retirement years (post 65). For instance, in 2014, the latest year of available data, the average per-person government spending on health care for Canadians between the ages of 15 and 64 was $2,664. Compare that to the cost for those 65 and over who had average annual per-capita health care costs of $11,625, which was 4.4 times greater than the 15–64 average. The higher proportion of Canadians expected to be in the over-65 category means higher and higher health care costs.
In addition to increased health care spending, an aging population will also require governments to direct more resources to senior income transfer programs like Old Age Security (OAS) and the Guaranteed Income Supplement (GIS). Currently, spending on these programs costs about $48.3 billion, which represents 2.4 percent of GDP. In 2045, spending on Elderly Benefits is projected to be approximately 1.1 to 1.2 percentage points of GDP higher than in 2017. This means that Elderly Benefits will represent between 3.5 and 3.6 percent of GDP by 2045, an increase of 47.0 percent from 2017. Using 2016 nominal GDP figures, the latest year for which we have complete data, this increase would be equivalent to $22.6 billion more being spent on Elderly Benefits.

Simply put, population aging will contribute to a large increase in future levels of government spending. When combined, projected government spending increases related to health care and Elderly Benefits are expected to be 5.3 percentage points of GDP higher in 2045 compared to 2017. In dollar terms, this additional spending would be equivalent to an increase of $107.1 billion using 2016 nominal GDP figures.

To illustrate the potential size of the looming fiscal imbalance, the study includes an analysis of probable revenues (conservatively estimated) with higher spending on health care and income transfer programs to seniors. Based on certain assumptions, by 2045, it is projected that there will be a 7.1 percent of GDP gap between government revenues and expenditures, in other words a deficit. For perspective, government deficits in 2016 would have been more than $143 billion based on 7.1 percent of GDP. Depending on interest rate assumptions, the accumulation of debt over this period could be substantial. The estimates in the paper of debt accumulation by Canadian governments range between 170 percent and 250 percent of GDP.

These rather worrying fiscal outcomes are not inevitable. Proactive steps can and should be undertaken to reform program spending and encourage stronger economic growth, both of which would mitigate the adverse effects from the aging of our population that are outlined in this paper.

**You Can’t be Fired for Being 65**

*That’s the good news. The bad news is that antidiscrimination rules can create new problems for older workers.*

The adage about retiring at age 65 because you had to… is not too common today.
Every province – except for New Brunswick – has eliminated mandatory retirement at 65. Nova Scotia became the latest jurisdiction to enact a partial or complete ban on mandatory retirement in 2009.

The good news for Canadians who hope to keep working past the once-common retirement age of 65—a growing number of whom are doing so from either need or desire—is that mandatory retirement is no longer allowed in Canada. You can’t be forced out the door just because you’ve reached a particular age.

The not-so-good news is that employers are therefore becoming more and more wary of hiring older workers, and age discrimination in the workplace seems to be rising as a result.

In recent years, all provinces and territories, as well as the federal government, have enacted or altered their human rights legislation to address workplace age discrimination.

All the human rights acts in Canada now prohibit mandatory retirement and protection doesn’t stop at age 65.

Prohibitions against discrimination based on age once applied only to those between 18 and 64. The Human Rights Code defines ‘age’ as 19 or older, so you can’t say to someone at age 65, “Okay, now you have to retire, so off you go.”

Nor can employers discriminate in other ways to compel an aging worker to leave or refuse employment based on age. Ontario’s human rights legislation, for example, specifies that:

- you have the right to be offered the same chances in employment as everyone else,
- you cannot be denied a job, training, or a promotion, or be forced to retire because of your age, and
- you have the right to the same level of services as everyone else, such as medical treatment and other health care.

In other words, you have the same rights as any other worker. Of course, this doesn’t mean you can never lose your job. People of any age can be let go at any time “with cause.” And even absent such justification as theft or negligence, an employee can be terminated at any time if given sufficient notice or severance pay in lieu of notice. It just can’t be done because you’ve turned a certain age.
THERE ARE EXCEPTIONS

An exception to the mandatory retirement prohibition is known as the Bona Fide Occupation Requirement (BFOR). This would apply primarily where the demands of the job are such that it couldn’t effectively be done by someone of an advanced age.

Firefighters or airline pilots, for example, can still be subject to this exception. Other types of work may be included, too, but it’s rare. The employer would need some pretty good scientific evidence to back up a mandatory retirement plan.

Employers can also implement a mandatory retirement program when continued employment would be detrimental to the employer. The employer would need to demonstrate that accommodating older employees would negatively affect safety, employee morale, or company costs, that it would interfere with other employees’ rights, or that it would be disruptive to collective agreements.

Where a program requires mandatory retirement, employers must show that their mandatory retirement program was developed in good faith and is rationally connected to the nature of the work, and that it would be impossible to develop a non-discriminatory program without undue costs or health and safety risks, Ontario’s Human Rights Commission literature states. For example, an employer would be required to show that the objectives of its mandatory retirement program could not be achieved through individual testing and assessment of employees.

Similarly, British Columbia’s Human Rights Code states that, to impose mandatory retirement, employers must be able to show that they adopted the requirement for a purpose rationally connected to the performance of the job and in an honest belief that it was necessary to the fulfillment of that legitimate work-related purpose, or that they would experience undue hardship by accommodating individual employees.

Furthermore, employers can’t use diminished capacity as an excuse for terminating employment.

They can’t discriminate on the basis that at, say, age 69, you are performing noticeably less efficiently than you were at age 60. They would have to accommodate someone if he or she were to be hit by a car; by the same token, age, per se, becomes a disability to be accommodated, up to the point of undue hardship on the part of the employer.
If an employer can show legitimate grounds for dismissal, there’s nothing wrong with that, but if it happens to affect only the four oldest workers in the company, the employer would have to prove that it was done for reasons other than age.

**PENSION PLANS CAN DIFFERENTIATE**

While employers can no longer use age to justify forced retirement (except where BFOR or hardship applies), pension plans can continue to make distinctions based on age. This is because when a pension plan is set up, the actuarial calculations must be based on age to make sense. For example, all pension plans must pick a termination age to calculate how much must be paid in premiums every year to ensure that the plan will be adequately funded at a certain dollar level.

Nevertheless, pension plans can’t force you to retire. They can only tell you that at a certain age, you’ll be entitled to X amount of pension benefits. But the fact that you now may continue working indefinitely throws a spanner into the calculations and raises many questions.

For example, can you continue contributing to your pension after age 65 and build a larger benefit entitlement? How do employers calculate how much more people should receive, if there’s no way of knowing how much longer they’ll work? Or do they simply pay the pre-established benefit and provide no further opportunity to contribute?

The question now is, does a pension plan trump human rights legislation? Or, should there be some kind of trade-off if you keep working? These issues have yet to be resolved.

**ENFORCEMENT VARIES BY PROVINCE**

If you feel you’ve been subjected to age discrimination, you have options for pursuing a claim. UK-based website agediscrimination.info, a source of statistics and information on age discrimination in various countries including Canada (access to the site depends on the browser you use), notes that enforcement mechanisms and remedies differ depending on province.

Some jurisdictions, such as Alberta, Manitoba, and Nova Scotia allow complaints to a Human Rights Commission, which will investigate the alleged incident of age discrimination and determine whether to refer the complaint to an adjudicative process. Other jurisdictions such as British Columbia and Ontario, allow an employee to apply directly to the administrative tribunal, which will accept, screen, mediate, and adjudicate the complaint.
You can also initiate a civil lawsuit alleging discrimination based on age. Often, age discrimination claims are pleaded with other actions, such as claims for wrongful dismissal.

Using Ontario as an example, the website notes that Human Rights Tribunal of Ontario (HRTO) can award financial compensation for money lost or spent due to discrimination, as well as for “injury to dignity, feelings, and self-respect.” Non-monetary judgements can include orders for the employer to hire or reinstate the person, provide a promotion, and remove any “harasser” from the workplace; in short, the employer must put the complainant in the position that would have existed in the absence of discrimination.

In addition, HRTO can require the employer to change hiring practices, develop non-discriminatory policies and procedures, implement appropriate education/training programs, post the Ontario Human Rights Code in the workplace, and even publish an extract of the HRTO decision in the corporate newsletter.

EMPLOYERS ARE BECOMING WARY

While all of this is clearly good, workplace age discrimination may in fact be increasing because of these new anti-discriminatory human rights laws.

In a 2014 article in The Globe and Mail, reporter Jeff Gray wrote: “With mandatory retirement for most workers gone, coupled with a demographic bulge and low returns on fixed-income investments, more older workers are putting off retirement and staying in the workforce than ever before. And employment lawyers say they are seeing an increasing number of age-discrimination cases as a result.”

Rudner confirms this development: “There are no statistics, but anecdotally, yes, a lot of employers have become wary of hiring older workers because they don’t have an end date. Before, when a worker turned 65, they could give them a gold watch and then they’re gone. Now if they hire someone at, say, age 63, they can’t let them go at 65.

“Even if a 64-year-old worker was slowing down, the employer knew that in another year, they’d be gone, so they let them continue working and then retire with dignity at 65,” GRAY says. “Now employers have no idea how much longer they’ll have to keep them, so they’re more reluctant to hire older employees. We’re definitely seeing more of that.”
The Globe article also noted that the courts are now more likely to award larger severance amounts to older workers who have less opportunity for re-employment: “For example, an Ontario court [in 2013] awarded a 70-year-old machine operator an additional 22-month severance, or $69,000, after 20 years of work. And in 2012, a 72-year-old civil servant in Alberta was given her job back and awarded several years of back pay after winning an age-discrimination case over a move not to renew her contract when she was 67.”

“The issue is a legal minefield for employers,” Rudner said at the time.

More Interesting Facts That You Should Be Aware Of

A Towers Perrin survey of 1,000 working Canadians revealed that three-quarters of those asked about their financial plans for retirement believe that their standard of living in retirement will be the same or better than it is right now. The same numbers of respondents are doing little or no planning for retirement.

More Contradictions

Three-quarters acknowledge it’s up to them to provide a major portion of their retirement income; but as many as half of working Canadians save less than $2,000 annually – and that includes contributions to workplace pension plans.

99 per cent of all survey respondents say planning is important; but the majorities say they are not doing enough planning.

People don’t plan to fail…they just fail to plan...

THE REALITIES OF RETIREMENT PLANNING

We are all looking to achieve goals, to feel that the thousands of hours that we spend working during our lifetimes are leading to a better future, and that at the end of it all, there might just be a pot of gold.

That pot of gold can be different for everybody. It could be an exotic holiday, a vacation home, or just to be able to provide a university education for the children. Many people, as they start to approach “retirement years”, would like to at least maintain or improve the same lifestyle that they had during their working years.

Often, it is assumed that this will happen because there are government benefits available and maybe even incomes from an employer pension plan as well.
They may have provided some retirement funding themselves throughout the years. The reality can be very different.

The total income you can expect from government and company pension sources is likely to be lower than your earnings during the working years.

It is also possible that you are not a member of an employment-related pension plan (less than half of all Canadians have the advantage of a company or union-sponsored pension plan).

When people finally do get around to looking at their anticipated retirement income requirements on paper, find the results surprising. In many of the cases, the figures show a far larger requirement for personal savings and investments than they even expected. Filling the financial gap between the retirement incomes you need and the retirement income you expect to receive is what your financial plan is all about. Your clients and prospects can have a retirement based on today’s lifestyle or one that is even more rewarding.

How much income a person requires for retirement is determined by their goals.

A person, who wants to travel extensively, would require more income than the person who is happy with staying close to home. There might also be personal circumstances to consider such as any dependents that rely on the financial support that you may provide. Many people realize that their lifestyle pattern is established during their middle years.

If your clients / prospects are between 40 and 60 years of age, it is wise for them to aim for retirement income that is equal to roughly 75% or the income that they currently have. This percentage is considered the accepted guideline if they wish to maintain a comparable standard of living in their retirement years. Obviously, it will not hurt to try to achieve a retirement income that is higher than your anticipated needs.

It is worth noting that tax incentives and increasingly flexible pension arrangements can tell a whole different story. The need for individual initiative in retirement planning is being encouraged because an increasing number of individuals will be drawing upon the pool of funds, which support government and private pension programs.

Bankers love the concept of mandatory retirement, or any other form of retirement. It means big money for the banks, who regularly fire up ads such as, "What are you doing after work?" And, "You're 20, you should be thinking of retirement."
The big season for bankers is the February run-up to the deadline for RRSPs, when they try to scare the daylights out of people by warning them if they don’t have $800,000 - or $500,000, or $1 million - socked away when they turn 65 they soon will be pushing their worldly goods ahead of them in a cart or living in a walk-up, eating cat food.

Retirement is big business for banks. Bankers believe people hate their jobs as much as bankers hate theirs, so they set out to convince people that retirement - Freedom 55 …Take This Job and Shove It - is the solution to worry and the road to happiness.

And yet, many people enjoy their jobs and dread being forced out of them merely because they have turned 65, which is a lot younger than 65 used to be in the 1920s, when pensions began. Someone turning 65 today is expected to live another 20 years.

The concept of retirement, especially mandatory retirement, is new. It began in the early decades of the 20th century. The first old-age pension in Canada began in 1927, financed by the federal and provincial governments, but administered by the provinces. It was available to Canadian citizens 70 years or older. The pension amounted to $20 a month, a munificent $240 a year, but only if the Canadian citizen passed a strict and demeaning means test. This was the situation for nearly 25 years.

Throughout the years, the age for receiving Old Age Security was lowered from 70 to 65 (more information about the OAS will be found later in this chapter).

There has been a sea change in attitudes to public pensions and the very concept of retirement, both mandatory retirement and early retirement. When the age of 70 was selected in the early 20th century as the age of eligibility for a government pension, life expectancy was between 60 and 65.

Because people live so much longer, and retire so much earlier, Ottawa has demanded higher contributions to the Canada Pension Plan, so it won’t dry up. There will be increased demands to raise CPP contributions in coming years as the parade of boomers opt out of the work force.

Compulsory retirement is especially hard on women, many of whom chose to stay home to be with their children in the early years, and then entered the work force in their late 20s or early 30s. Because they were, and often still are, paid significantly less than men, women can’t put away as much money as men. And it gets worse down the line, as women live, on average, five years longer than men.
Today there are four workers in Canada for every retired person. By 2020, there will be three workers for every retired person. The ratio will sink further without a dramatic increase in immigration, preferably people with lots of money and excellent job prospects.

Some companies are coping with this workforce shortage by instituting plans such as "retirees on call" and "phased retirement." These plans address the arguments of employers who favour compulsory retirement because it unloads workers who are at the peak of their earnings, allowing the companies in some cases to hire two young workers for the price of one older worker.

Bankers are correct in assuming most people don't like their jobs and want to retire if they can afford to. Only eight per cent of workers continue to work full-time after the age of 65. The average age of retirement in Canada is close to 62. But the eight per cent who want to keep working do so for a variety of reasons, including office camaraderie, job satisfaction, a sense of purpose and destination – and sometimes economic survival.

Many overestimate the joys of retirement. After a summer or two of playing golf or watching birds or afternoon soaps, they come to appreciate what Shakespeare meant when he wrote, "If all the year were playing holidays, to sport would be as tedious as to work.

Throughout this chapter, we will be looking at the various sources of retirement income that as Canadians, could be available to us. We will look at these areas in a general way, but we recommend that you do some research on your own so that you will be in a good position to be able to offer the best advice possible to your clients and prospects.

**How Much Do You Need to Save For Retirement?**

Retirement planning is about managing your money, so you can make the most of your retirement years. Your retirement plan should balance your needs, wants and the reality of your finances.

3 reasons to have a retirement plan

1. **Set goals** – A plan helps you set goals for retirement, including the age when you want to stop working and your lifestyle.

2. **Know how much to save** – It can help you figure out how much money you need to save to live comfortably in retirement.
3. **Choose what to invest in** – A plan can guide your investment choices based on your goals and your risk tolerance.

**How much you need to save depends on 3 things**

1. **Your age** – When you start saving makes a big difference in how much you need to put away. The younger you are when you start, the less money you must put aside, thanks to the power of compounding.

2. **Your lifestyle** – Do you plan to stay home or travel the world? The amount you’ll need to save will depend on the life you plan to lead when you retire.

3. **Federal government benefits** – You could be entitled to government retirement benefits like the Canada Pension Plan (CPP), Old Age Security (OAS) and the Guaranteed Income Supplement (GIS). If you’re eligible for income from these government programs, you might not have to save as much.

**THE RETIREMENT PLANNING PROCESS**

Now that we have looked at various retirement saving vehicles, and options on what to do with our retirement funds, do we have a retirement planning process that we can go through with our clients and prospects to determine what they want. This next section will deal with just that.

Many people realize that their lifestyle pattern is established in their middle years. It is at this point in their lives that it is usually possible to picture how they want to spend their retirement years. Depending on the type of lifestyle one wants to have in their retirement years will determine how much income they want to live on. A rough rule of thumb is to try and aim for about 75% of the income that you have now. This seems to be the required amount if they want to maintain a comparable standard of living in retirement.

Recently it has been widely publicized that we cannot rely solely upon various Company pensions and Government plans. Individual initiative is being encouraged because of an ever-increasing number of individuals who will be drawing upon the pool of funds, which support government and private pension programs.

Planning for your client’s retirement now is the best guarantee of a financially secure future.
A Financial Advisor has a special interest in their clients. This has a very definite link to the market place responsibilities of the advisor. Part of the responsibility lies in the open and full disclosure of the fund and its performance, how the fund performs, the returns that are earned and any capital gains paid. Each term requires an accurate and precise explanation to enable the client to make an informed decision when buying. Dividends, Capital Gains and Yields all have separate and distinct meanings that can be misleading if they are not explained properly.

THE RETIREMENT PLANNING PROCESS REQUIRES SIX PLANNING STEPS

1. Establishing Retirement Objectives

Not all a client’s objectives are well defined or thought out. Using a form of a “Retirement Planning Checklist” will help determine some of their objectives.

2. Gather Background Information

Before determining what steps a client must take to achieve their goals, it is necessary to establish their present situation. Detail all their income that they will have in their retirement years.

3. Develop Retirement Planning Strategies

This involves preparing a plan to accumulate and invest the necessary funds required to meet the client’s objectives.

Funding the client’s desired level of retirement income depends on:

- Expected lifestyle during retirement.
- How long to go before retirement?
- Life expectancy of the client and spouse.
- Anticipated income from RPPs, CPP and OAS etc.
- Built in assumptions to provide for inflation, interest earnings on invested funds and future tax rates.
- The amount currently being invested for retirement.

In addition to determining these facts, the planner will be required to look at all the investment products and determine which ones best suit the client’s savings targets. For the client who is still in the accumulation stage, this analysis may cause an adjustment in the level of income required or a reduction in expected lifestyle expenditures after retirement.
For a retired client, step 3 may determine the level of income that can be maintained and how best to utilize this income.

4. Implementing the Plan

The best-laid plans still require a first step. After determining the retirement planning strategies, the financial planner must assist the client in putting the action plan to work.

The action plan will involve objectives such as:

- Establishing a Spousal RRSP BY February 15, 2018
- Review Lifestyle Expenditures by October of 2018
- Contribute allowable contribution to RRSP for 2018 by February 28, 2019

Implementing the retirement plan may require a financial specialist to start certain specific strategies. This may involve an Investment and Tax Specialist as the plan progresses. A retired client may require an Estate Planning Specialist. The retirement planner may still be involved in providing an overview to see that all retirement objectives are being met.

5. Monitoring Progress

Monitoring the plan progress requires regular reviews and making changes as necessary. For younger clients, every 3 to 5 years may be sufficient, but for older clients, annual reviews may be necessary. Many changes take place such as, tax, government legislation, family changes and deaths.

It is also necessary to analyze the investment mix and performance and make changes when required.

6. Documenting Your Work

This step is important, to keep the client fully involved making sure they understand the recommendations that have been presented. It also protects the planner from future liability claims if the retirement investments do not perform as expected.

Computers and other forms of technology have generally reduced the effort required to organize the information required.
Each stage needs to be recorded regarding:

- Planning procedures.
- Assumptions regarding inflation, interest and tax rates.
- The outline of recommendations and strategies.
- The client’s decisions.
- Commitment to provide future monitoring.

This documentation follows the critical part of planning. It will help establish the long-term goals and relationship required for the plan to be successful. Documentation is the final step that a professional planner will provide in developing client’s needs.

The process is not completed at any one time, but usually is an ongoing function that is part of your client’s overall financial and estate-planning program.

All the foregoing steps can be referred to as establishing a financial plan with the client or prospect by doing a Financial Planning process. When this is completed, the following myths will be shattered.

**Some Reasons Why Your Clients and Prospects Might Say That They Do Not Need Financial Planning**

1. **I need to have some investments before I’ll have a need for a CFP.**

   Investing is about one fifth of what financial planning is all about. There is also risk management and insurance, income tax planning, retirement planning and estate planning. And to the extent that you don’t reduce your insurance expenses and income taxes and develop the discipline to start saving the amount needed to fund your retirement, you won’t have any investments to need advice about.

2. **I (or my stockbroker, or the managers of my mutual funds) can beat the market.**

   So, can about half of all orangutans flinging darts at a list of stocks. In any given year, there are many managers and investors who beat the market due to luck. But over the long haul, very few active managers beat the market because of management fees and transaction costs, and because they are wrong.

   The wonder is not that people like Warren Buffett and Peter Lynch exist, but that more of them do not exist. Based on pure probability, there should be hundreds or thousands more like them, but there are not. Why is that?
The market is a giant, efficient pricing mechanism that instantly incorporates new information into securities prices. Since all known information and all expected future events are already reflected in securities prices, prices are fair, and very few abnormal profit opportunities exist net of expenses (or at least you can’t take advantage of them.) What causes prices to change is new, unexpected information reaching the market. Since no one can consistently predict the future, no one can consistently beat the market, unless they are lucky and repeatedly guess correctly.

3. My estate won’t be subject to tax.

While that will probably be true for the first spouse to die, it will not be true for the surviving spouse, though life insurance can pay much if not all the tax bill. Other than the primary residence and the first $500,000 of capital gains on a small business, taxes will be due on all other capital property after both spouses die. And if you don’t have a spouse, guess what? CRA comes knocking after you meet your maker to take its pound of your flesh.

4. All my insurance is in order.

I have yet to meet a client who did not have inadequate limits, unnecessary coverage or inappropriate deductibles.

Additionally, consumers are generally unaware of all the factors that need to be considered for each type of policy whether it is life insurance, disability insurance, critical illness insurance or car insurance.

5. I’m saving enough for retirement.

Most Canadians aren’t, and most underestimate the amount of money they’ll need. The only way that one will know the amount they need for retirement is to create a financial plan that sets out specific goals you wish to prepare for, and after this you can then determine the capital you will need to set aside to accomplish your very personal goals. It is when you know the amount needed at the end of your working career are you able to know the amount of money you will have to set aside each month to achieve the retirement you so desire.

6. My estate will pass according to my will.

If your will is valid, it will only cover your probate estate. Jointly owned property, retirement plans, and life insurance proceeds are not covered by your will.
7. If something happened to me, my family would know what my wishes would be.

Did you know that many Canadians mistakenly believe that having a will or a power of attorney are not priorities? Nothing could be further from the truth. In fact, your will and power of attorney are probably the most important documents you will ever write.

Unless you’ve discussed your wishes with your family in detail and put them in writing, chances are they wouldn’t know what you want.

If you die without a will the province will decide how to distribute your estate. And if you have children who are minors, the provincial government through the public trustee will decide who will raise them and care for them. Children might be taken into public custody until guardians are identified.

This situation may occur if you become incapacitated and do not have a continue power of attorney. You should be reminded that the wishes and directions that you place in your will do not have legal authority and until you have died.

8. Old Age Security and the Canadian Pension Plan will provide most of my retirement income.

For 2012, the maximum combination that Old Age Security and the Canadian Pension Plan benefit for people who retire at 65 years old is $1,526.79 per month. Our government administered retirement benefit programs were only designed to provide one third of an individual’s total retirement income. The remainder is to be generated from both employer pension plans and the retiree’s own savings.

9. I don’t need to save for my retirement because I’m going to die young.

So, what will happen if you don’t die young? This year, approximately one in 117 Canadians will die, what are the odds that you will be one of them. In past generations people lives would go like this, they work for 40 years, retire at age 65, live off their savings for a few years, and by the age of 70, they would be pushing up daisies.

In the past, the primary concern of retirees was losing their money. Going forward, the top worry for retirees will be the chance of out-living their money. With advances in health and science, some futurists are predicting that many people alive today will live to be well over 100.
10. I can’t afford a financial plan right now.

Perhaps part of the reason you think you can’t afford one is because you’re paying too much in insurance premiums, income taxes, interest and investment expenses, all of which a Certified planner can help you reduce. And fees you pay for investment advice and tax planning are tax deductible. Hiring a competent, fee-only planner to prepare a comprehensive financial plan will probably be the best investment you will ever make.

SAMPLE RETIREMENT PLANNING CHECK LIST

One of the most important functions of planning is the ability to foresee future needs. The answers to the following questions will assist you in helping your clients and prospects to plan their future.

<table>
<thead>
<tr>
<th>QUESTION</th>
<th>ANSWERS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Do you know of any potential health problems?</td>
<td></td>
</tr>
<tr>
<td>2. Will you have the financial resources you need for retirement?</td>
<td></td>
</tr>
<tr>
<td>3. Considering inflation, will the growth of these resources be sufficient to fund retirement</td>
<td></td>
</tr>
<tr>
<td>4. What money can you expect from each source?</td>
<td></td>
</tr>
<tr>
<td>5. What will be your after-tax income?</td>
<td></td>
</tr>
<tr>
<td>6. What fixed expenses will you have?</td>
<td></td>
</tr>
<tr>
<td>7. What expenses will you be able to reduce or eliminate?</td>
<td></td>
</tr>
<tr>
<td>8. Will you live in this home or move?</td>
<td></td>
</tr>
<tr>
<td>9. If moving, will you live: in this area, another part of the country, or abroad?</td>
<td></td>
</tr>
</tbody>
</table>
10. Will you move to a house or condo?

11. Will it be in a retirement community?

12. Will you continue to work: full time, part time or will you start a business?

13. What hobbies and activities will you have to keep you active?

**GOVERNMENT RETIREMENT INCOME SOURCES**

Canada’s Public Pension Plan History

Canada’s first public pension plan had been introduced in 1927 with the passing of the *Old Age Pensions Act*. That legislation established a means-tested pension for men and women 70 years of age and over who had little or no income. Benefit costs were shared equally between the provinces and the federal government until 1931, when Ottawa’s portion was increased to 75 per cent. This increase was the result of an election campaign promise made by Prime Minister Bennett.

The provinces joined the program gradually. British Columbia led the way in 1927. The other three western provinces joined by the end of the decade, as did Ontario. The Atlantic provinces were relative latecomers, partly because of internal political factors and partly out of concerns over the cost. These provinces were not well off financially, and they had larger than average numbers of seniors amongst their populations.

Prince Edward Island began participating in the Old Age Pensions program in 1933, Nova Scotia in 1934, and New Brunswick in 1936. Nova Scotia was helped in meeting its pension payments by the revenues from government-owned liquor outlets opened after the ending of Prohibition in the province.

Quebec entered the program shortly after New Brunswick in 1936. By this time enduring traditional attitudes to poor relief that saw responsibility resting with municipalities and charities, not with the state, had been overcome by political figures and labour groups in the province.

Over time, amendments to the *Old Age Pensions Act* relaxed some of the eligibility criteria and opened the program to greater inclusiveness.
In 1937, benefits for blind people over the age of 40 were provided, and in 1947 the British citizenship and five-year provincial residence requirements were removed, while the age of qualification for blind pensioners was reduced to 21. Incidentally, 1947 was also the year that Canadian citizenship first became possible, by the new Canadian Citizenship Act. It is interesting to note the implications that this had for women. The Old Age Pension legislation had made a point of allowing widows who had been British subjects before marriage to a non-British subject to continue to qualify for a pension under the program like other British subjects. This had to be clarified since, before the 1947 citizenship legislation, a married woman was usually seen to share the nationality of her husband. Now she was able to hold citizenship in her own right.

While the most recent Old Age Pensions scheme was an improvement on earlier relief practices, official efforts to minimize public costs and enforce family responsibility for the care of seniors made it increasingly unpopular. The means test, for example, was justified by the fact that the provinces formally obliged adult children to support their aged parents if they were able to do so.

Applicants had to prove that their children could not support them to be considered for a pension. Officials even encouraged some elderly parents to sue their children for maintenance so that the state could be relieved of responsibility or, at the very least, benefits could be reduced.

Equally distasteful was the provision in the Old Age Pension program that enabled the government to recover the total amount of benefits paid out through claims against the estates of deceased recipients. By the end of the 1940s, the Old Age Pension system was in disrepute. There was popular demand for reform that would do away with the degrading means test and lower the qualifying age to help workers who found themselves out of the workplace before reaching the age of 70.

By 1951, maximum Old Age Pension payments were $40 per month and 308,825 people were participating in the program. The latter figure amounted to about 47 per cent of Canadians 70 years of age or over. In comparison, more than 3.5 million people in Canada received the maximum Old Age Security pension in 2000. According to Statistics Canada’s data this represents 93 per cent of the population aged 65 and over, with many non-recipients being newcomers to Canada who had not met the minimum residence requirements.

In 1951, the Old Age Pensions Act of 1927 was replaced by the Old Age Security Act and the Old Age Assistance Act. The new programs generated by this legislation went into effect on January 1, 1952 under the administration of the federal Department of National Health and Welfare.
The *Old Age Security Act* introduced a universal, flat-rate pension for people 70 and over, with 20 years residence in Canada immediately prior to the approval of an application as sufficient qualification. People who had been absent in that time could still receive payments if they had been a resident prior to the 20 years for twice the length of time away, provided the last year had been spent in Canada.

Benefits would be $40 per month as they had been since 1949 under the *Old Age Pensions Act*, an amount that would be equivalent to $266 in the year 2000. The program would be managed by the federal government alone. Old Age Security pensions would be financed through a small (two per cent) increase in personal income and corporate taxes and the earmarking of a portion (again, two per cent) of manufacturers’ sales taxes for this purpose. Application forms for the new pensions could be picked up at the post office and once enrolled in the program, everyone received the full amount. Pensioners who went to live abroad forfeited their benefits, but an absence of six months or less entitled them to receive payment for three of those months upon their return.

The number of Canadians receiving old age pensions more than doubled with the introduction of the new program, and this time status North American Indians were included. Blind people, formerly receiving benefits under the *Old Age Pensions Act*, were provided with their own program under the *Blind Persons Act* passed in 1951. By March 1952, Old Age Security was being paid to over 643,000 people. Over the next full fiscal year, that figure would rise steadily, and expenditures would reach $323 million, or about seven per cent of the total federal budget. In comparison, combined Old Age Security and Canada Pension Plan payments totalled $42 billion in 2000 and represented about 25 per cent of federal spending in Canada.

To complement the new Old Age Security program, the *Old Age Assistance Act* established a cost-shared, income-tested allowance for people between the ages of 65 and 69. The provinces would administer the Old Age Assistance program and the federal government would reimburse them for 50 per cent of their benefit costs through grants-in-aid from the Consolidated Revenue Fund, made up of general revenues. When recipients reached 70, they would transfer to the Old Age Security pension.

Eligibility was confined to people between 65 and 69 whose income fell below a certain threshold. Maximum benefits were set at $40 per month, but as outside income approached the threshold, the $40 figure would be reduced. Residency rules were the same as for Old Age Security, except that it was not necessary to have lived in the country for the year immediately prior to the start of payments. Old Age Assistance would not be paid for absences from Canada.
There was no citizenship requirement, and Aboriginal peoples were eligible for this program as well, but exclusions included people who were in receipt of war veterans or blind persons allowances. Significantly, the federal government no longer insisted that provinces make recovery attempts against pensioners’ estates. A little over a year after Old Age Assistance went into effect on March 31, 1953, approximately 20 per cent of the population between the ages of 65 and 69 were receiving these benefits.

By the early 1960s, the 20-year residence rule had been reduced to 10 years and regulations applying to the payment of Old Age Security pensions to people who were absent from the country had become less restrictive. Benefits had risen to $75 per month through ad hoc increases made by governments from time to time. As well, the personal, corporate, and sales taxes that funded the Old Age Security program had been increased.

By 1964, the government was distributing $755 million per year in Old Age Security pensions and $77 million per year in Old Age Assistance. The Old Age Security Fund out of which pensions were paid had acquired a deficit of approximately $670 million. Increases in funding were not sufficient to cover the rising pension costs, and more and more the program had to rely on the Consolidated Revenue Fund (i.e. general taxes) to make up the shortfall.

In 1965, with the passing of the Canada Pension Plan legislation, the qualifying age for Old Age Security was reduced from 70 to 65. The adjustment would take place one year at a time over the next five years. Old Age Security benefits were still $75 per month, but they would now be indexed, with provision for automatic increases of up to two per cent per year based on inflation. Old Age Assistance benefits would continue to be paid until Old Age Security came down to the age of 65 and rendered them obsolete. A revision in the residency requirements made it possible for applicants to discount absences if they had lived in Canada for a total of 40 years after reaching the age of 18.

Another amendment of the Old Age Security Act in 1966 established the income-tested Guaranteed Income Supplement. Although the first Canada Pension Plan pensions would commence on January 1, 1967, full pensions would not be available until 1976. The Guaranteed Income Supplement was meant to be in place only long enough to help the people who reached 65 before the full Canada Pension Plan pensions became available and who would have little or nothing other than Old Age Security, and perhaps a reduced Canada Pension Plan pension, to live on. However, the supplement was later made a permanent feature of the program. Under its provisions, income outside Old Age Security benefits was measured and the maximum supplement payable was reduced 50 cents per dollar.
Guaranteed Income Supplement payments would start in 1967 with a maximum set at 40 per cent of the indexed Old Age Security benefits. Unlike benefits under the earlier Old Age Assistance program, Guaranteed Income Supplement payments could be made to persons absent from Canada, but only if they were gone for six months or less. By the end of March 1967, Guaranteed Income Supplement payments were being paid to over 500,000 people.

While Old Age Security and the Guaranteed Income Supplement were designed to provide a basic minimum amount to Canadian seniors, the new Canada and Quebec Pension Plans were contributory social insurance programs established to provide basic death, survivor and disability benefits as well as retirement coverage. The Canada Pension Plan was compulsory and earnings-related. It would cover the clear majority of workers between the ages of 18 and 70, and there were no residency requirements.

Like Old Age Security, the qualifying age for the Canada Pension Plan retirement pension would be reduced to 65 over the five-year period between 1965 and 1970. Contributions would commence in 1966 and were to be made by both employees and employers, with each paying the equivalent of 1.8 per cent of a worker's earnings between an exempted minimum amount and a stipulated maximum, or ceiling. At the beginning of the Plan, this meant earnings between $600 and $5,000 were considered "pensionable".

For the self-employed, the contribution rate would be 3.6 per cent of pensionable earnings, as they were to pay both employee and employer shares. Anyone with an income less than $600, or $800 if self-employed, was not included in the Plan and made no contributions. Contributions would not be collected on income over $5,000.

Retirement benefits would be 25 per cent of the average pensionable earnings a worker earned in his or her lifetime. These earnings were adjusted to inflation, and benefits would be paid monthly. The higher the earnings, the higher the ultimate benefits. In the beginning, for an individual to qualify for a full pension, he or she had to have made contributions for at least ten years. Therefore, although the first benefits would start on January 1, 1967, full pensions would not be available until 1976. If a person took the pension before that time, he or she would receive an amount proportionately below the 25 per cent that had been established as the level in the legislation.

Canada Pension Plan contributions were collected through payroll deductions, or at the time of tax return submissions in the case of the self-employed. North American Indians whose income was earned on reserves and therefore not subject to income tax were excluded from the Canada Pension Plan.
For people who were in the Plan, contributions but not benefits would be exempt from income tax.

All contributors needed a Social Insurance Number. The Social Insurance Number was introduced in 1964 to provide the Unemployment Insurance program with an improved numerical system for record-keeping. Since the Canada Pension Plan and the Quebec Pension Plan would also require an efficient and computer-compatible system for keeping track of transactions with contributors and beneficiaries, and a majority of future Canada Pension Plan and Quebec Pension Plan participants were already registered for Unemployment Insurance, the same nine-digit personal identifier was to be used for both programs.

Old Age Security recipients were not required to have a Social Insurance Number. Their benefits were partly funded by income tax, but the government did not keep a record of individual contributions, or link them to eventual benefits, as was the case with the Canada Pension Plan.

Like Old Age Security and the Guaranteed Income Supplement, the Canada Pension Plan was placed under the general administration of the Department of National Health and Welfare, although the Department of National Revenue would take care of matters related to the collection of contributions. The Department of Finance would oversee surplus monies, which were loaned to the provinces at a favourable rate of interest.

When the Department of National Revenue received Canada Pension Plan contributions, they were placed in a special account in the Consolidated Revenue Fund. In addition to the Canada Pension Plan Account, there was a Canada Pension Plan Investment Fund that would take the surplus that accumulated over and above administration costs and the amount of money required to pay immediate benefits (i.e. three months' worth) and invest it in provincial and federal securities.

As the Quebec Pension Plan was a separate (though parallel) plan, contributions remained under the control of the Quebec government, which was responsible for investing any reserves. The other provinces would have access to Canada Pension Plan surpluses, in proportion to the contributions made by their residents, through the sale of provincial bonds and provincially guaranteed securities on 20-year terms at the long-term federal bond rate. These were payable to the Canada Pension Plan Investment Fund. Access to the Canada Pension Plan surpluses would provide the provinces with a valuable and much-desired borrowing source for development capital. The federal government agreed to this access during Canada Pension Plan negotiations.
It was an additional enticement to get provinces to agree to federal proposals for a national contributory program.

The Canada Pension Plan legislation provided for an appeals process for people who were unhappy about decisions concerning their benefits or eligibility. The first resort was to the Minister of National Health and Welfare. Then further appeals could be made to a Review Committee and, finally, the Pension Appeals Board. Queries related to contributions were to be directed to the Tax Court of Canada (formerly the Tax Review Board) established under authority of the *Income Tax Act*. Old Age Security appellants were provided with the first two levels only, although appeals related to income were, likewise, heard by the Tax Court of Canada.

The Canada Pension Plan came into effect on January 1, 1966 and applied to all provinces and territories except Quebec, where the separate but similar Quebec Pension Plan was established in the same year. By agreement the two plans would be coordinated so that workers could move freely from one to the other without penalty.

Both were subject to the same contribution and benefit rates and offered not only retirement benefits, but disability, survivor, and lump-sum death benefits. Both were indexed on a yearly basis. Membership and contributions did not terminate with a change in employment as they had under private employer-sponsored plans; they were portable. Contributions merely commenced again with the new employment. In addition, there was provision for future agreements with other countries regarding reciprocal pension arrangements.

**CANADA (CPP) AND QUEBEC PENSION PLANS (QPP)**

**Recent CPP Changes**

In the June 2016 federal, provincial and territorial finance ministers finally reached an agreement to expand the Canada Pension Plan. However, because the changes will be phased in over an extended period, there has been considerable confusion among many Canadians about how both CPP contributions and benefits will increase, and who the winners and losers will be.

An expanded CPP is designed to address the shortfall in middle-income retirement planning that is occurring because of disappearing corporate pensions. “Most at risk are workers under the age of 45 with middling incomes – say, families earning about $50,000 to $80,000 a year,” note authors Janet McFarland and Ian McGugan. “Without the defined-benefit pensions that their parents enjoyed, many could hit retirement with little in savings.”
Here Is What You Need to Know About the Planned CPP Changes

Effects on CPP retirement pension and post-retirement benefit

Currently, you and your employer pay 4.95% of your salary into the CPP, up to a maximum income level of $55,300 a year. If you are self-employed you contribute the full 9%.

When you retire at the age of 65, you will be paid a maximum annual pension of $13,370 (2017) under the program if you contributed the maximum amount each year for 40 years (subject to drop out provisions). People earning more than $55,300 do not contribute to CPP above that level, and do not earn any additional pension benefits.

The first major change will increase the annual payout target from about 25% of pre-retirement earnings to 33%. That means if you earn $55,300 a year, you would receive a maximum annual pension of about $18,250 in 2017 dollars by the time you retire — an increase of about $4,880/year (subject to the phase in discussed below).

The second major change will increase the maximum amount of income covered by the CPP (YMPE) from $55,300 to about $79,400 (estimated) when the program is fully phased in by 2025, which means higher-income workers will be eligible to earn CPP benefits on a larger portion of their income.

For a worker at the $79,400 income level, CPP benefits will rise to a maximum of about $19,900 a year (estimated in 2016 dollars). Contributions to CPP from workers and companies will increase by one percentage point to 5.95% of wages, phased in slowly between 2019 and 2025 to ease the impact. The federal finance department says the portion of earnings between $54,900 and $79,400 will have a different contribution rate for workers and employers, expected to be set at 4%.

The enhancement also applies to the CPP post-retirement benefit. If you are receiving a CPP retirement pension and you continue to work and make CPP contributions in 2019 or later, your post-retirement benefits will be larger.

Impact on CPP disability benefit/survivor’s benefit

The enhancement will also increase the CPP disability benefit and the CPP survivor’s pension starting in 2019. The increase you receive will depend on how much and for how long you contributed to the enhanced CPP.
Impact on CPP death benefit

There is currently a one-time lump sum taxable death benefit of $2,500 for eligible contributors of $2,500. This amount will not change.

The main beneficiaries of the CPP changes will be young employees, who are less likely to have workplace pension plans than older workers. To earn the full CPP enhancement, a person will have to contribute for 40 years at the new levels once the program is fully phased in by 2025. That means people in their teens today will be the first generation to receive the full increase by 2065.

The recently released Old Age Security report from chief actuary Jean-Claude Ménard which includes the GIS illustrates how higher CPP premiums scheduled to begin in 2019 will ultimately affect the OAS program.

The report reveals that because of the planned CPP changes, by 2060, 6.8% fewer low-income Canadians will qualify for the GIS, representing 243,000 fewer beneficiaries. This will save the federal government $3-billion a year in GIS payments.

In other words, higher CPP benefits mean some low-income seniors will no longer qualify for the GIS, which is a component of the Old Age Security program. The GIS benefits are based on income and are apply to single seniors who earn less than $17,688 a year and married/common-law seniors both receiving a full Old Age Security pension who earn less than $23,376.

What Is CPP Like Today?

These earnings-related plans are intended to provide, from age 65, a pension of 25% of average earnings of the average industrial wage.

Several supplementary benefits are available to family members in the event of death or disability.

Unlike the Old Age Security program, which is financed out of general tax revenues, the Canada and Quebec Pension Plans are financed principally by compulsory contributions from income-earners on their annual “pensionable earnings,” as determined each year. There are joint contributions made by the employer/employee. These contributions are all tax deductible. Benefits when received are taxable.
All CPP/QPP pensions and benefits are payable without regard to other income.

Generally, all person’s ages 18 to 69 whose employment earning exceed a minimum known as the “year’s basic exemption” are eligible to receive this benefit.

**Canada Pension Plan Contributions**

For 2018, employees and employers must each pay 4.95 % of employees' contributory earnings. Contributory earnings are those between a certain “floor” (years' basic exemption) and “ceiling” (years’ maximum pensionable earnings) and are subject to change yearly. The self-employed rate is 2 x the employee rate or 9.9% of earnings on the same basis.

**Quebec Pension Plan Contributions**

The QPP factors are the same as the CPP factors up to and including 2011. However, Revenue Quebec announced changes to the QPP contribution rate at that time. The employee and employer rates each increased by 0.075% per year starting in 2012, until each of these rates reached 5.4% in 2018. The self-employed rate is 2 x the employee rate or 10.8%.

Contributions are payable from January 1, 1966 or age 18 (whichever occurs later) until age 70 or until retirement from regular employment between ages 60 and 70.

**How do you calculate CPP average monthly pensionable earnings?**

Monthly retirement pensions at age 65 are at the level of 25% of AMPE. The AMPE is adjusted by calculating one-twelfth of the year’s maximum pensionable earnings (YMPE) averaged over the last five years, including the current year.

This description is an oversimplification and the actual amounts payable will be affected by several factors including adjustments to the floor and ceiling for contributions, and the Pension Index.

A contributor can elect to receive a reduced pension from age 60 upon satisfactory evidence of having “wholly or substantially ceased working.” For each month that the contributor is under age 65 when the pension begins the amount will be reduced by 0.5% (6% per year).

Therefore, at age 60 the pension will be 70% of the pension that would have been payable at age 65.
Likewise, for each month that the contributor is over age 65, the amount of income will be increased by 0.5%. This translates to an increase of 30% for a pension beginning at age 70. Age 70 is the maximum age that a pension can commence.

A reduced pension will not be adjusted upward when the pensioner reaches age 65.

**AMPE is calculated by using the formula:**

\[
AMPE = TPE \times \frac{TMCP}{120}
\]

where:
- **TPE** (Total pensionable earnings)
- **TMCP** (Total months in contributory period) or 120 months, whichever is greater?

TPE represents the total earnings of the contributor, excluding any earnings over the annual ceiling each year from the effective date for contributions (January 1, 1966 or age 18, whichever occurs later) until age 65. TMCP means the total number of months from the effective date of the plan (January 1, 1966) or age 18, whichever occurs later, until age 65.

Adjustments may be made to both TPE and TMCP. For example, to some extent any periods of low or zero earnings are automatically excluded, as are the periods of low or zero earnings when a person cared for a child under the age of seven years old.

**Can retirement pensions be shared with spouses?**

You can share your Canada Pension Plan retirement pension with your spouse or common-law partner. To do so, you must be receiving your pension, or be eligible to receive it, and be living with your spouse or common-law partner.

Sharing your pension may result in tax savings.

You **must apply** to share your pension.

There are two ways to share a pension:

1. If only one of you contributed to the Canada Pension Plan (CPP) and/or the Quebec Pension Plan (QPP), you can share the one pension.
2. If both of you contributed, you and your spouse or common-law partner may receive a share of both pensions. The combined total amount of the two pensions stays the same whether you decide to share your pensions or not.
The portion of your pension that can be shared is based on the number of months you and your spouse or common-law partner lived together during your joint contributory period. This period is the time when either one of you could have contributed to the CPP and/or QPP. Your Statement of Contributions has all the details about your contributions.

**What happens to the CPP retirement pension when pension sharing ends?**

- Your pension is adjusted to the amount you were to receive before the pension-sharing arrangement.
- If you contributed less to the CPP than your spouse or common-law partner or if you never worked, the amount of your retirement pension could decrease.
- If you contributed more to the CPP than your spouse or common-law partner, your retirement pension amount could increase.

**CANADA and QUEBEC PENSION PLAN – 2018 FACTS AT A GLANCE**

Canada Pension Plan rates are adjusted every January if there are increases in the cost of living as measured by the Consumer Price Index.

**Consumer Price Index**

Statistics Canada developed the CPI to measure changes in the cost of living. The CPI tracks cost changes in common household expenses. This "basket" of goods consists of food, shelter, clothing, transportation, health care and other average household expenditures.

Statistics Canada is currently using 1992 as the base year. In 1992, the CPI was equal to 100. This means that the basket of goods in 1992 cost Canadians $100.00. The CPI in January 2018 was measured at 131.7, meaning that the same basket of goods that cost $100.00 in 1992 cost $131.70 in 2018.

This FOLLOWING table lists the maximum monthly rates for the CPP & QPP benefits for 2018.
Canada Pension Plan Payment Rates as of January 1, 2018

<table>
<thead>
<tr>
<th>Type of benefit</th>
<th>CPP Maximum</th>
<th>QPP Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disability benefit (severe &amp; prolonged)</td>
<td>$1,335.83</td>
<td>$1,385.80</td>
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<tr>
<td>Retirement pension (at age 65)</td>
<td>$1,134.17</td>
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<tr>
<td>Survivors benefit (age 65 and over)</td>
<td>$680.50</td>
<td>$680.50</td>
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<tr>
<td>Children of disabled contributors benefit (Severe and prolonged)</td>
<td>$244.64</td>
<td>$77.67</td>
</tr>
<tr>
<td>Children of deceased contributors benefit (Orphan Benefit)</td>
<td>$244.64</td>
<td>$244.64</td>
</tr>
<tr>
<td>Death benefit (max lump sum)</td>
<td>$2,500.00</td>
<td>$2,500.00</td>
</tr>
</tbody>
</table>

Various other important CPP & QPP information

| Year’s maximum pensionable earnings (YMPE) (ceiling) | $55,900.00   |
| Year’s basic exemption (YBE) (floor)                | $3,500.00    |
| Year’s maximum contributory earnings (YMPE – YBE)   | $52,400.00   |

Maximum CPP required contribution in 2018 - Employee and employer each pays 4.95% (9.9% total) of contributory earnings for a total of $2,593.80

Maximum QPP required contribution in 2018 - Employee and employer each pays 5.4% (10.80% total) of contributory earnings for a total of $2,829.60

PLANNING FEATURES OF THE CANADA PENSION PLAN

Canada Pension Plan survivor benefits are paid to a deceased contributor's estate, surviving spouse or common-law partner and dependent children.

There are three types of benefits

1. The death benefit is a one-time payment to, or on behalf of, the estate of a deceased Canada Pension Plan contributor.
2. The survivor’s pension is a monthly pension paid to the surviving spouse or common-law partner of a deceased contributor.
3. The children’s benefit is a monthly benefit for dependent children of a deceased contributor.
It is important to apply for Canada Pension Plan benefits. If you do not apply, you may lose benefits you are entitled to receive.

For the survivors’, orphans’ and death benefits, the contributor must have contributed for at least three years. If the contributory period is more than nine years long, contributions must have been made for the lesser of 10 calendar years, or one-third of the calendar years in the contributory period. The contributory period is from the start of the plan or age 18 (whichever is later) until death, disability or retirement at age 65 or over.

Disability Pension

To be eligible for the disability pension or for benefits for the child of a disabled pensioner, a contributor must have contributed for five of the last 10 years of the contributory period or two of the last three years of the period. There is a three-month waiting period. This income is based on a flat rate (indexed and adjusted annually) plus 75% of what retirement benefit would have been at age 65.

Surviving Spouses Pension

This benefit is available to people under age 35, with dependents or if disabled.

For the survivor between the ages of 35 – 45 with no dependents, 1/120th reduces the benefit for each month under age 45. This pension continues at a reduced level to age 65.

Orphans Benefit

An orphan is a child (under age 18 or up to age 25 if they are still in school) whose contributing parent or guardian has died. The benefit is a flat rate component for each orphan (subject to change).

The benefit for each child of a contributor who becomes disabled will be the same as for orphans. Orphan’s benefits are paid to the surviving spouse or guardian if the orphan is under the age of 18 and are payable directly to the orphan from age 18.

In cases where both parents are contributors and they die or become disabled, a dependent child can receive two benefits.
Death Benefit

The CPP maximum death benefit for 2018 is a lump sum that is equal to 6 times the monthly retirement pension that would have been paid to a maximum of $2,500.00.

OLD AGE SECURITY (OAS)

Old Age Security benefit rates are reviewed in January, April, July and October to reflect increases in the cost of living as measured by the Consumer Price Index.

As previously mentioned, The Old Age Security Act came into force in 1952, replacing legislation from 1927 requiring the federal government to share the cost of provincially-run, means-tested old age benefits.

The Act has been amended many times. Among the most important changes have been:

- The reduction in age of eligibility from 70 to 65 (1965);
- The establishment of the Guaranteed Income Supplement (1967);
- The introduction of full annual cost-of-living indexation (1972);
- Quarterly indexation (1973);
- The establishment of the Spouse’s Allowance (1975);
- Payment of partial pensions based on years of residence in Canada (1977);
- The inclusion of Old Age Security in international social security agreements (ongoing);
- The extension of the Spouse’s Allowance to all low-income widows and widowers aged 60 to 64 (1985);
- Maximum of one year of retroactive benefits (1995);
- The ability for an individual to request that their benefits be cancelled (1995); and
- The extension of benefits and obligations to same-sex common-law partners (2000).

And Still Further OAS changes

The Liberal Party was elected with a majority government on October 19, 2015. They indicated they will restore the eligibility age for OAS and the Guaranteed Income Supplement (GIS) to 65 and will increase the GIS for single low-income seniors by 10%.
The Federal 2016 Budget cancelled the provisions in the Old Age Security Act that increased the age of eligibility for OAS and GIS benefits from 65 to 67 and Allowance benefits from 60 to 62 over the 2023 to 2029 period. Thus, some of the information below is no longer applicable.

The Budget also announced that the Government is looking at how a new **Seniors Price Index** that reflects the cost of living faced by seniors could be developed to be used as the index for increasing the OAS and GIS.

Proactive enrolment was implemented in a phased-in approach starting in 2013, eliminating the need for many seniors to apply for OAS and GIS. Service Canada sends a notification letter to those who can be automatically enrolled. The letter is sent the month after you turn 64.

Since July 1, 2013, the Government allows for the voluntary deferral of the OAS pension, for up to 5 years, to receive a higher, actuarially adjusted, annual pension. The OAS pension will be increased by 0.6% for each month that it is deferred past the usual starting age of 65. This is 7.2% for each full year that it is deferred. If it is deferred for the maximum length of time, to age 70, it will be increased by 36%.

**Funding**

The Old Age Security program is financed from Government of Canada general tax revenues.

The Income Security Programs Branch of HRDC administers the Old Age Security program through regional offices located in each province and territory. The International Operations Division in Ottawa, as its name suggests, is responsible for benefits stemming from Canada’s International Social Security Agreements.

**Indexation**

All benefits payable under the Old Age Security Act are adjusted in January, April, July and October if there are increases in the cost of living as measured by the Consumer Price Index.
Reconsidering and appealing a decision

Old Age Security clients may request an explanation or a reconsideration of any decision that affects their eligibility or the amount of their Old Age Security pension. This request must be made in writing to their Regional Director of Income Security Programs within 90 days of receiving a decision.

If not satisfied with the decision of the Regional Director, the client may appeal, again within 90 days, to a Review Tribunal. If the grounds of appeal are income related, the appeal will be referred to the Tax Court of Canada for a decision.

OAS Qualifications

The Old Age Security pension is a monthly benefit available, if applied for, to most Canadians 65 years of age or over. Old Age Security residence requirements must also be met. An applicant's employment history is not a factor in determining eligibility, nor does the applicant need to be retired. Old Age Security pensioners pay federal and provincial income tax. Higher income pensioners also repay part or all of their benefit through the tax system.

Eligibility conditions

To qualify for an Old Age Security pension:

- A person must be 65 years of age or over, and must be a Canadian citizen or a legal resident of Canada on the day preceding the application's approval; or
- A minimum of 10 years of residence in Canada after reaching age 18 is required to receive a pension in Canada.
- If you have lived in Canada for 40 years after age 18, you should be eligible to receive the maximum pension.
- For Canadian seniors living outside Canada, the OAS is still available for those who were Canadian citizens or legal residents at the time they left the country, if they lived at least 20 years in Canada after age 18. If no longer living in Canada, you must have been a Canadian citizen or a legal resident of Canada on the day preceding the day he or she stopped living in Canada.
- If you spent time outside Canada working for a Canadian employer, this may still count toward your time lived in Canada. For Canadian seniors living outside Canada, the OAS is still available for those who were Canadian.
In such cases, a person must have lived in Canada for the 10 years immediately prior to approval of the Old Age Security application. Absences during this 10-year period may be offset if, after reaching the age of 18, the applicant lived in Canada before those 10 years, for a period that was at least three times the length of absence.

In this case, however, the applicant must also have lived in Canada for at least one year immediately prior to the date of the application’s approval. For example, an absence of two years between the ages of 60 and 62 could be offset by six years of residence after age 18 and before reaching age 55.

A person who has lived in one or more countries with which Canada has a reciprocal social security agreement may count the periods of residence in those countries to satisfy the minimum residence requirements. Canada has agreements with more than 27 countries.

Amount of benefits

The amount of a person’s pension is determined by how long he or she has lived in Canada, according to the following rules:

- A person who has lived in Canada, after reaching age 18, for periods that total at least 40 years, may qualify for a full Old Age Security pension;

- A person who has not lived in Canada for 40 years after age 18 may still qualify for a full pension if, on July 1, 1977, he or she was 25 years of age or over, and lived in Canada on July 1, 1977; or

- Had lived in Canada before July 1, 1977, after reaching age 18; or possessed a valid immigration visa on July 1, 1977.

OAS Clawback for 2018

Revenue Canada has a claw back provision in the form of a special tax of 15% for taxpayers that have a net income over $75,910.

The repayment amounts are normally deducted from their monthly payments before they are issued.
If the full amount is received, it will be clawed back on the same basis, with the repaid portion being deductible in determining the amount of income subject to personal income tax.

The full OAS pension is eliminated when a pensioner’s net income is $122,843 or above.

OAS benefits are indexed quarterly in relation to increases as reflected in the Consumer Price Index.

This is not a benefit that will come without applying for it. Up to one year’s retroactive payment will be allowed to a person entitled and who files a late application.

**Capital Gains Can Increase Your OAS Clawback**

Yes, this is true even if you have capital losses carried forward that will eliminate the capital gains and is also true of the age amount clawback. This is because the OAS clawback is calculated based on your net income before adjustments on line 234 of your tax return.

The capital losses (and non-capital losses) **carried forward** are deducted after this, on line 253. The total taxable income is on line 260 of your tax return.

### THE 2018 OAS BENEFITS

<table>
<thead>
<tr>
<th>OLD AGE SECURITY PROGRAM</th>
<th>Jan. – Mar. 2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clawback rules are in effect as per above</td>
<td>$586.66</td>
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<table>
<thead>
<tr>
<th>Guaranteed Income Supplement (GIS)</th>
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<tbody>
<tr>
<td>Single</td>
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<tr>
<td>Married to pensioner</td>
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<tr>
<th>Spouses Allowance (SPA)</th>
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<tbody>
<tr>
<td>Regular</td>
</tr>
<tr>
<td>Allowance for Survivor</td>
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</table>
GUARANTEED INCOME SUPPLEMENT (GIS)

In addition to the OAS pension, a Guaranteed Income Supplement (GIS) is available based on need, as determined by income. In the case of a married applicant, the income of both spouses is considered.

The amount is determined by one of two rates. One rate applies to a single pensioner and to a married pensioner whose spouse is receiving either the OAS pension or the Spouse’s Allowance.

The other rate applies to a legally married or “common-law” couple where each spouse is a pensioner or one of them is a pensioner and the other is receiving the Spouse’s Allowance.

If a pensioner is receiving only a partial OAS pension (due to insufficient residence) the GIS is increased to close the gap between the full pension and the partial pension.

Depending on income, a Spouse’s Allowance may be available to a pensioner’s spouse (legal or common law) or to a widowed spouse. The applicant must be between the ages of 60 and 65 and satisfy the residency requirements.

A claw back of $1 for every $2 of other income applies to single GIS recipients. When a single recipient has other income of $17,784 or more (2018) all their GIS is clawed back.

If either spouses or common-law partners in a couple are both receiving the Old Age Security pension, the maximum monthly supplement of each pensioner is reduced by $1 for every $4 of their combined other monthly income.

There is one exception to these two basic rates - for a couple in which only one spouse or common-law partner is a pensioner and the other is not in receipt of either the basic Old Age Security pension or the Allowance. In this case, the pensioner can receive the Guaranteed Income Supplement at the higher rate paid to those who are single.

The GIS stops being paid to a couple in this situation when net income exceeds $42,624 (2018).

Service Canada says as of June 2017, 1.94 million seniors were receiving the GIS, roughly a third of the country’s 5.93 million OAS pensioners.
GIS Eligibility

You qualify for the GIS if you meet all the following conditions:

- you are receiving an Old Age Security pension; and
- your annual income (or in the case of a couple, your combined income) is lower than the maximum annual threshold.

Using your income information from your federal Income Tax and Benefit Return, we will review your eligibility for the GIS every year. If you still qualify, your benefit will be automatically renewed. In July, you will receive a letter telling you:

- that your benefit will be renewed;
- that your benefit will be stopped; or
- that your income information is required.

GIS Sources of income and deductions

When applying for the Guaranteed Income Supplement and the Allowance, you, or in the case of a couple you and your spouse or common-law partner, must report your income and deductions. Use the information slips issued to you for income tax purposes, as well as your federal Income Tax and Benefit Return, to report the following income and deductions:

- Canada Pension Plan (CPP) or Quebec Pension Plan (QPP) benefits;
- other pension income, such as private pensions, superannuation and foreign pension income;
- Registered Retirement Savings Plans (RRSPs) that you cashed during the year;
- Employment Insurance benefits;
- interest and other investment income;
- capital gains and taxable Canadian dividends;
- net income from any rental properties;
- net employment income minus the following deductions:
  - your CPP or QPP contributions, your Employment Insurance premiums and the $3,500 earnings exemption;
- net self-employment income minus the following deductions:
  - your CPP or QPP contributions on self-employment and your Employment Insurance premiums;
- other income from sources such as workers’ compensation payments and alimony; and
- other deductions, such as union dues, RRSP deduction, moving expenses and other employment expenses.
You were selected for automatic enrolment for the Old Age Security pension and the Guaranteed Income Supplement

If you were automatically enrolled for the OAS pension, you will be automatically enrolled for the GIS if you are eligible. If so, you will be considered for the GIS on an annual basis, without needing to apply. If you can be automatically enrolled, Service Canada will send you a notification letter the month after you turn 64.

If you did not receive a letter from Service Canada informing you that you were selected for automatic enrolment, you must apply in writing for the GIS. An application kit will be sent to you automatically.

How to delay receipt of the GIS

You may decline automatic enrolment for the GIS by:

- accessing your My Service Canada account and following the directions;
  or
- signing and returning the automatic enrolment letter by mail.

Sponsored immigrants

If you are a sponsored immigrant and you have resided in Canada less than 10 years after age 18, you are not eligible to receive an OAS income-tested benefit (the GIS, the Allowance or the Allowance for the Survivor) during your sponsorship period unless your sponsor:

- suffers personal bankruptcy;
- is imprisoned for more than six months;
- is convicted of abusing you; or
- dies.

Non-sponsored immigrants

If you are a non-sponsored immigrant, you may be eligible to receive the GIS based on the number of years you have resided in Canada after age 18.

If you have lived in Canada for fewer than 10 years since you turned 18, but you have lived or worked in a country that has a social security agreement with Canada, you may be eligible for a partial benefit. Your GIS entitlement will gradually increase with every year that you continue to reside in Canada until you have reached 10 years of residence.
How do you apply for the GIS?

In December 2017, Service Canada implemented a process to automatically enroll seniors who are eligible to receive the GIS. If you can be automatically enrolled, Service Canada will send you a notification letter the month after you turn 64. If you did not receive a letter from Service Canada informing you that you were selected for automatic enrolment, you must apply in writing for the GIS; however, you must first apply for OAS.

You must apply in writing for the GIS. Complete and mail the Application for the Guaranteed Income Supplement (ISP-3025) for the payment year that applies to you and include certified true copies of the required documentation. You will find this form on the Old Age Security forms page.

Spouses Allowance

A means test is done to determine whether this benefit will be available to the pensioner. If qualified, it is available to people between the ages of 60 – 65. The normal residence requirements must be met.

This benefit is available for couples living on a single OAS Pension. The income ceases at death, divorce or separation. It also stops when the pensioner attains the age of 65. This benefit is non-taxable to the recipient.

Spouses Allowance Exception

A sponsored spouse or common-law partner of an Old Age Security pensioner or a survivor between the ages of 60 and 64 with less than 10 years of residence in Canada after reaching age 18 is not eligible for the Allowance benefit for the period of his or her sponsorship, up to a maximum of 10 years, unless he or she:

1. Was receiving a pension in March 1996 or before; or

2. Was residing in Canada or had resided in Canada as a Canadian citizen or permanent resident before March 7, 1996 and will receive a pension in January 2001 or before.

The Allowance is an income-tested benefit. The maximum amount payable to the spouse or common-law partner of a pensioner is equal to the combined full Old Age Security pension and the maximum Guaranteed Income Supplement at the married rate. The maximum amount for a person whose spouse or common-law partner has died is somewhat higher.
Taxation

Except for the GIS and the Spouse’s Allowance, CPP & OAS benefits are considered taxable income under the Income Tax Act.

PRIVATE SECTOR INCOME SOURCES

REGISTERED RETIREMENT SAVINGS PLANS (RRSP’s)

Since RRSPs were introduced in 1957, they have become one of the most popular ways for Canadians to save for their retirement and defer taxes.

Your prospects and clients can contribute, from earned income, within certain limits to a registered retirement vehicle from an approved source. When this happens, you reduce your taxable income when filing income tax returns. Tax on the investment income earned in the plan is postponed until you withdraw the income, this usually begins at retirement. This income is taxed at personal income tax rates along with Pension Income from all other sources. Some of these sources may be RPP, DPSP, RCA, CPP and OAS to name a few.

A person between the ages of 18 and 71 is eligible to contribute to RRSP’s. The contribution must be made within 60 days following December 31st of the previous year.

Where can you get RRSPs from?

The Canada Revenue Agency allows all RRSPs that are issued by Trust Companies, Banks, Life Insurance Companies, Credit Unions, Investment and or Mutual Fund Companies to be eligible when setting up RRSPs.

Yearly contribution limit

Your right to make an RRSP contribution for one year depends on your earned income for the previous year. For 2018, your contribution will be limited to 18% of your 2017 earned income, to a maximum of $26,230. Therefore, you need at least $145,722 of earned income in 2017 to maximize your 2018 contribution. This limit is further reduced by your pension adjustment for 2017.

In general terms, earned income is income you receive from employment, business or the rental of real property, as well as any alimony and taxable maintenance. It is reduced by business or rental losses and any alimony and maintenance payments made.
If you have some control over your income level, make sure that you have factored in the ability to make RRSP contributions into your decision of whether to earn a salary rather than dividends.

Pension Adjustments (PA)

A PA is the total amount of contributions made to an employer sponsored pension plan, (Defined Benefit, Money Purchase or Deferred Profit Sharing plans), on your behalf by your Employer (s) in the preceding year in accordance with the terms of your Collective Agreement.

In laymen’s terms, the PA. represents value of benefits accrued during the years for an employee enrolled in any of the above-mentioned pension plans regardless of whether the employer or employee or both contributed. The PA. is reported to CRA and the Employee on the T-4 slip. The PA. reduces the Employee's Contribution Limit.

Deduction Carry Forward

Any portion of contribution limit not used in prior years can be carried forward indefinitely. This replaces the old rule, which limited the carry forward to a period of seven years.

In general terms, an individual’s unused RRSP deduction room available at the end of a year is the difference between the RRSP deduction limit for the year less the deductible contributions made in respect of the year. This will allow an individual to catch up on contributions to which the individual was entitled in a year but was unable to make for some reason, such as not having the cash.

What constitutes earned income?

Earned income generally includes salaries, commissions, royalties, net rental and business incomes less losses, alimony or maintenance benefits, taxable benefits, supplemental EI benefits, net research grants, CPP & other taxable Disability income.

From earned income, there are certain reductions that will decrease the earned income total. These are interest earnings, dividends, union dues, and professional membership fees.
Alimony or maintenance payments made by the taxpayer that are deductible for tax purposes will reduce earned income for RRSP purposes. Periodic pension payments and retiring allowances no longer qualify as earned income as well.

Yearly RRSP contribution levels

<table>
<thead>
<tr>
<th>Year</th>
<th>RRSP Limit</th>
<th>Maximum Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>$22,000</td>
<td>$122,222</td>
</tr>
<tr>
<td>2011</td>
<td>$22,450</td>
<td>$124,722</td>
</tr>
<tr>
<td>2012</td>
<td>$22,970</td>
<td>$127,611</td>
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<td>$147,222</td>
</tr>
<tr>
<td>2020</td>
<td>TBD</td>
<td>TBD</td>
</tr>
</tbody>
</table>

Maximizing your contribution

If you are making an RRSP contribution it may make sense to borrow to increase the amount you are putting in your RRSP and then use the tax refund on your total RRSP contribution to pay back the loan. Make sure that your total RRSP contribution is within your maximum contribution limit.

For example, let’s say you have $3,200 in available cash and your tax rate is 30%.

Divide $3,200 by 1 less your marginal tax rate.  - $3,200 / (1-30%) = $4,571

Your total contribution would be $4,571 based on borrowing $1,371 which is what you’d receive from your tax refund ($4,571 X 30% tax rate) and you could use it to repay the loan (assuming you are eligible for a tax refund and no other factors affect the amount of your refund).
RRSP Over-contributions

Currently, individuals who were at least 18 years of age in the preceding year can over-contribute to their RRSPs by up to $2,000 without incurring the monthly 1% penalty tax. You cannot claim a tax deduction for the over contribution in the taxation year it is made but you can wait until new RRSP contribution room is available in a future year and deduct the over contribution in that year.

The $2000 figure is designed to help those people who may have miscalculated their pension adjustment and contributed a little too much.

Using the new over contribution rules to the client’s advantage

If you are already contributing your allowable maximum, it still pays to over contribute the $2,000. It does not matter if you do this deliberately or by mistake. If it is no more than $2,000, there are no penalties, and that money can compound tax-free inside your plan.

Nowadays, many people in retirement still have earned income. This income may be earned through a professional practice, consulting contract, or a small business, and don’t forget that directors’ fees and net rental income also qualify as earned income.

If you have earned income for RRSP purposes, you can contribute to your own RRSP any time before the end of the year you reach age 71 (if you turn age 71 in 2012, you can contribute to your RRSP until December 31, 2012).

After your deadline for RRSP maturity options, you can also still make eligible RRSP contributions to a spousal RRSP if your spouse is under age 71.

What you might not realize is that even though you cannot make RRSP contributions to your own RRSP after your RRSP maturity option deadline, you can make an RRSP over contribution before your RRSP maturity deadline (think of it as contributing in advance). Keep in mind that any over contributions more than $2,000 are subject to a penalty of one per cent per month.

If you will have earned income after age 71, you may wish to consider the following:

- Making the $2,000 over contribution before your RRSP maturity option deadline (there would be no one per cent penalty to worry about). You could then claim a $2,000 deduction against earned income in later years.
• Over contributing beyond the $2,000 limit. The penalty is applied at the end of each month; therefore, if you over contributed on December 1st of the year you turned 71, you should only have one month's penalty.

With some active planning, it is possible to generate earned income during your clients’ retirement years.

**Taxpayers with the following attributes may wish to take advantage of the new rules for RRSP over-contributions:**

• A person who has a sophisticated knowledge of the tax rules.
• A person with excess cash flow.
• A person who has a high marginal tax bracket.
• A person who may have the expectation of RRSP deduction room in future years.

Taxpayers should be encouraged to discuss this strategy with their tax advisors before making an over-contribution.

The ability to use an over-contribution in an RRSP, as a deduction in a subsequent year is limited to RRSP deduction room based on earned income.

**Advantages of over-contributing to an RRSP**

• Tax-sheltered growth on RRSP funds, including the excess contribution.
• Can be used to fund future contributions, providing a hedge against future cash flow problems.

**Disadvantages of over-contributing to an RRSP**

• Over-contribution is taxable when withdrawn even if it is never used as a deduction (for example, emergency cash need or death of the annuitant).
• One per cent penalty tax per month will apply to any amount of excess contribution exceeding the $2,000 cumulative balance.

**Borrowing to Make an RRSP Contribution**

How much can you afford to put into your RRSP? Does it make sense to borrow to increase your contribution? There are two key factors to consider when deciding whether to borrow to deposit in an RRSP: how badly you need the tax break and how quickly you can afford to repay the loan.
When to borrow for your RRSP

Consider borrowing when you haven’t set anything aside for your RRSP or you want to increase your RRSP contribution. Either way most financial advisors will suggest that you borrow to make your RRSP contribution. Contributing is a sure way to reduce your taxable income as well as providing for your retirement. Borrowing to make all or part of your RRSP contribution makes sense when the return on your RRSP outweighs the interest cost of borrowing, or if you are eligible for a tax refund.

Example of Borrowing for an RRSP

Let’s say you borrow $3,000 at 8% and pay it back over 12 months. Your total interest cost is $131.64 (assuming the loan is repaid in 12 equal monthly installments of $260.97 with interest calculated monthly on a declining balance). If you invest your $3,000 in an RRSP earning 6% compounded annually, the total earnings are $180 in the first year. So, you’re ahead by $48.36. Plus, by making your RRSP contribution, you may receive a tax refund. For example, if you’re in a 35% marginal tax rate, you may receive a tax refund of $1,050 on a $3,000 contribution. You can then pay down your loan more quickly or you could even re-invest your refund in your RRSP for next year.

Spousal RRSP contributions

An individual may contribute to an RRSP of which he or she is beneficiary and/or to a spousal plan. The spousal plan provides a means of splitting retirement income between spouses.

However, if an amount is withdrawn from a spousal RRSP within two years from the year in which the last contribution was made, the withdrawal will be taxed in the hands of the contributing taxpayer.

A spousal RRSP may also be advantageous where the spouse is younger, since a longer accumulation period will be available.

It should be noted that a taxpayer’s ability to contribute to a spousal RRSP will not be reduced if the spouse has earned income and has contributed to his or her own RRSP. The receiving spouse is the applicant, owner and annuitant and signs the request for registration. The tax deductions certificate issued may or may not include the spouse contributor’s name but can be used by them regardless.
RRSP Beneficiaries

Choosing the right RRSP beneficiary can benefit your estate. In most provinces, you can designate a beneficiary on your RRSP – and most people automatically designate their spouse.

There are major advantages to designating an RRSP beneficiary:

- Without a beneficiary designation, up to 48% of your total RRSP value could be lost to taxes.
- In most provinces, your assets immediately become the beneficiary’s property, so they are available sooner than if the assets were left to your estate.
- RRSP assets do not form part of your estate and, therefore, do not attract probate fees (except in Quebec).
- And, if your beneficiary is your spouse (or a disabled dependent child or grandchild) your RRSP is transferred on a tax-deferred basis to your beneficiary’s registered plan.

RRSPs held with life insurance companies have usually been thought to be inaccessible to creditors, if a spouse or dependent is named beneficiary of the plan. However, recent court decisions may affect this result in certain circumstances. Professional advice should be sought if you are uncertain about the creditor proofing of your client / prospects RRSP.

Your clients / prospects should still consider making their spouse the beneficiary who will receive the proceeds of an RRSP in the event of the person’s death prior to the maturity of the plan. If there is no spouse, then a dependent child or grandchild should be named.

If any other beneficiary is named, the fair market value of the RRSP is included in the deceased taxpayer’s income in the year of death. Where the spouse is named, the fair market value of the plan is included in the spouse’s income in the year of death, but the spouse may usually contribute to an RRSP or RRIF for the equivalent amount and claim a deduction, therefore deferring the tax until later.

If a dependent child or grandchild is named as beneficiary, the fair market value of the RRSP will be included in the child’s income rather than that in that of the deceased in the year of death.
Where the dependent child is under eighteen years of age and in the same year the RRSP is included in income, or within 60 days after the end of the year an annuity is purchased for a fixed number of years not exceeding 18 minus his or her age at the time the annuity is acquired, a deduction is available to the child equal to the amount of the RRSP included in income.

If the individual is dependent on the deceased by reason of physical or mental disability, the fair market value of the RRSP will be included in the dependents income rather than in the deceased’s income in the year of death.

**RRSP Funds – Should They Form Part of the Estate?**

Another frequent question is whether RRSP funds form part of the estate assets or whether they go directly to the beneficiary.

If your RRSP was issued by an insurance company, the Insurance Act provides that the funds go directly to the beneficiary and do not form part of the estate assets.

Conversely, if the RRSP was issued by a financial institution other than an insurance company, then the funds will form part of the estate. The estate will be responsible for paying the taxes on the plan, notwithstanding that the benefits may be paid directly to a beneficiary named in the plan.

Revenue Canada takes the position that the person who receives the benefit is jointly liable with the estate for the payment of the tax. Unless there is some direction in the Will, the estate will have no claim against the designated beneficiary for the taxes paid out of the estate. Also, the RRSP trustee is not required to withhold part of the RRSP proceeds to meet potential tax liability.

The Testator of a Will can state in the Will that the taxes payable on a RRSP are to be paid from the proceeds of the plan and that the beneficiary receives the net proceeds. If there is no express direction in the Will, the tax liability is paid from the residue of the estate first and if the residue is insufficient to cover the tax, then the tax will be taken from the RRSP proceeds, leaving a beneficiary of the RRSP with net proceeds.

Your client’s RRSP is an important part of their overall retirement and estate plan. To be sure that they make the right choices that keep their RRSP on track for their benefit, and to maximize any legacy to their heirs’ means seeking the advice of a professional financial advisor to help them work through all the RRSP mazes.
Registered Life Insurance plans

Dividends from Registered Life Insurance Policies may not be used as a contribution. These plans like other life insurance plans cannot be used for collateral assignment. If payments cease before maturity, the plan will remain a registered reduced paid up policy. Should the plan be de-registered and or a partial withdrawal is taken, the proceeds are fully taxable in the current year.

Throughout the past few years, registered life insurance plans have had a difference of opinion with Financial Planners and the public. This is partly because the portion of the premium being used to pay the protection element is not deductible, but the remaining premium can be deducted. The non-deductible portion includes the costs of Life Insurance and riders.

RETIRING ALLOWANCE TRANSFERS

Retiring allowances and RRSPs

Individuals who receive an amount from their former employers upon dismissal or retirement in 2018 may be eligible to contribute an extra amount to their RRSP or RPP.

The maximum amount that can be transferred to your RRSP or RPP is $2,000 multiplied by the number of years you worked for your employer before 1996. You can also add in $1,500 multiplied by the number of years you were employed prior to 1989 in which your employer did not make vested contributions to a registered plan on your behalf. The contribution, which is in addition to your regular contribution limit, must be made to your own retirement plan, not your spouse’s.

A retiring allowance is defined to include an amount received in respect of a loss of an office or employment. Revenue Canada has said that any payments received by a terminated individual, which represent payments in lieu of notice, do not qualify as a retiring allowance.

WHAT DO I DO WITH MY REGISTERED FUNDS NOW THAT I AM AGE 71?

Okay, so now your clients and prospects are now age 71. This is a significant age, because it is now time to do something with their RRSP’s that they have been saving for years. How they decide to take the income is very crucial at this stage.
Many questions should be addressed before a decision is made to take income. Some of those may be:

- What age am I?
- What age is my spouse?
- How is our health?
- How much is my company pension?
- How much is my spouse’s pension?
- Do I take CPP at age 60 or 65?
- Will my spouse get CPP?
- Is it imperative that I leave an estate?
- What are my living expenses?
- Do I need more money now? Less later?

I’m sure that you can probably think of many more questions that should be asked to make sure that your clients / prospects are on the right track to a long and prosperous retirement.

A few short years ago, RRSP funds had to be deposited into a Life Annuity, Term Certain or a Registered Retirement Income Fund (RRIF).

Over the last few years, a new generation of RRSP variations has provided several attractive alternatives.

At a time when Canadians are healthier in retirement and are, in fact living longer than ever before, it is important that their incomes are every bit as healthy as they are and last just as long.

An increasing number of people are living beyond age 90. Below are some figures from the Canadian Institute of Actuaries that illustrates the probability of living beyond age 90 at various current ages.

<table>
<thead>
<tr>
<th>Present Age</th>
<th>Probability of surviving beyond age 90</th>
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<tr>
<td></td>
<td>Males</td>
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<tr>
<td>60</td>
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<td>75</td>
<td>34 in 100</td>
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<td>80</td>
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</table>
The previous table illustrates that one-third of all males and almost one-half of all females retiring today can expect to live beyond age 90.

Most people find that an annuity, RRIF, or a combination will best meet their retirement income needs. The choice, however, depends upon individual needs.

Let's look at a few more retirement income alternatives.

**ANNUITIES**

An annuity is a contract purchased with a lump sum of money *TODAY* in return for regular payments of this money (plus the interest earned) in the *FUTURE*. It provides a continuing and guaranteed income.

**Types of annuities**

Although there are many variations of annuities, most fall into two categories:

1. **Annuities (Term) Certain**

These types of annuities provide income payments for a specific guaranteed period, such as income for 10 or 15 years, or until the buyer reaches a specific age.

They are always based on only one annuitant. The payments are guaranteed for a specific number of installments.

When RRSP funds are used, the annuity must run until age 90 (or the annuitant may take a term certain which runs to their spouse’s age 90, if the spouse is younger). Once the period expires, the contract terminates.

**Example**

A 10-year annuity certain is finished after 10 years, even if the annuitant is still alive and in need of continuing income. If the annuitant dies before the end of the certain period, the annuitant’s estate or named beneficiary is entitled to the rest of the payments.
2. **Life Annuities**

These types of annuities can be set up with or without a guarantee period. They provide income payments for the annuitant’s lifetime. There can be single life annuities, which make annuity payments to the annuitant only during his or her lifetime. There can also be joint and last survivor annuities.

These types of annuities make payments to one annuitant until he or she dies and then to the spouse.

There can be a guaranteed period of any length (only age 90 for registered funds are allowed).

At death, the annuitant’s estate, unless a beneficiary has been named, will receive the remainder of the payments during the guaranteed period should the annuitant die during that period. If RRSP funds are used, and the annuitant dies, any remaining guaranteed payments must be commuted, unless the beneficiary is the spouse.

Although we have described only a couple of different annuities, many more are available to suit your clients and prospects.

**Many other variations of annuities**

- Life annuity with no guarantees
- Life annuity with a guarantee
- Increasing life annuity
- Joint and last survivor annuity with no guaranteed period (full income to survivor)
- Joint and last survivor annuity with a guaranteed period
- Joint and last survivor with income reducing
- Increasing joint and last survivor annuity
- Integrated annuity
- Impaired annuity
- Commutable annuities

Life annuities and annuities certain can be either *immediate or deferred* payments. With immediate annuities, the income payments to the individual usually will start exactly one installment period after the institution receives the funds. With a deferred annuity, the income commences more than one installment frequency after the funds are received. Usually, this commencement date is several years in the future.
Deferred annuities are usually for non-registered funds. For registered funds, Revenue Canada says that the individual must receive one entire year of payments in the year they reach age 72.

**How are annuities taxed?**

**While Living**

When we are dealing with registered funds, the total of the payments received in any given year must be included as income in the year received.

**At Death**

Where the annuity is joint and last survivor, or the spouse is the named beneficiary, the guaranteed annuity payments will continue to be paid to the spouse and will be taxed as received. Otherwise if the commuted value of any remaining guaranteed annuity payments exceeds the dependents allowable limits, it will be taxed on the final return of the deceased annuitant.

**Some key points to remember about annuities**

When determining life annuity incomes, several factors are considered: Interest, mortality and expense rates, the annuity option selected, the amount of the funds, and when the first payment starts. Annuity certain annuities are influenced by the same factors, except for mortality rates.

A single annuity with no guarantee usually offers the highest monthly income. However, if annuitants die shortly after purchasing this plan, no benefits are available to their estates. A longer guarantee period or the addition of a joint and last survivor option will lower the monthly income, but also provide more assurance of income for the surviving spouse or estate.

Your client’s age, health, lifestyle, income needs and the needs of their spouse and dependents should all be considered in recommending an annuity option. Asking a few disturbing questions in consideration of these important points will earn your client’s respect and result in sales for you.

Clients should consider an annuity if they want the security of knowing exactly what their income will be for the full term. If they do not want to make any more investment decisions and want to lock in current interest rates, then this is the best option for them.
**REGISTERED RETIREMENT INCOME FUNDS (RRIF)**

A RRIF provides a retiree with a means of converting RRSP savings into a flexible and secure retirement benefit.

RRIFs work like a continuation of your RRSP, with the same tax sheltering advantages. You can continue to hold GICs, stocks, bonds and mutual funds within your RRIF and have the income, interest and capital gains protected from tax. The major difference between an RRSP and a RRIF is that you can no longer make yearly contributions to your RRIF, and you must withdraw a minimum amount from your RRIF each year as taxable income.

**Here are some features of RRIFs that make them very attractive as investment and retirement vehicles:**

**Control**

The types of investments held within the plan are up to you. You are still in charge of your investment decisions. You control the asset mix - the selection of individual investments - of your RRIF just as you did with your RRSP.

**Flexibility**

You can choose a RRIF now and an annuity later, if you require other forms of income.

**Benefits**

Your spouse and other beneficiaries can receive the remainder of your RRIF after your death.

**Protection**

Because a RRIF is an investment instrument that allows for continuing growth, it can provide protection against the erosion of your estate as you draw on the funds as a retirement benefit. Unlike an annuity, which provides a fixed benefit, your investments continue to work for you while held in a RRIF account.
Generally, the following rules apply:

RRIFs may be established at any time before the end of the year in which the individual reaches the age of 71. A RRIF is an excellent means of financing an early retirement. You can have multiple RRIFs if desired, allowing diversification of an individual's RRIF portfolio.

RRIF funds may be invested in the same types of investments as RRSPs. The RRIFs may be self-administered. That is, an individual may personally determine, along with the trustees of the RRIF, what investments to make. As with an RRSP, an RRIF is not taxed on its earnings. Thus, income accumulates on a tax-free basis in the RRIF.

A minimum amount must be withdrawn each year, although any amount more than the minimum is allowed, offering further flexibility in being able to meet unforeseen expenses or financial emergencies. Amounts withdrawn from an RRIF more than the minimum amount, however, will be subject to withholding tax at the same rates that are applicable to RRSP lump-sum withdrawals.

In the first year of the RRIF, the individual need not withdraw any amount.

**RRIFs qualify for the $2000 pension income credit.**

If you are over the age of 65 and you do not have a company pension plan, you may be able to withdraw $2000 per year of income from the RRIF tax-free.

Subsequently, the minimum amount must be withdrawn in either a lump sum or periodic payments. The minimum amounts to be withdrawn are determined by the fund holder’s age. An individual may elect, at the commencement of the RRIF, to have the minimum amount determined by the age of a younger spouse (including common-law), thereby lowering the minimum and in effect extending the useful life of the RRIF. This election does not make the spouse or common-law spouse necessarily the beneficiary of the RRIF after the individual’s death.

**What is the minimum annual withdrawal from a RRIF?**

There is no withdrawal necessary in the year a RRIF (Registered Retirement Income Fund) is set up, but there are minimum amounts that must be withdrawn annually starting in the year after setup.
Unless certain types of annuities are held in the RRIF, the minimum withdrawal amount is calculated by multiplying the market value of the RRIF holdings at the beginning of the year by a "prescribed factor".

Under the old rules, if the RRIF was started before 1993, then it is a "qualifying RRIF", if no new property was transferred into the RRIF after 1992, other than from another qualifying RRIF. The prescribed factor for the qualifying RRIF is $1/ (90\text{-age})$ while the annuitant (owner) of the RRIF is under 79 years old.

Under the old rules if the RRIF was started after 1992, the prescribed factor is $1/ (90\text{-age})$, but only while the annuitant (owner) is under 71 years old. Age is referred to as the age of the annuitant at the beginning of the year.

**THE 2015 FEDERAL BUDGET MODIFIES RRIF MINIMUM WITHDRAWALS**

On April 21, 2015, the Federal Government released its 2015 Economic Action Plan (the "Budget"). The Budget includes several announcements relating to retirement and benefit plans.

The minimum withdrawal from a RRIF has been reduced for ages 71 to 94. An individual is required to make RRIF withdrawals commencing in the year following the year in which the RRIF was established. Individuals are generally required to transfer Registered Retirement Savings Plan (RRSP) funds into an RRIF by the end of the year in which they turn age 71.

An individual’s minimum withdrawal from an RRIF is calculated by multiplying the market value of the RRIF holdings at the beginning of the year by a “prescribed factor”. This prescribed factor will be updated commencing in 2015.

The existing RRIF factors were determined based on providing a regular stream of payments from age 71 to 100 assuming a seven per cent nominal rate of return on RRIF assets and indexing at one per cent annually. Budget 2015 proposes to adjust the RRIF minimum withdrawal factors that apply in respect of ages 71 to 94, based on a five per cent nominal rate of return and two per cent indexing. These assumptions are more consistent with long-term historical real rates of return on a portfolio of investments and expected inflation.

The new RRIF factors will range from 5.28 per cent at age 71 to 18.79 per cent at age 94. The percentage that seniors will be required to withdraw from their RRIF will remain capped at 20 per cent at age 95 and above.
These updated minimum withdrawals would also affect life income funds (LIFs) established using funds transferred from registered pension plans and locked-in retirement accounts. The maximum withdrawals for such products are set out in pension legislation and are unaffected by the change. Similar rules will apply to those receiving annual payments from a variable payment account in a defined contribution RPP or a PRPP (Pooled Registered Pension Plan).

The new RRIF "prescribed factors" will apply for the 2015 and subsequent taxation years to allow you to preserve more of your RRIF savings to provide income at older years.

The annuitant can elect to use the age of their spouse or common-law partner in calculating the prescribed factor, for both qualifying and non-qualifying RRIFs.

**Post 2015 RRIF Withdrawal Changes**

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What happens to a RRIF at death?

The general rule for a RRIF is that the value of the RRIF at the date of death is included in the income of the deceased for the tax return for the year of death.

However, income tax may be deferred if the beneficiary of the RRIF or estate is:

1. The spouse or common-law partner
2. A financially dependent child or grandchild under 18 years of age, or
3. Financially dependent mentally or physically infirm child or grandchild of any age.

For the tax to be deferred, the RRIF must be transferred to the RRSP, RRIF, or eligible annuity of the beneficiary before December 31st of the year following the year of death. Other conditions also apply.

RRIF Transfers

Your clients and prospects can transfer additional RRSP funds to an existing RRIF until they reach age 71. Funds can be transferred from one RRIF to another RRIF at any age. In addition, RRIFs can be transferred from one company to another (there may be a penalty or charges applied by the company losing the funds). As well, clients can transfer funds from registered commutable annuities to RRIFs.

Who should consider buying RRIFs?

Your clients and prospects should consider a RRIF if they want control over their money and how the funds are invested. They offer an attractive alternative to clients who either does not want to invest their retirement savings in “traditional” annuity products. They may already own an annuity and want to supplement their annuity income with a flexible, inflation-sensitive program.

They may want to achieve some investment growth. Most institutions provide a wide variety of options and competitive returns. You should be prepared to present your clients with a customized plan designed to fit their personal retirement needs.

Your clients may want maximum tax deferral. RRIFs can provide lump sum payout, enabling your clients to change their retirement income from year to year as their need change. RRIFs can be collapsed at any time and transferred to an annuity, another RRIF or withdrawn in cash.
Finally, if your clients and prospects are concerned about leaving an estate, the RRIF option is the best way to achieve the flow of tax – free money to the named beneficiary.

**LOCKED-IN RETIREMENT ACCOUNTS (LIRAs)**

A Locked-In Retirement Account (LIRA), sometimes called a locked-in RRSP, contains accumulated pension benefits transferred out of a workplace pension plan. It is subject to the rules and regulations governed by the pension regulatory authorities at federal and provincial levels. If the funds in your LIRA come from a pension plan in Ontario, for example, it will be subject to Ontario’s pension regulations.

If your workplace pension plan fell under federal jurisdiction – as it would if your worked for a bank, communications or transportation company, for instance – you would own LRSP that is subject to federal pension regulations.

Generally speaking, funds in a LIRA may be invested in the same way as an RRSP – although some provinces do not allow a LIRA to contain the holder’s mortgage. The financial institutions holding your LIRA should be able to give you information about this if you need it. Like an RRSP, a LIRA must be converted to a stream of income by the end of the year in which the holder reaches age 71.

Most pension regulators do not allow a LIRA to mature until you are within 10 years of the normal retirement age provided in the pension plan form which the funds. That’s generally age 55. However, your options when your LIRA reaches maturity are limited. You may convert your LIRA to an annuity or to a Life Income Fund (discussed later in chapter).

In some provinces, you also have the option of converting a LIRA to a Locked-In Retirement Income Fund (LRIF). You may not cash in your plan or take out a lump sum (some exceptions apply).

**LIRAs at a Glance**

**Objective**
To maintain tax-deferred savings of lump sum transfers from an employer-sponsored pension plan.
Suitability

Customers choosing to receive and control the lump sum, commuted value of their pension rather than a monthly pension amount.

Features

- Tax-Deferred Income earned in the plan accumulates tax-deferred as long as it remains in the plan.
- Generally, no withdrawals are permitted from a LIRA.
- Exceptions are made based on various provincial rules. It must be converted to a LIF, LRIF or annuity to withdraw from the plan.
- LIRAs are governed by different provincial legislations.

LIFE INCOME FUND (LIF) AND LOCKED-IN RETIREMENT INCOME FUND (LRIF)

If you left a job where you had a pension plan, you may have transferred your pension entitlement to a locked-in retirement account (LIRA) or locked-in RRSP, where it has been invested according to your directions. Typically, that money cannot be withdrawn until you start retirement.

After a minimum age (set by your province) you can start to receive income from this pension money by converting it into a LIF or LRIF/RLIF or buying a life annuity. (Depending on your province, you may have a choice between the 2 types of accounts. As well, there may be different rules affecting these accounts.)

In many ways a LIF/LRIF/RLIF works like a LIRA or locked-in RRSP in reverse: Instead of putting money in, you take an income out.

LIF Payments – Minimums and Maximums

Some information on the new rates effective January 1, 2018

Financial institutions are required to calculate a client's maximum income each year from Life Income Funds (LIFs) and Restricted Life Income Funds (RLIFs) based on the client’s age on January 1 and the CANSIM rate percentage factors.

The CANSIM rate is set monthly by the Government of Canada based on that month’s average rate for long-term Government of Canada bonds. The formula used to calculate maximum payments is based on the previous year's November 30th CANSIM rate.
All jurisdictions, except for the Federal Pension Benefits Standards Act (PBSA), default to a minimum 6% CANSIM rate if the rate falls below that amount. Federal maximums are calculated using the actual CANSIM rate, no matter how low it falls.

The maximum withdrawal limits for federal LIFs in 2018 have been set using the following long-term interest rate assumptions:

- 2.16% for the first 15 years, and
- 6.00% for the years remaining to the end of the year in which the LIF owner attains 90 years of age

LOCKED-IN RETIREMENT INCOME FUNDS (LRIF)

Locked-in retirement income funds (LRIFs) pay out the accumulated value of locked-in RSPs, LIRAs or RPPs.

LRIFs, like LIFs, have minimum and maximum payout levels. The LRIF minimums are established under Canada Revenue Agency rules. The maximums are dictated by provincial rules.

Unlike LIFs, your LRIF assets don’t have to be converted to an annuity when you turn 80. Instead you can hold your existing LRIF investments and manage them for the rest of your life.

LRIFs are offered only in:

- Alberta
- Manitoba
- Newfoundland and Labrador
- Ontario

Other provinces are expected to offer LRIFs in the near future as an alternative to a LIF.

Locked-in retirement income funds are investment instruments used to hold and pay out pension funds upon retirement. Funds cannot be cashed out in one lump sum because the money is meant to last you for the rest of your life. LRIFs are like LIFs but don’t require individuals to purchase a life annuity when they turn 80. Under the LRIF, there is no age limit for the termination of the fund.
Like a LIF, there are minimum and maximum withdrawal rates. Talk with your financial specialist about the withdrawal rates. They vary according to investment income and market value.

LRIFs are considered the most volatile investment option, because the amount that can be taken any year will change depending on investment earnings during the previous year.

*Be cautious with financial institutions that offer more flexible LRIF options, for example:*

**Variable-Rate LRIF**

Your interest rate varies with changing marketplace conditions.

**Fixed-Rate LRIF**

Earn a fixed rate of interest for the time you select.

**Which financial institutions carry LRIFs?**

To convert a RRSP or pension plan to an LRIF, your financial institution or financial advisor will go over the details, which vary from province to province.

**Make sure the following questions are discussed with the client:**

1. How much do you want your minimum and maximum withdrawal to be?
2. Do you want to access the money in case of an emergency?
3. Where do you want the money to go when you die?
4. Are any of your other funds considered?

If the client is thinking of converting a RRSP or pension plan into a LRIF, most institutions don’t charge for the transfer. Management fees vary with most while some companies waive all management fees. Some will even pay for the transfer of funds from one company to another.

**LIF/LRIF Withdrawal Limits for 2018**

A Life Income Fund (LIF) is a type of Registered Retirement Income Fund (RRIF) established under the Income Tax Act (Canada), with the added provincial or federal pension act requirements associated with pension funds.
As a result, the *minimum annual withdrawals* from an LIF are the same as for an RRIF, but the pension legislation dictates that a maximum annual withdrawal limit be set according to the governing provincial or federal pension legislation.

### 2018 LIF/LRIF Minimum/Maximum Withdrawal Percentages

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Please note for the above chart - Quebec, Alberta, Manitoba, New Brunswick & British Columbia pension legislation permits LIF clients who begin a LIF in the middle of a calendar year with funds transferred from a LIRA or pension plan to take the FULL maximum payment for the year. First year payments under the other jurisdictions must be prorated based on the number of months the LIF was in force.

- For Ontario New LIF, Ontario Old LIF, Ontario LRIF maximum calculation is based on the greater of a) the result using the factor and b) the previous year’s investment returns.
- For Saskatchewan and Newfoundland LIFs must be converted to a life annuity at age 80.
- For British Columbia LIF maximum calculation is the greater of 1) the result using the applied factors and 2) the previous year’s investment returns under the same LIF contract.
- For Alberta LIF maximum calculation is based on the greater of 1) the result using the new factors or 2) the previous year’s investment returns.
For Manitoba LIF maximum calculation is based on the greater of a) the result using the factor and b) the previous year’s investment returns + 6% of the value of all transfers in from a LIRA or Pension Plan during the current year.

Two major differences between a LIF and a RRIF are:

1. Although both require a minimum payment amount be withdrawn out of the plan each year, the LRIF imposes a maximum annual withdrawal.

2. With a RRIF, you control the investments during your entire lifetime. With a LRIF (except in Quebec) you must purchase an immediate life annuity, which must include a 60% spousal survivor benefit, unless the spouse waives this requirement, by the end of the calendar year of your 80th birthday.

How will a LIF/LRIF/RLIF fit into the overall financial plan?

1. **You control your investments** - Your money can be invested in many ways, so it keeps growing and working for you.

2. **You have some control over your income** - While there is a variety of income payment options available, there is also a minimum income you're required to take out of the plan every year and a maximum you're allowed to take. The maximums for LIFs are a bit different than for LRIFs/RLIFs.

3. **You maximize the tax deferral** - Since income is taxed only when it’s taken out of the plan, the tax deferral you enjoyed with your LIRA or locked-in RRSP continues.

4. **You can use money remaining in a LIF to purchase a secure guaranteed income in a life annuity** - Depending on the pension rules in your province, you may be required to do this at a certain age.

5. **You can name a beneficiary to receive your money after you die** – This can add to the overall estate planning process
Can Your Clients Claim the Pension Income Tax Credit?

Depending on your age, RRSP or RRIF payments may qualify for the pension income tax credit.

The tax credit is equal to the lesser of your ‘pension income’ or $2,000. This means that the maximum pension income credit is between $440 and $720 depending on where you live. Any provincial taxes credits will increase the effect of this credit.

If your clients are under the age of 65, you may claim the tax credit if your payments are received because of a spouse’s death.

Lump sum RRSP payments do not qualify for the pension income tax credit.

WHAT ABOUT YOUR CLIENT’S OTHER ASSETS FOR RETIREMENT INCOME?

People began to invest for the future seriously in the 1950’s. Since that time, the Canadian economy has had a very positive effect on them. Savings and investments have compounded many times over. Many of the investments have had a certain element of risk attached to them, but due to the skill level of the advisors that they dealt with throughout the years; their assets for the most part have increased.

Retirement should be a time of expectation and enjoyment; a time to put all the plans and goals that you have made over the years into action. But when the time comes, will you have the resources to live the life you have imagined? If the advertising in the media is correct, you will either be quite rich or very broke. It’s a good idea to aim in between.

The following examples are just a few of the flexible options that are available for the development of personal non-registered assets that can be converted to retirement income.

TAX-FREE SAVINGS ACCOUNTS (TFSA)

Tax-Free Savings Accounts (TFSAs) were first introduced in Canada in 2009. Most Canadian financial institutions now offer them. A TFSA allows any Canadian over the age of 18 to save or invest money in a tax-free account. “Tax free” means that you don’t pay taxes on the money you make inside your TFSA.
Any Canadian resident aged 18 or older with a social insurance number may open a TFSA.

The flexibility of the TFSA may meet your client or prospects requirements for various reasons, for example, if:

- *They want to save money for a specific purchase or to prepare for the unexpected,* the TFSA is an ideal, multi-purpose savings tool offering all the flexibility you need to save for a range of reasons in a single account (for example, toward a down payment on a major purchase such as a house, car or cottage). You can withdraw your money whenever you need it knowing that income on your investment grows tax-free in the meantime.

- *You are a high-income earner:* the TFSA is ideal if you seek to build up additional income in a tax-free environment ahead of retirement. It enables you to convert your taxable income into non-taxable revenue for life while establishing an investment portfolio subject to preferential tax treatment. This helps you to maximize the growth of your investments.

- *They are retired:* the TFSA is an ideal vehicle to keep your investments growing tax-free. Since TFSA withdrawals are not considered as income, they won’t affect Old Age Security nor Guaranteed Income Supplement benefits.

Investment income generated by this account accumulates tax-free on a lifelong basis! This applies regardless of whether the income comes from interest, dividends, capital gains or income trust distributions.

Neither income nor withdrawals from a TFSA affect your eligibility for other benefits based on your income level such as the Canadian Child Tax Benefit or the Guaranteed Income Supplement.

*Investments in a TFSA* can contain GICs and segregated funds.

**Contributions to a TFSA**

TFSA limits will remain indexed to inflation for future years.

There is a maximum amount of money you can deposit into your TFSA each year. Currently, this annual maximum is **$5,500.** Luckily, your total contribution is cumulative, so you can roll over this contribution room year to year. So, the amount you can save will go up each year, whether you deposit money or not.
It doesn’t matter how much the savings or investments in your TFSA are worth; the only thing the government limits is how much you can put in.

If you don’t have a TFSA in 2018, then you could open one and contribute a maximum of $57,500.

The TFSA limit determines how much you can deposit in your Tax-Free Savings Account each year.

The TFSA Contribution Limits Since Inception (2009)

<table>
<thead>
<tr>
<th>Year</th>
<th>TFSA Annual Limit</th>
<th>TFSA Cumulative Limit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>$5,000</td>
<td>$5,000</td>
</tr>
<tr>
<td>2010</td>
<td>$5,000</td>
<td>$10,000</td>
</tr>
<tr>
<td>2011</td>
<td>$5,000</td>
<td>$15,000</td>
</tr>
<tr>
<td>2012</td>
<td>$5,000</td>
<td>$20,000</td>
</tr>
<tr>
<td>2013</td>
<td>$5,500</td>
<td>$25,500</td>
</tr>
<tr>
<td>2014</td>
<td>$5,500</td>
<td>$31,000</td>
</tr>
<tr>
<td>2015</td>
<td>$10,000</td>
<td>$41,000</td>
</tr>
<tr>
<td>2016</td>
<td>$5,500</td>
<td>$46,500</td>
</tr>
<tr>
<td>2017</td>
<td>$5,500</td>
<td>$52,000</td>
</tr>
<tr>
<td>2018</td>
<td>$5,500</td>
<td>$57,500</td>
</tr>
</tbody>
</table>

TFSA withdrawals

You can make withdrawals from your TFSA at any time. In addition, the funds withdrawn (capital and interest) are not taxable! However, the usual restrictions apply to certain products (for example, maturity dates for a GIA). You can then re-contribute the funds to your TFSA as soon as the next calendar year without affecting your contribution room.

For clients who have withdrawn from TFSAs, their crystallized gains and losses from withdrawals are factored in to their TFSA room.

Here’s the withdrawal formula:

Unused TFSA contribution room to date + Total withdrawal made in this year + next year’s TFSA dollar limit = TFSA contribution room at the beginning of next year
What happens if you exceed my contribution amount for any year?

As with an RRSP, if the amount you deposit ever exceeds your annual contribution room, you will be subject to a monthly tax of 1% on the excess amount for that year.

For example, if you contribute $6,000 to a TFSA in 2009 and the maximum contribution amount is $5,000, then you will be taxed 1% of the excess amount of $1,000, per month, for each month that this surplus remains in the TFSA. Also, effective October 17, 2009, any earnings or increase in value attributable to excess contributions will be considered an advantage on which an additional tax will be applicable.

You should know that the TFSA does not offer any margin, as with an RRSP, whereby you may invest up to $2,000 more than your maximum contribution amount before the 1% tax becomes applicable.

What happens to my TFSA at the time of death?

The assets held in your TFSA may be transferred to the TFSA of your spouse or common-law partner without affecting his or her maximum contribution limit if you have named that person as the sole beneficiary of your contract. Investment income can continue accumulating in a tax-free environment in this manner. Note that the transfer must take place before the end of the year following your death.

What happens if I designate someone other than my spouse or common-law partner as my beneficiary?

According to the Canada Revenue Agency, gains accumulated in a TFSA after the death of the account holder are generally taxable, while gains accumulated prior to the death remain tax-exempt. On receipt of proof of death, our company consequently pays out any funds to the designated beneficiary promptly to limit the accumulation of taxable gains inside the TFSA of the deceased.

Are you allowed to contribute to a spouse's or common-law partner's TFSA?

Yes. You may contribute to the TFSA of your spouse or common-law partner without affecting your own contribution room. In this case, you are making a cash "gift" for that person to then invest in his or her TFSA.
Can the income earned from the other person's account be returned to my account?

No. Any investment income or capital gains accumulating in your spouse's or common-law partner's TFSA remain that person's property.

What happens to my TFSA if my relationship breaks down?

When a marriage or common-law partnership breaks down, an amount can be transferred directly from one current or former spouses or common-law partner's TFSA to the other person's TFSA in the following situation.

You and your current or former spouse or common-law partner were living separate and apart at the time of the transfer and you are entitled to receive the amount:

- under a decree, order or judgment of a court or under a written separation agreement; and
- to settle rights arising out of your relationship on or after the breakdown of your relationship.

The amount of the transfer does not affect the recipient's TFSA contribution room. However, since this transfer is not considered a withdrawal, the transferred amount is not added back to the transferor's contribution room at the beginning of the following year.

In addition, the transfer does not eliminate any excess amount in the TFSA.

Does a transfer from a non-registered contract to a TFSA have tax consequences?

Transferring funds from a non-registered contract to a TFSA has tax consequences in the event of capital gains or losses within the non-registered contract.

For example:

You purchased 100 units of a segregated fund on June 1, 2006, within your non-registered contract, when the fund's unit value was $10. On March 1, 2009, you decide to transfer the money from the non-registered contract to a TFSA. The fund's unit value on the date of the transfer is $13. You are consequently required to declare a capital gain of $300 on your income tax return for the year 2009.
What happens to my TFSA if I leave Canada?

If you become a non-resident, you may keep your TFSA, and your investment income and withdrawals remain non-taxable in Canada. However, you may neither contribute to your TFSA nor build up contribution room during the years that you spend as a non-resident.

Which should I choose, a TFSA or an RRSP?

Both, if possible! Of course, the reality is that people’s savings capacity is often limited by personal constraints, making this recommendation impossible for many to follow. In that case, how do you choose? The answer to this depends on your savings requirements.

What can a TFSA be used for?

For needs over the short to medium term

If you expect to require money over the short term, then the TFSA may be the better choice, especially since it allows you to leave your RRSP contribution limit intact. This rare tax gift enables you to set aside money to cover the unexpected, save toward a major short- or medium-term purchase or invest in your retirement if you have maximized your RRSP contributions.

For retirement

If you do not plan to withdraw the invested funds before retirement and expect a lower tax rate at that time, then an RRSP remains the best choice for you. This is because investing in an RRSP, if you have not already maximized your contributions, provides an immediate tax deduction and remains an essential tool in saving for retirement.

For client’s subject to a high marginal tax rate, the tax savings generated by RRSP contributions continue to offer a significant advantage. What’s more, people may tend to be more reluctant to dip into an RRSP than a TFSA before retirement. However, if your current tax rate is lower than it will be in retirement, or if you expect to collect the Guaranteed Income Supplement in retirement, the TFSA is probably the better choice.

Long before the tax-free savings account, there was the principal residence exemption – the grand-daddy of tax-free savings.
How to fit your house into your TFSA

Like a TFSA, capital gains made on the sale of your principal residence is tax free. In comparison, half of any gains on a stock sold outside a registered account are taxed, and any gain in a registered retirement savings plan (RRSP) is fully taxed when withdrawn.

You really can’t avoid being taxed on your RRSP, but you can save big tax dollars by planning ahead and keeping RRSP withdrawals in the smallest tax brackets and topping your income off with the two tax-free alternatives.

Contribution limits make the TFSA less effective in retirement, and that’s where tax-free cash generated from your house can get you where you need to be.

How to use the principal residence exemption in retirement depends on the individual situation. Homeowners who sell and become renters can pocket the entire amount without tax implications. Those who move to less expensive houses in retirement can simply pocket the difference tax free. Even those who want to stay in their homes can borrow from a home equity line of credit for tax-free income.

If you’ve drained part or all your TFSA by the time you sell your house, that cash can even be invested using whatever contribution room has opened up.

Tax planning and determining if your home is a principal residence can get complicated. It might be best to run your tax-free plan by a specialist.

TFSA vs RRSP

Perhaps the most stunning trend is that the TFSA is catching up to the RRSP as the tax-sheltered investment of choice.

An RRSP gives a person an up-front tax deduction that they don’t get with a TFSA. But the federal government then snags its share in income tax assessed on the back-end cash withdrawals, typically after the taxpayer retires.

As a result, it's not uncommon for financial advisers to recommend TFSAs over, or in equal partnership with, RRSPs as a savings vehicle for taxpayers.

For someone's in a low tax bracket now — say under $50,000 a year — with the effect from income taxes and the claw back of government benefits they could find themselves in a higher effective tax bracket when they take the money out."
That means both the principal and the return could end up taking a big tax hit when the investment is taken out of an RRSP.

When you withdraw the money, you lose some government benefits, which causes your effective tax rate to be higher. For very low-income people, it's the GIS [guaranteed income supplement]. For middle-income people, it's the age credit and the GST/HST credit. So, it may make sense for those people to maximize a TFSA before looking at an RRSP.

TFSA gives people more options for what to do with their money, in part because they can withdraw it and put it back the following year — something you can't do with an RRSP. That's useful for people with lower and middle incomes, who are more likely to need access to their long-term savings if they hit fiscal adversity, or just need cash for pricey outlays like a new car or home renovations.

The following table provides an overview of the main differences between an RRSP and a TFSA at a glance:

<table>
<thead>
<tr>
<th></th>
<th>TFSA</th>
<th>RRSP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual contribution limit</td>
<td>$5,500 since 2015</td>
<td>18% of eligible income</td>
</tr>
<tr>
<td>Contributions tax-deductible</td>
<td>NO</td>
<td>YES</td>
</tr>
<tr>
<td>Investment income taxable</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>Withdrawals taxable</td>
<td>NO</td>
<td>YES</td>
</tr>
<tr>
<td>Option to carry forward unused contribution room</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>Contribution room recovered after withdrawals</td>
<td>YES</td>
<td>NO</td>
</tr>
<tr>
<td>Maximum age to contribute</td>
<td>None</td>
<td>71</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>TFSA Fair Market Value, Contributions, and Withdrawals</th>
<th>Grand Total of Counts and Amounts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total dollar value of contributions</td>
<td>$61,925,669,000</td>
</tr>
<tr>
<td>Number of contributions (transactions)</td>
<td>101,158,590</td>
</tr>
<tr>
<td>Average number of TFSA contributions (per individual)</td>
<td>12.78</td>
</tr>
<tr>
<td>Average dollar amount of TFSA contributions (per individual)</td>
<td>$7,826.36</td>
</tr>
<tr>
<td>Total dollar value of withdrawals</td>
<td>$21,835,766,000</td>
</tr>
<tr>
<td>Number of withdrawals (transactions)</td>
<td>16,643,290</td>
</tr>
<tr>
<td>Average number of TFSA withdrawals (per individual)</td>
<td>4.48</td>
</tr>
<tr>
<td>Average dollar amount of TFSA withdrawals (per individual)</td>
<td>$5,875.86</td>
</tr>
<tr>
<td>Average unused TFSA contribution room</td>
<td>$24,191.99</td>
</tr>
<tr>
<td>Total Fair Market Value</td>
<td>$193,587,386,000</td>
</tr>
<tr>
<td>Average Fair Market Value (per individual)</td>
<td>$15,205.96</td>
</tr>
</tbody>
</table>

OTHER UNREGISTERED PLANS

In unregistered plans that provide income, the principle is received tax free, while any interest portion such as capital gains, dividends etc. are added to a person’s income tax return.

Some of the following investments have stood the test of time and have done an excellent job in combating inflation and increasing the purchasing power of the dollar.

SHORT-TERM INVESTMENTS

To provide for the basic living expenses and contingencies, an investor should maintain an adequate amount of funds in a savings account at a financial institution. Some people consider daily interest accounts to provide a convenient means of earning a return on funds on hand for short periods. When they gather a surplus of funds more than emergency reserves, the investor should look at a range of short-term investment vehicles to maximize their yield without sacrificing safety.
Financial institutions such as banks and trust companies offer a wide variety of short-term debt instruments. It is wise for you to shop around, as there is a wide variation in the minimum investments required yields and maturates to suit individual circumstances.

The two main types of short-term investments are:

**Redeemable term deposits**

This type of investment requires the investor to deposit a fixed amount of money at a predetermined rate of interest for a stated period, usually ranging from 30 days up to 6 years. The minimum deposit is usually in the $1,000 to $5,000 range. Interest rates are higher than on premium savings accounts but will reflect the amount invested, the term to maturity and general money market conditions. This type of deposit can normally be redeemed before maturity but at a reduced rate of interest. An example is a chartered bank term deposit certificate.

**Non-redeemable term deposits**

These are very similar in many respects to redeemable term deposits except that they have longer terms such as one to six years and they are generally non-redeemable before maturity (except on death of the purchaser). This is not a good choice, if the investor needs the funds before maturity, but they can be accepted as collateral for a loan. Rates are competitive and will vary as to the amount invested, the term and general conditions in the financial markets.

Securities firms can normally help with short-term investments including money market instruments such as treasury bills, commercial paper and short-term bonds. The minimum investment required may be greater than for many deposit vehicles.

All the above does not attempt to exhaust all short-term investment alternatives. Caution and careful investigation should be taken before any commitment is made, as there may be considerable risk involved.

**STOCK MARKET**

An organized stock exchange is a market place where buyers and sellers of securities meet under competitive conditions to trade with each other and where prices are established according to the laws of supply and demand. Here in Canada, trading is carried on in common and preferred shares, rights and warrants, listed options and futures contracts.
Business cycles result in peaks and valleys in economic activity and alternating periods of prosperity and slowdowns or recessions. During these cycles, the prices of securities tend to rise or fall as the economic outlook improves or deteriorates.

Fortunes rise and fall regularly for purchasers of equity products that are purchased from the stock market. Usually, long-term investments in Canadian Equities have had an enviable record against inflation.

**CANADIAN STOCK EXCHANGES**

**Toronto Stock Exchange**

The *Toronto Stock Exchange (TSX)* is Canada's largest stock exchange, and the division of the TSX Group that holds senior equities. A broad range of businesses from Canada, the United States, and other countries are listed on the exchange.

The TSX is headquartered in Toronto, the third largest financial centre in North America, and maintains offices in Montreal, Winnipeg, Calgary, and Vancouver. The TSX is one of the world's largest exchanges and the third most active in North America behind the New York Stock Exchange and the NASDAQ.

**Vancouver Stock Exchange**

The *Vancouver Stock exchange (VSE)* was one of Canada's junior company stock exchanges. On March 15, 1999, the VSE and the ASE (Alberta Stock Exchange) agreed to merge and form the CDNX - the Canadian Venture Exchange - which will also take on some junior Toronto and Montreal Exchange companies.

The VSE got a bad reputation in the 80's due to many unscrupulous scam artists manipulating VSE listed companies. New regulatory controls and surveillance systems which had been implemented on the VSE were transferred to the new CDNX. In 2002, the CDNX became the TSX-V.

**Montreal Stock Exchange**

In 1982, the *Montreal Stock Exchange (MSE)* changed its name to the Montreal Exchange to reflect the growing importance of financial instruments other than stocks – primarily options and futures – on its trading floor.
In 1999, the Vancouver, Alberta, Toronto and Montreal exchanges agreed to restructure the Canadian capital markets along the lines of market specialization, resulting in the Montreal Exchange assuming the position of Canadian Derivatives Exchange for the following 10 years. Trading in the shares of large companies was transferred to the Toronto Stock Exchange (TSX), and in the trading of smaller companies to the new TSX Venture Exchange.

This change, which reflected the economic reality that most equity trading had moved to the TSE, caused consternation among those in favour of political independence for the province of Quebec, because it means that any future independent Quebec would not have its own equities exchange.

So today the MSE is a Canadian derivatives exchange that facilitates the trading of stock options, interest rate futures and options, as well as index options and futures.

Located in Montreal, Quebec, it is the country's main financial derivative market, while the Winnipeg Commodities Exchange in Manitoba is the home to Canadian commodity derivative trading.

The equity option trading on the Montreal Exchange covers most of the larger Canada-traded companies but is not as broad as the U.S. options markets.

The interest rate derivatives cover short-term banker's acceptances ranging from the overnight rate to the three-month rate and two- and ten-year Canadian Government Bonds. The index futures and options cover the S&P Canada 60 index and several S&P/TSX sector indexes.

In April 2005, the Toronto Stock Exchange made public its intention of acquiring the Montreal Exchange, circumventing the non-compete agreement that would expire in 2009.

**Historical Investment Returns on Stocks, Bonds, T-Bills**

The Canadian Consumer Price Index has been quite stable since 1992. In the 30 years from 1963 to 1992, the average annual increase (inflation rate) was 5.7%. During that time, there were 5 years where the inflation rate was over 10%, including 1981, when the rate was 12.4%. 1981 is also the year when Canadian 5-year mortgage rates were over 21% for a couple of months. The average 5-year mortgage rate from 1963 to 1992 was 11.03%.
Some typical long-term stock results:

<table>
<thead>
<tr>
<th>Type of Investment</th>
<th>1 year</th>
<th>5 years</th>
<th>10 years</th>
<th>Since Dec 31, 1979 38 years</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AAR</td>
<td>Val</td>
<td>AAR</td>
<td>Val</td>
</tr>
<tr>
<td>Cdn 3-month T-bills</td>
<td>0.7%</td>
<td>$1,007</td>
<td>0.7%</td>
<td>$1,036</td>
</tr>
<tr>
<td>Cdn Govt Bonds 1 to 3 year *</td>
<td>1.1%</td>
<td>1,011</td>
<td>0.9%</td>
<td>1,045</td>
</tr>
<tr>
<td>Cdn Govt Bonds over 10 years *</td>
<td>2.2%</td>
<td>1,022</td>
<td>2.3%</td>
<td>1,118</td>
</tr>
<tr>
<td>S&amp;P/TSX (Cdn) Composite Total Return Index (formerly TSE300 Total Return) (3)</td>
<td>9.1%</td>
<td>1,091</td>
<td>8.7%</td>
<td>1,514</td>
</tr>
<tr>
<td>Nikkei 225 TRI © Nikkei Inc. in Cdn$ (2)</td>
<td>17.5%</td>
<td>1,175</td>
<td>18.2%</td>
<td>2,307</td>
</tr>
<tr>
<td>S&amp;P 500 (US) Index in Cdn$</td>
<td>14.6%</td>
<td>1,146</td>
<td>21.3%</td>
<td>2,625</td>
</tr>
<tr>
<td>Emerging markets stocks in Cdn$ (1)</td>
<td>28.7%</td>
<td>1,287</td>
<td>9.7%</td>
<td>1,589</td>
</tr>
<tr>
<td>Canadian Consumer Price Index All Items</td>
<td>1.9%</td>
<td>1,019</td>
<td>1.5%</td>
<td>1,079</td>
</tr>
</tbody>
</table>

Some notes for the previous table:

Value is the value at the end of the period, of $1,000 Cdn invested at the beginning of the period.
n/a = not available

The column for returns since December 31, 1979 reflects the earliest data we have for the Nikkei 225 Index.

* Note that the average annual return on bonds is the average yield if the bonds are held to maturity.

(1) For Emerging Markets, the earliest data that we have is December 31, 1987. The average annual return in Canadian dollars for emerging markets for the 30 years from 1987 to 2017 is 11.2%. $1,000 invested at the end of 1987 would have a value of $23,859 Canadian at the end of 2017.

(2) The Nikkei 225 Total Return Index (TRI) yearend factors in yen are used with the permission of Nikkei Inc. to calculate the above results. Recent Nikkei year end factors are available on the Nikkei website. The earliest data that we have is December 1979, when the Nikkei 225 TRI was started. The average annual return in yen for the Nikkei 225 TRI for the 38 years from 1979 to 2017 is 4.5%. 1,000 yen invested at the end of 1979 would have a value of 5,391 yen at the end of 2017.

(3) Some of the earlier S&P/TSX Composite Index Total Return data is from Libra Investment Management Inc., sourced from the Canadian Institute of Actuaries. Data for recent years is available from Yahoo Finance.

Yields

Yield to the investment industry is the annual income from an investment expressed as a percentage of the cost or market price. In the case of stocks, yield is simply the indicated annual dividend expressed as a percentage of the market price.

Unlike a stock yield, a bond yield not only reflects the investor’s return in the form of income, but also makes allowances for any capital gain (or loss) realized when the bond matures.

A terminal yield is the final price when shares are sold, against what they cost to buy.

Current yield is the dividend paid as a percentage of the current price. When the shares are sold, a capital gain is realized in the excess over the Adjusted Cost Basis.
Currently, only 50% of the capital gain is subject to tax at Personal Income Tax rates. Sale (or purchase) of shares incurs a cost base, which is deductible from Capital Gains.

**Capital gain**

Capital gain is the difference between an asset's purchase price and selling price. (The difference is called a "capital gain" only if it's a positive amount. If it's negative, it's a capital loss.) For example, if you buy 100 shares of Intuit stock at $35 per share and sell them for $45 per share, your capital gain is $1,000 ($4,500 - 3,500). The capital gains inclusion rate is currently one half. (The inclusion rate is the portion of a capital gain that is subject to income tax.)

**Capital loss**

A capital loss is the negative difference between an asset's purchase price and its selling price. If the difference between the purchase price of an asset and its selling is positive, then it is called a capital gain. For example, if you buy 100 shares of Intuit's stock at $35 per share and then sell them for $25 per share, your capital loss is $-1,000 ($2,500 - 3,500).

**INVESTMENT FUNDS**

An investment fund is a company or trust engaged in managing investments for other people. Selling shares or units to many investors raises capital and the money raised is then invested according to the fund's investment policies and objectives.

The fund's earnings are the dividend and interest it receives on the securities it holds and the capital gains it may make in trading its investment portfolio.

**There are two basic types of investment funds:**

1. **Open Ended Funds (Mutual Funds)**

By far the most common type of fund is known as a Mutual Fund. It is an open-ended fund because it continuously sells its own treasury shares or units to the investing public. The fund then operates on the original capital and re-invested earnings. Those shares are continuously available for purchase, not from other shareholders – but from the fund itself.

The fund guarantees to buy back the shares (or units) at any time for the net asset value of the days following redemption.
The funds are evaluated at the close of the day and after subtracting costs and a management fee, the number of units is divided into the entire equity portfolio to produce the Net Asset Value.

Mutual funds can be purchased with a single, periodic or monthly investment.

A mutual fund’s shareholders have an ongoing right to withdraw their investment in the fund simply by submitting their shares to the fund itself. This characteristic is known, as the right of redemption and it is the hallmark of mutual funds.

Acquisition charges (loading charges or sale charges) are either loaded on as “front end charges or redemption charges”. “No load” funds usually have an additional charge applied before determination of the Net Asset Value of The Shares. (NAVPS)

2. Closed-End Investment Funds

Closed-end funds are started by a select group of investors who provide the startup Investment Capital by purchasing an initial issue of shares. Thereafter, the fund operates on the original capital and re-invested earnings.

These funds are like mutual funds, as they invest the money of their own shares or unit holders in investments that reflect the fund’s policies and objectives. However, unlike the mutual fund whose shares are continually being sold and redeemed, the number of shares in a closed-end fund remains relatively fixed. These shares must be bought from an original shareholder or from a stockbroker. Purchasers of closed-end investment fund shares pay a negotiated commission when the shares are purchased and when they are sold. These shares or units trade on the various stock exchanges or on the over-the-counter market.

The direct price relationship, between a mutual fund's shares and the current market value of its investment portfolio, is also in contrast to the market price of equities of closed-end investment companies, which typically trade at substantial discounts below the break-up value of their portfolios. The pledge of continuous redemption by mutual funds however assures a continuing close relationship between their redemption and their current portfolio valuation. The smaller the fund, the harder it is to market their shares.

Taxation of Investment Funds

In general, the Canadian tax rules provide that Canadian mutual funds are essentially conduits through which the fund’s investment income and net capital gains pass to the fund holders without double taxation.
When shares are sold, a capital gain is realized in the excess over the ACB currently only 50% of the Capital Gain is subject to tax at Personal Income Tax rates. Sale (or purchase) of shares incurs a cost base, which is deductible from any Capital Gain.

Each year, unit holders of an unincorporated fund are sent a T3 form and shareholders are sent T5 forms by each fund reporting all the income paid out over the year, including foreign income and Canadian interest, dividends and capital gains.

MUTUAL FUNDS (Open End Funds)

An open-end fund is a type of mutual fund that does not have restrictions on the amount of shares the fund can issue. Many mutual funds are open-end, providing investors with a useful and convenient investing vehicle.

Investment Companies that form Mutual Fund Companies operate either as a Trust or a Corporation, however, wanting to eliminate double taxation, trusts are becoming far more common.

They primarily operate the same as Segregated Funds, without the basic guarantees (75% of the deposit made) and are governed by the Securities Act of the Province.

A Mutual Fund operates with five components:

1. The Investment Company

The fund itself will either be a Trust issuing units, or an Incorporated Company issuing shares.

2. Management Company

As in any corporation, the Management Company has officers and a Board of Directors. It can sue or be sued. The primary objective of these positions will be the oversight of the objective of the mutual fund and see that it fulfills its mandate.

The Board of Directors may appoint an Investment Advisory Committee to direct this activity.

The Mutual Fund in fact engages the company to manage its investments. The contract between them can be changed, if approved by shareholder majority.
Generally, the same people start the fund and the company and some of the people involved will have similar functions for both the fund and the company.

The duties of the management company are paid by way of 1 to 2% annual fee, based on the net asset value of the fund and these duties include providing and paying for the offices, salaries, and providing research and statistical developments.

The actual investment of the funds may be conducted by the officers of the Investment Company, its committee or to a separate “specialty” fund Management Company.

3. **Distribution**

The distributor may also be known as the sponsor or underwriter, markets the shares (called units if a trust format is used). For this function, the distributor receives the difference between the sales charge and the dealer concession. If the sales charges are 9%, over 6% of the charge can go to the distributor.

4. **Custodian**

The custodian is generally a trust company or a bank. It is the “safe keeper” of the fund assets, initiating the purchases, paying fees and receiving payments for securities when sold. Fund expenses, including fees from the management company are payable from the income earned by the funds’ investments.

5. **Transfer Agent**

The Transfer Agent is generally a trust company, frequently the same trust company that acts as custodian. Its duties include being the keeper, issuer of shares, receipts and certificates. It also redeems the shares from shareholders, but its functions have nothing to do with fund management. This sharing of function also occurs with the Management Company, which may provide its own distributor network, each with its own functions.

**Evaluation and Pricing**

Both Mutual Funds and Closed End Funds are evaluated the same way. The net asset value is determined daily by the following formula:

\[
\text{Net Asset Value} = \frac{\text{Assets} - \text{Liabilities}}{\text{Number of Shares Outstanding}}
\]
The buying price includes a Front-End Load (Sales Charge) although the fund may operate as a "No Load" fund or it may have redemption charges.

**Investing in a Mutual Fund**

A deposit is paid to the custodian who pays the sales charge to the distributor and forwards the balance to the Transfer Agent. The Transfer Agent issues a confirmation form showing the number of shares purchased at the funds net asset value, date of purchase and price per share paid.

Subsequent deposits repeat the process. Each fund transaction (capital gains, dividends earned etc.) will also trigger a new transaction slip. Unlike a purchase of actual stock purchases on the stock market, mutual fund shares can be purchased in full or fractional amounts to account for all the dollars paid.

Each purchase must be initiated by a presentation of a prospectus. This contains the Security Commissions details regarding investment limits as well as other regulatory items and guarantees. Each fund decides and sets up its own operating limits according to the regulations and must abide by them.

**A Prospectus contains the following restrictions:**

- No bonds, debentures or senior securities may be issued.
- They may not underwrite securities of other companies.
- May not lend money directly.
- May not borrow money.
- May not speculate in commodities, selling on margin or sell short.

**Types of Investment (Mutual) Funds & Risk Tolerance**

One would think that Professional Fund Managers get professional results. This is not always the case, but the fund results over a long period produce a much higher return than conventional investments.

It is essential when buying a mutual fund to target funds that are compatible with your investment risk tolerance. A fund’s prime investment goals are stated in the fund’s offering prospectus and generally cover the degree of safety or risk that is acceptable, whether income or capital gain is the prime objective, and the main types of securities in the fund’s investment portfolio.
When you consider your client’s risk portfolio, the following main types of funds should be considered:

1. Growth Funds (Common Stock or Equity Funds)

The primary purpose of these funds is to produce long-term capital growth. Dividends place second to anticipate growth. Most growth occurs in common stocks. The investment risk is higher. Dividends if paid may be automatically reinvested.

Short term notes or other fixed income securities may be purchased from time to time in limited amounts for diversification, income and liquidity, but the bulk of the assets are in common shares in pursuit of a capital gain.

Because common share market prices are more volatile than market prices of other fixed-income securities, net asset values of equity funds tend to fluctuate more than those of income or balanced funds. These funds range greatly in degree of risk and growth potential.

2. Income Funds (Bonds & Debentures)

The main investment goals are those of safety of principal and high income. Investment by such funds is primarily in good quality, high yielding government and corporate debt securities, some high-yield preferred and common shares and mortgages. There is limited opportunity for capital gain in income funds and comparatively little fluctuation the price of their shares.

Income funds provide for an immediate income produced from a lump sum investment into the fund. Changes in interest rates directly result in corresponding opposite change in the values of the bond holdings.

One type of income fund that has become very popular with investors is the money market fund. The objective of this type of fund is to achieve a high level of income through investment in short term, fixed income securities such as treasury bills and short-term government bonds.

3. Balanced Funds

The main investment objective for these funds is a mixture of safely, income and capital appreciation. These objectives are achieved through a balanced portfolio of fixed income securities for stability and income, plus a broadly diversified group of common stock holding for diversification, dividend income and growth potential. The managers of these funds adjust the asset mix in accordance with
current market trends and future expectations. Large upswings or down swings in the market will not greatly influence the returns of Balanced funds.

4. Specialty Funds

These funds concentrate on shares of a group of companies in one industry, in one geographic area or in one segment of the capital market. Even though these funds offer some diversification in their portfolios, they are more vulnerable to swings in the industry in whose shares they specialize in, or if they have a portfolio of foreign securities, in currency values.

5. Dividend Funds

These funds invest in primarily high quality preferred and sometimes common shares of taxable Canadian Corporation to obtain maximum dividend income.

6. Real Estate Funds

These funds invest in income-producing real property to achieve long term growth through capital appreciation and the reinvestment of income.

7. Ethical Funds

These fund investments are governed by moral criteria. These criteria may vary from fund to fund. One ethical fund may avoid investing in companies that profit from tobacco, alcohol or armaments, while another fund may invest according to certain religious beliefs.

8. Global and Foreign Funds

May be fixed income, growth or balanced funds that invest in foreign securities.

These funds can offer investors international diversification and exposure to foreign companies but are subject to risks associated with investing in foreign countries and foreign currencies.

9. Index Funds

Invest in a portfolio of securities selected to represent a specified target index or benchmark such as the S&P/TSX Composite Index.
Key Points to Remember

- Funds fall into several broad-based categories.
- Mutual funds never invest at random.
- Match a fund’s investment objectives to your own.
- Risk is the potential for losing money.
- No investment is risk free.
- The higher the risk, the higher the potential return.

Advantages of Mutual Funds

- Professional management
- Broad diversification
- Variety of types of funds
- Invest correctly, they could be low risk
- Variety of purchase plans to allow affordability
- Liquidity
- Transferability

Disadvantages of Mutual Funds

- Unsuitable for short-term investment due to fees and sales commission
- Unsuitable as an emergency reserve
- Professional investment management is not infallible
- Management fees can be expensive

SEGREGATED FUNDS

These funds are the Insurance Industries answer to the Investment Funds. The challenge for the Savings (Investment) dollars prompted the launch of the Segregated Funds in 1961. Except for a few segregated funds, many have not seen considerable growth throughout the years.

The conservative nature of their fund managers, and the fact that they were used initially for the pension industry, has had a large influence on the returns. In later years, their methods have seen much better results.

These funds are held in a separate and distinct investment fund and are not mixed with their other guaranteed investments. Due to their conservative nature, the funds have a mixture of equities, cash and short-term bonds.
Like mutual funds, these funds tend to be operated in “families of funds” each with their own investment strategy and philosophy.

While some segregated funds may be short of investor’s hopes, they are long on dependability and have been a very respectful history of returning value for the money invested.

They operate under the Insurance Act because of their basic guarantee of 75% (may be more), return of the gross premium paid at death or maturity or the value of the fund, whichever is greater.

Most segregated funds are valued daily, although weekly or no less once a month is common. They operate in much the same way as a mutual fund.

**Segregated Funds have Mutual Fund Wraps – The Best of Both Worlds?**

Even though Life Insurance companies have been marketing segregated funds for years, many of the major fund companies are doing it. Because of this wrap, clients can access a brand name mutual fund, and its fund manager, while receiving the death benefit and maturity guarantees that have become so popular.

These death and maturity guarantees are the major attraction of Segregated funds. As seen earlier, the guarantees vary, from carrier to carrier, and it pays to shop around.

Legislation dictates that insurance companies must offer a minimum death benefit and maturity guarantee of 75% to 100%. Many companies have gone over and above this minimum.

All segregated funds are not the same. What they do have in common is a minimum 75% to 100% guarantee of initial investment capital at fund maturity or death of policy holder. Very few segregated funds are unique in that they have 100% guarantee of investment capital at fund maturity or death of policy holder. Very few segregated funds offer a reset (lock-in) of any kind when value of an investment increases.

To reduce costs, many mutual fund companies have decided to have a scaled-back guarantee in their fund wrappings. A 100% death benefit guarantee is often available until a certain age, usually around 80, and then it is cut back to a lower amount. This is done to offset the higher mortality costs at the higher ages. This helps to keep MER expenses lower.
3 Advantages of Segregated Funds

1. **Principal can be guaranteed**

   Depending on the contract, 75% to 100% of your principal investment is guaranteed if you hold your fund for a certain length of time (usually 10 years). If the fund value rises, some segregated funds also let you "reset" the guaranteed amount to this higher value – but this will also reset the length of time that you must hold the fund (usually 10 years from date of reset).

2. **Guaranteed death benefit**

   Depending on the contract, your beneficiaries will receive 75% to 100% of your contributions.

3. **Potential creditor Proofing**

   This is a key feature for business owners.

3 Disadvantages of Segregated Funds

1. **Your money is locked in**

   You must keep your money in the fund until the maturity date (usually 10 years) to get the guarantee. If you cash out before that, you’ll get the current market value of your investment, which may be more or less than what you originally invested. You may also be charged a penalty.

2. **Higher fees**

   Segregated funds usually have higher management expense ratios (MERs) than mutual funds. This is to cover the cost of the insurance features.

3. **Penalties for early withdrawals**

   You may have to pay a penalty if you cash out your investment before the maturity date.
ASSURIS’ PROTECTION

Segregated funds are protected by Assuris, whereas mutual funds don’t offer this type of protection.

The actual value of the fund is not impacted if your life insurance company fails. The fund will be transferred to another company and the guarantees will continue.

If your life insurance company fails, Assuris guarantees that you will retain up to $60,000 or 85% of the promised guaranteed amounts, whichever is higher.

Steps to Calculating Assuris’ Segregated Funds Protection

Step 1

<table>
<thead>
<tr>
<th>Segregated Amounts Invested (with 75% guarantee)</th>
<th>Original policy guarantee at death or maturity when company fails</th>
<th>Guaranteed amount protected by Assuris</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100,000</td>
<td>$75,000</td>
<td>$75,000</td>
</tr>
</tbody>
</table>

Step 2

<table>
<thead>
<tr>
<th>Guaranteed amount protected by Assuris</th>
<th>Explanation</th>
<th>Assuris Protected Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>$75,000</td>
<td>Since the amount is higher than $60,000, the 85% protection is applied to the guaranteed amount. ($75,000 x 85% = $63,750)</td>
<td>$63,750</td>
</tr>
</tbody>
</table>

If at death or maturity the fund value exceeds the guaranteed amount, Assuris protection is not required.
### Segregated Funds vs. Mutual Funds at a Glance

<table>
<thead>
<tr>
<th>Features</th>
<th>Segregated funds</th>
<th>Mutual funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Professional portfolio management</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Diversification among asset classes and management styles</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Grow a portfolio while diversifying risk</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Liquidity: easy access to your money through daily price valuations</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Ability to bypass probate* and keep financial affairs private</td>
<td>Yes</td>
<td>Occasionally²</td>
</tr>
<tr>
<td>Potential creditor protection for registered accounts</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Potential creditor protection for non-registered accounts</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>A guarantee of the principal (or a specified percentage) at maturity³</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>A guarantee of the principal (or a specified percentage) at death³</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Lock in market growth using resets</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

**Notes for previous comparison chart:**

1) Segregated fund fees are higher than mutual funds, as they include a management fee and an insurance fee component.

2) Non-registered accounts with joint ownership and right of survivorship only (all provinces except Quebec). Registered accounts can bypass probate when a beneficiary is named.

3) Withdrawals reduce guarantees proportionately. Guarantees end at age 100.

*Probate fees and requirements vary by province.
VARIABLE CONTRACTS

The Insurance Act defines fund as “a separate and distinct fund, maintained in respect of the no-guaranteed benefits of a variable contract”.

It also defines variable contract as:

“A variable contract means an annuity or Life Insurance contract for which the reserve, or part thereof, vary in amount with the market value of a specified group of assets held in a separate and distinct fund, and includes a provision in a Life Insurance Contract under which policy proceeds may be retained for investment in such a fund”.

There are two distinct elements in a Variable Contract

1. **An Insurance Element**

   Either Insurance protection in the event of death or a Life Annuity option in the event of survival.

2. **Equity Element**

   A reserve, which varies in value, depending on the performance of a segregated fund upon which it is based.

   The variable contract can be a deferred annuity with a lengthy accumulation or an Immediate Annuity with a lump sum deposit. In either case, the funds are placed in the segregated fund as an investment vehicle. The Variable Contract combines an investment in the segregated fund with annuity options.

   The term “VARIABLE CONTRACT” refers both to variable annuity contracts as well as variable annuity settlement options.

   The segregated fund varies in value due to the equity nature of the investment it holds. The value of the variable contract will vary during the accumulation period and each payment of the variable annuity will vary in value, however, the number of payments will be guaranteed.

   The insured variable contract provides, in addition to the equity fund, a sum insured such as a Term Insurance, Reducing Term Insurance or a Whole Life Policy.
The premium portion that goes into the reserves and the dividends may also be invested in the segregated fund. If dividends alone are the source of deposit, reduced sales charges usually apply.

Gross premiums (in relation to the 75% minimum return) include not only the premium paid, but also the cost of the “return of premium” guarantee, which is included with the sales charge. For example, a 9% sales charge may include 5% commission, 2% return of premium charge and 2% operating costs.

**Accumulation Deposits**

**Single Deposits**

A single premium can be deposited either into an immediate annuity (Income commences immediately) or into a deferred annuity (Investment accumulates, income deferred). Sales charges are applied in the form of front-end charges or redemption charges and a contract fee may be charged in addition. Additional deposits may be made.

**Monthly Contractual**

These plans require regularly scheduled contractual payments such as monthly, semi-annually or annually. Additional lump sum payments may be made. The plan may be a stand-alone or a rider to another policy. Sales charges generally apply.

**Flexible Deposit**

A deferred annuity may be considered an open deposit account, payments being made when available. Since it allows for partial withdrawals and cancellation, it can be used as a source of Investment Capital, Emergency or Education Funds as well as many other benefits.

**Calculation of Value**

The investment portion of each deposit is translated into units, which are then credited to the policy. The unit value is the value calculated on the valuation date following the deposit. As unit values fluctuate, varying number of units will be purchased with equal monthly payments or with a lump sum payment.

At death or maturity, the units are converted back into cash at the then prevailing unit value, unless the minimum guarantee applies (death or maturity).
INSURED PLANS

Insured Plans are issued in two types:

The premium is split into two parts:

Part is used to provide Life Insurance Benefits, Riders, Sales Charges and Contract Fees. The remainder is deposited into the Segregated Fund.

1. **At death**, both the Life Insurance Benefits and the Investment Benefit are payable.

2. **At maturity**, both the Equity Value and CSV, if any, is available. The Insured Plan can be issued as one policy or two distinct policies. The Linked Life Policy can be Term, Reducing Term or Whole Life.

Fully Variable Plans

In variable plans, not only is the equity fund vulnerable to the changing nature of the segregated fund, but also the sum insured. The sum insured will vary but will have the same basic guarantees as the equity fund to “maintain” the Life Insurance Act status of the plan.

*The guarantees may be worded as follows.* The *Sum Insured will be the greater of*:

- The dollar value of the sum insured, assuming no change in the unit value after the effective date of the policy, *OR*
- 75% of the total dollar value of the basic premiums due and paid before Age 75.

The contract will also contain a minimum guarantee at maturity of 75% of the total dollar value of the premiums paid in the case of annuity contracts. Some contractual guarantees are as high as 100%.

Settlement Options

The same basic settlement options are available as guaranteed annuities, however, a few additional options are added in:

- Deposit Option
- Fixed Period or Fixed Guarantee Period
- Life Annuity with no Guaranteed Period
• Life Annuity with a Minimum Guaranteed Pay Period (10, 15, 20 years)
• Joint, Last Survivor Annuity, payable to the second death
• A Variable Annuity Option Payment where the dollar amount of each payment is linked to the changing value of the units. The units in turn are based on the value of the segregated fund. The duration of the payments whether Lifetime, Guaranteed for a minimum of 10 years or Term Certain Annuity will be guaranteed. In good market times the dollar value of the payment will be higher than in poor market times.

GUARANTEED MINIMUM WITHDRAWAL BENEFIT PLANS (GMWB)

GMWB products are a combination of investments and insurance. This is known as a variable annuity. With GMWB products, you get a guaranteed minimum income from your savings each year – starting as early as age 50 for some products. They also provide the potential for investment gains to help increase this income over time.

Fees for this product can be expensive as the annual management fees can be significantly higher than for other types of investment funds. Penalties can decrease your guarantee if you make a withdrawal that exceeds the guaranteed amount.

GMWB products are offered by insurance companies and can have a variety of features.

Here’s how a typical GMWB product might work:

1. You deposit a lump sum of money

In your pre-retirement years, say at age 55, you transfer money to the insurance company either from your non-registered or registered plan savings, to buy the GMWB product. You can also make additional deposits to the product. Like a traditional annuity, a GMWB product is based on a contract between you and the insurance company.

2. You choose the investments

The insurance company will provide you with a variety of investment funds to choose from. Insurance companies typically limit how much you can invest in equities, which is another word for investments in the stock market
For example, the contract may limit you to investing 70% of your deposit amount in equity funds. Or, the insurance company may only offer balanced funds with different mixes of stock, bond and money market investments.

3. **Ask if the contract can change**

Depending on the terms of the contract, the insurance company may be able to make changes, such as increasing the fees they charge or increasing investment restrictions on new money that you invest. Before you buy, find out what can be changed and decide if you are comfortable with these terms.

4. **Your income guarantee comes into effect**

Once your money is deposited and invested, you are entitled to a guaranteed income, beginning at a specified age. A typical product guarantees that you can withdraw 4% of your investment amount each year for life, no matter how long you live or how well your investments perform.

For example, if you deposit and invest $100,000 at age 55, you will be entitled to income of $4,000 each year starting at age 65, guaranteed for life. While you can withdraw more than this guaranteed amount in a year, penalties apply to these “excess” withdrawals – and can reduce your future guaranteed income level.

5. **You can increase your guaranteed income**

A key feature of GMWB products is the ability to increase your income guarantee, especially in the years leading up to retirement.

This is done in 2 ways:

1. **By receiving an annual 5% bonus** – The bonus is based on the amount used to calculate your lifetime income guarantee. It is applied in any year you haven’t taken a withdrawal. Bonus features vary by company but are typically only paid in the first 15 years of the contract.

2. **By locking in market gains every 3 years** – If your investments have gone up in value after 3 years, the amount used to calculate your income guarantee will be based on this value — and never drop below it. This reset feature continues even after you begin making withdrawals.
6. You start making guaranteed income withdrawals

At a specified age, typically around 65, you begin making annual income withdrawals. While these withdrawals decrease the market value of your investments, they do not change the amount used to calculate your annual income guarantee.

7. Your beneficiaries receive the market value

At your death, your beneficiaries receive the market value of your investments.

The Main Points of the GMWB

GMWB products are complex and can vary significantly among insurance companies. Understand all the product features and fees before you buy.

1. Guaranteed income for life
2. Potential to increase guarantee
3. Protection against market declines
4. Potential payment to beneficiaries
5. High fees
6. Restrictions on investment options
7. Penalties for excess withdrawals

REVERSE MORTGAGES

If you’re like many other 55+ Canadians, much of what you own fits into two categories—the equity in your home and the money you’ve saved. Chances are, the value of your home has grown over the years and makes up a good portion of your net worth. While having a home that has built value is a positive, you typically can’t spend that value unless you sell it. And that’s something many homeowners simply do not want to do.

More Canadians are tapping the value of their homes to make ends meet as they head into retirement. Is it a good idea?

It’s an open secret that many older Canadians are heading into retirement with either too much debt, or not enough savings, or both.

It’s a deadly combination because as they leave the workforce their income drops but the debt remains. Many are having trouble managing it and living a stress-free life.
Some homeowners in this position wonder whether a reverse mortgage is the way to go. It allows them to take money out of their home but continue to live there. If they bought decades ago, they’ve got lots of equity. A reverse mortgage can ease their financial pressure with something left over to live a little, renovate, or maybe give their kids an early inheritance.

A good idea? The answer is yes, in some cases. But it should come after all other avenues have been exhausted.

Reverse mortgages carry a higher rate of interest than a conventional mortgage. They run down your biggest asset, which you might need to sell later to live on. If you are prepared to overlook this, you are probably under financial pressure. If the reason is poor money habits, you may just be delaying the inevitable unless you change your ways.

Reverse mortgages are available in most urban areas and are offered on most standard property types (house, townhouse, condo etc.), provided that the home being mortgaged is the borrower’s primary residence. These loans can be paid off at any time, although there are stiff penalties if you break your mortgage in the first two years of the contract.

While real estate investments have served boomers well over their lifetimes, with steadily appreciating values and tax-free capital gains, this asset class is also relatively illiquid and has a future that some fear may not be as bright as its past.

That said, a reverse mortgage is still an expensive way to borrow money and, in many cases, may not be the best option on the table when emotional factors like selling the family home are excluded.

The following information will explain how reverse mortgages work and outlines the strengths and weaknesses of this option.

**Eligibility for a reverse mortgage**

To be eligible for a reverse mortgage, you must be:

- a homeowner
- at least 55 years old

If you have a spouse, both of you must be at least 55 years old to be eligible.
Qualifying for a reverse mortgage

To get a reverse mortgage, your lender will consider:

- your home equity
- where you live
- your age
- your home’s appraised value
- current interest rates

In general, the older you are and the more home equity you have when you apply for a reverse mortgage, the bigger your loan will be.

Accessing money with a reverse mortgage

You may choose to get the money from your loan through:

- lump-sum payment
- planned advances, giving you a regular income
- a combination of both options

You must first pay off any outstanding loans that are secured by the equity in your home with the funds you get from your reverse mortgage.

You can use the remainder of the loan for anything you wish, such as:

- pay for home improvements
- add to your retirement income
- cover healthcare expenses

Repaying the money you borrow with a reverse mortgage

You don't need to make any regular payments on a reverse mortgage. You have the option to repay the principal and interest in full at any time.

Interest will be charged until the loan is paid off in full. The interest will be added to the original loan amount, which increases the loan amount over time.

If you sell your house or if you move out, you'll have to make payments. When you die, your estate will have to repay the loan.
Costs to get a reverse mortgage

Costs associated with a reverse mortgage may include:

- higher interest rate than for a traditional mortgage
- a home appraisal fee
- a closing fee
- a prepayment penalty if you sell your house or move out within 3 years of getting a reverse mortgage
- fees for independent legal advice

Shop around and explore your options before getting a reverse mortgage.

Compare the costs and impact of the following:

- getting another type of loan, such as a line of credit or credit card, etc
- selling your home
- buying a smaller home
- renting another home or apartment
- moving into assisted living, or other alternative housing

Make sure your clients understand the terms and conditions of the contract before they sign it.

Where to get a reverse mortgage

Two financial institutions offer reverse mortgages in Canada:

- HomEquity Bank offers the Canadian Home Income Plan (CHIP). It is available across Canada directly from HomEquity Bank or through mortgage brokers
- Equitable Bank offers the PATH Home Plan. It is available through mortgage brokers in Alberta, British Columbia and Ontario

Your financial institution may offer other products that might meet your needs.

Pros and cons of a reverse mortgage

Before you decide to get a reverse mortgage, make sure you consider the pros and cons carefully.
Pros

- You don't have to make any regular loan payments
- You may turn some of the value of your home into cash, without having to sell it
- The money you borrow is a tax-free source of income
- This income does not affect the Old-Age Security (OAS) or Guaranteed Income Supplement (GIS) benefits you may be getting
- You still own your home
- You can decide how to get the funds

Cons

- Interest rates are higher than most other types of mortgages
- The equity you hold in your home may go down as the interest on your loan adds up throughout the years
- Your estate will have to repay the loan and interest in full within a set period when you die
- The time needed to settle an estate can often be longer than the time allowed to repay a reverse mortgage
- There may be less money in your estate to leave to your children or other beneficiaries
- Costs associated with a reverse mortgage are usually quite high compared to a regular mortgage

Questions to ask a lender about reverse mortgages

Before getting a reverse mortgage, ask your lender about:

- the fees
- any penalties if you sell your home within a certain period
- how much time will you or your estate have to pay off the loan’s balance if you move or die
- what happens if it takes your estate longer than the stated time period to fully repay the loan when you die
- what happens if the amount of the loan ends up being higher than your home’s value when it's time to pay the loan back

Sample Reverse Mortgage Interest Rates

For all provinces outside Québec, the following is a summary of the current CHIP Reverse Mortgage interest rates and terms offered by HomEquity Bank effective January 2018
<table>
<thead>
<tr>
<th>term</th>
<th>interest rate</th>
<th>closing and administrative costs</th>
<th>Annual Percentage Rate (APR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
<td>5.74%</td>
<td></td>
<td>6.02%</td>
</tr>
<tr>
<td>6 Month</td>
<td>5.64%</td>
<td>$1,795</td>
<td>5.91%</td>
</tr>
<tr>
<td>1 Year</td>
<td>5.64%</td>
<td></td>
<td>5.91%</td>
</tr>
<tr>
<td>3 Years</td>
<td>5.84%</td>
<td></td>
<td>6.12%</td>
</tr>
<tr>
<td>5 Years</td>
<td>6.24%</td>
<td></td>
<td>6.53%</td>
</tr>
</tbody>
</table>

Notes to previous table:

1 These fees may vary based on individual circumstances.
2 APR is the estimated cost of borrowing for 5 years expressed as an annual percentage. It is based on a mortgage of $150,000 and includes the applicable closing costs.
3 Variable refers to the HomEquity Bank Prime Rate plus a fixed spread of 2.29%. The fixed spread is guaranteed for 5 years. For contract 21-30, the variable rate is 6.14%

VIATICAL /LIFE SETTLEMENTS

The need for additional financial resources for our aging population during retirement and the ever-increasing government costs for healthcare has never been more important.

The financial struggle of seniors is well documented, and their plight is destined to get worse before it gets better. According to a recent CIBC report, future generations can also expect to face a “steep decline in living standards … and see a 30-per-cent decline in their standard of living upon retirement.”

To put it another way, government purse strings will be affected by aging. More people will be looking for pensions, and fewer people (again, relatively speaking) will be paying taxes.” We are at a tipping point. For example, with Ontario’s senior population going beyond the 15% “balance” that she warns of – heading to 23% – it is a convergence of costs and time with little relief in sight. We are getting older and poorer, faster.

in a February 21, 2015 column in Globe and Mail, Financial freedom is just $4.5 million away, a price tag on financial freedom in Canada, which was based on the annual median income for a Canadian family of $74,000 after-tax [i.e., unsecured debt of $69,000 equals a year’s income]. It was stated that freedom would cost, roughly $4.5 million. This compares to $1.4 million twenty years ago.
In fact, for most, there is no route at all. And $4.5 million is a mountain that many seniors and many in the economically stagnating middle class will never climb.

The assumption that if people just save more then everything will work out is a fallacy. How long can we work? How much can we save, even with a Tax-Free Savings Account (TFSA)? And how can you contribute more to RRSPs if you have less?

As a 2012, BMO Retirement Institute Report stated: “At a time when it is expected that individuals will have accumulated sufficient assets to carry themselves throughout their retirement years, the increase in the bankruptcy rate of Canada’s aging population is of concern … Boomer’s retirement security is in severe jeopardy.”

One option to look at might be Viatical Settlements if the individual has a serious health problem and wants to add to the quality of their lives during retirement.

A Viatical Settlement is a contract made between a terminally ill individual (known as the viator) and a third party whereby the third party agrees to buy the terminally ill person's life insurance policy at a steep discount for readily available cash.

Also known as "viatication", "spin-life", a "transferrable insurance policy", "life settlement", or STOLI (stranger originated life insurance), a viatical settlement is an option for those who lack the funds to continue paying their medical bills and wish to buy themselves a few more months or years.

With a life settlement, an investor agrees to maintain the premiums while also offering policyholders a fair bit more than they would get from a life insurance company—roughly three times the cash surrender value.

**What is the difference between life settlements, “viatical” and “STOLI?”**

Often the term life settlement is co-mingled – and confused – with these but they are different. We have briefly described the terminology here.

**Life Settlement**

A life settlement is different from a viatical settlement in that the individual insured on the policy has a longer life expectancy. It is like a viatical in that a life settlement pertains to the sale of an unneeded in force life insurance policy for an amount that is more than the policy’s cash surrender value but less than its death benefit. In a life settlement transaction, the policy owner is usually at least 65 and
not terminally or chronically ill. The individual sells the policy to a third party and the third party becomes the new owner of the policy, pays the monthly premiums, and receives the full benefit of the policy when the insured dies.

Viatical (from the Latin “Viaticum”, from via meaning “way”):

A viatical settlement typically is used for a settlement involving an insured who is terminally or chronically ill and pertains to the sale of a policy owner’s life policy to a third party for more than its cash surrender value but less than its net death benefit. The sale provides the policy owner with a lump sum payment. The third party becomes the new owner of the policy, pays the monthly premiums, and receives the full benefit of the policy when the insured dies. In a viatical settlement, the life expectancy of the insured is generally 24 months or less. As medical advancements have made progress in the lives of those living with AIDS and other life-threatening illnesses, viatical settlements have become less common.

STOLI (stranger originated life insurance):

STOLI generally means that at or prior to the issuance of a policy an arrangement is made to initiate a life insurance policy for the intended benefit of a person who, at the time of policy origination, does not have an insurable benefit in the life of the insured. The main characteristic of a STOLI transaction is that the insurance is purchased solely as an investment vehicle rather than for the benefit of the policy owner’s beneficiaries. This is quite different from a life settlement.

Not all Provinces allow Viatical

Currently life settlements (formerly known as viatical settlements) are permitted in Quebec, Saskatchewan, Nova Scotia and New Brunswick. The legislation preventing life settlements in the rest of the country typically characterizes this practice as “trafficking in insurance.”

But even in provinces permitting third-party life settlements, life insurance companies have generally adopted very strict policies prohibiting their agents from engaging in or even discussing life settlements. Frequently they threaten cancellation of their agents’ contracts if they do so.
Related Viatical Terms and Acronyms

Accelerated Benefit Option

An option that allows the insured to receive insurance benefits before they would ordinarily be available.

Financing Entity

An entity that purchases an insurance policy or settlement contract.

Living Benefits

The option for a life insurance policyholder to receive a portion of their death benefit in advance of their death.

Loss Payee

An entity that is legally entitled to the benefits of an insurance claim.

Policy Loan

A loan where a life insurance policyholder's death benefit is used as collateral.

Spin-Life

A financial industry that specializes in buying life insurance policies from individuals or convincing individuals to take out new life insurance policies with an investor as a beneficiary.

Surrender Charge

A charge levied when a life insurance policyholder cancels his or her policy.

Surrender Rights

The contractual right for a life insurance or annuity policyholder to cancel his or her policy.

Viator

A person who agrees to sell his or her life insurance policy to a third party.
EMPLOYER SECTOR

CORPORATE RETIREMENT SPONSORED PENSION PLANS

Types of Corporate Retirement Plans

- Defined Benefit
- Defined Contribution

  - Final Average
  - Career Average
  - Money Purchase
  - Group RRSP
  - Group DPSP
  - Structured RRSP
  - Voluntary RRSP

If your clients / prospects have a corporate sponsored retirement plan, it will probably be a variation of the above examples.

AN OVERVIEW OF PENSION PLANS IN CANADA, AS OF JANUARY 1, 2016

- Membership in registered pension plans (RPPs) in Canada totalled 6,262,000 in 2015, up 4,900 members compared with 2014.

- Membership in public sector pension plans increased by 16,500 to 3,229,000. Meanwhile, the number of members in private sector plans fell by 11,600 to 3,032,000. The public sector accounted for 51.6% of total RPP membership in 2015.

- RPP membership moved closer to gender equality in 2015. The number of men with an RPP rose 3,500 to 3,141,000, representing 50.2% of the total, while the number of women with an RPP rose 8,400 to 3,121,000, a second consecutive record high.
• Both men and women saw lower membership counts in the private sector, while there were gains in the public sector compared with a year earlier. Women accounted for 63.1% of the members in public sector plans in 2015 and 35.7% in the private sector.

• The pension coverage rate, or the proportion of all employees covered by an RPP, edged down from 38.1% in 2014 to 37.8% in 2015. The pension coverage rate for women (39.5%) was higher than the rate for men (36.2%) in 2015, and these rates were both down slightly from a year earlier.

• In 2015, 4,204,000 employees were members of defined benefit pension plans, down 4.0% from 2014. Defined benefit plans accounted for 67.1% of employees with an RPP in 2015, down from 70.0% in 2014 and down from a rate of over 90% in the 1980s.

• Membership in defined contribution plans, the next most common type of plan, increased 2.8% to 1,128,000 in 2015, accounting for 18.0% of all RPP membership. Most members in defined contribution plans (87.1%) worked in the private sector.

• Membership in other plan types, excluding defined benefit and defined contribution, such as hybrid, composite and defined benefit / defined contribution plans, grew 19.3% in 2015. There are now 930,000 people belonging to plans not classified as the conventional defined benefit or defined contribution models. Membership in these other plan types has more than quadrupled in the past decade.

• Total employer and employee contributions to RPPs rose 5.9% from 2014 to $67.2 billion in 2015. Employer contributions for unfunded liabilities accounted for $11.4 billion of the total compared with $10.2 billion in 2014. When payments for unfunded liabilities are excluded, employers contributed 60.0% of the total, while employee contributions accounted for the remaining 40.0%.

• The market value of assets in RPPs rose 3.0% from 2014 to $1.71 trillion in 2015. Of these assets, 55.2% were held in large plans with 30,000 or more members. There were 32 such plans in 2015, accounting for 50.0% of total membership.
REGISTERED PENSION PLANS (RPP’s)

A Registered Pension Plan is an arrangement by an employer or a union that provides pensions to retired employees through periodic payments. Essentially, RPPs are the standard pension fund that many employees receive as part of their job. It is a group plan where your employee contributions are withheld at source from your pay and often matched — in whole or in part — by your employer. The plan is managed by a financial institution chosen by the employer, the union or both.

If you are a participant in an RPP, you can deduct your employee contributions from your income on line 207 of your return. The income earned by the plan is not taxable and you are not required to report it.

However, when you retire and begin to receive benefits from the plan, you will then need to include these payments in your income for the year when they are received. Declare this income on line 130 of your tax return.

A registered pension plan (RPP) is a pension plan that has been set up by your employer, and registered by us, to provide you with a pension when you retire.

RPP amounts can include:

- contributions for current service
- contributions for past service for 1990 or later years
- contributions for past service for 1989 or earlier years while a contributor
- contributions for past service for 1989 or earlier years while not a contributor

You can deduct the total of your RPP contributions for current service, or for past service for 1990 or later years, on your 2017 income tax and benefit return. However, you cannot carry forward the amount not deducted to 2018 or later years.

In some cases, you may be able to deduct for 2017 only part of the past service contributions you made for 1989 or earlier years. If this applies, you can carry forward the amount not deducted to 2018 or later years.

Pension benefits you earn on a past-service basis for 1990 or later years may cause a past-service pension adjustment (PSPA).
DEFINED BENEFIT PLANS

A plan that provides a pension that is generally calculated based on final average or best average earnings and years of service. The amount of defined benefit pension that can be provided under a plan registered under the Income Tax Act is limited, in general terms, to the lesser of 2 per cent of the employee's best average earnings and $2000 (indexed) per year of service.

To meet this obligation, the company must invest wisely so that it has the funds to pay the promised benefits. The company bears the investment risk because it has promised to pay employees a fixed benefit and must make up for any investment losses.

For these reasons, defined benefit plans have been the choice of most workers, especially union members.

More recently, along with some of the other potential challenges that come with mergers and amalgamations, many employers are attacking defined benefit plans, and proposing less secure, inferior alternatives in the form of money purchase plans (or worse yet, group RRSPs or nothing at all!). In money purchase plans, employers and employees contribute at a certain level (a percentage of earnings); with these contributions to be invested during an employee's work life.

The total amount of money accumulated in an individual's account will be used to "purchase" a monthly retirement income (e.g. an annuity). No one knows what this monthly income will be, and in fact, the cost of annuities fluctuates dramatically each year with changes in interest rates, inflation rates, etc. In other words, with a money purchase plan, the employer is only committed to a predetermined contribution level and will not guarantee any level of retirement wage.

An easy way to remember Defined Benefit plans

A defined benefit RPP is like going into the gas station for gas. You tell the attendant that you want $20.00 worth, so therefore you are going to know how much gas you are going to get.

These types of plans provide for a Guaranteed Retirement Benefit. A defined benefit RPP provides for a specified pension benefit unrelated to market or economic contributions.
Advantages of Defined Benefit Plans

- Guaranteed retirement income security for workers
- No investment risk to participants
- Cost of living adjustments
- Not dependent on the participant’s ability to save
- Tax deferred retirement savings medium

Disadvantages of Defined Benefit Plans

- Difficult to understand by participant
- Not beneficial to employees who leave before retirement

DEFINED CONTRIBUTION (MONEY PURCHASE PLANS) - DCRPP

DC plans are often called money purchase plans, since the money in the account will often be used to purchase an income option at retirement.

Under a Defined Contribution Registered Pension Plan (DCRPP), the contributions to the plan are pre-determined, whereas the benefits are not. Employer contributions are mandatory; a DCRPP can be set up with the employee either contributing or not contributing. DCRPPs are formal plans that must abide by pension legislation. They are creditor proof, create a pension adjustment, and are designed to provide monthly retirement income for the employee. The pension benefits from a DCRPP depend on several factors, like contribution amounts, number of years enrolled in the plan and the performance of the fund investments.

DCRPPs are surpassing the Defined Benefits Plan in popularity since they provide the employer with more flexibility and certainty in terms of planning and sustaining the pension costs.

Defined Benefit Plans require the employer to fund any shortcomings in the plan, but with Defined Contribution Plans, you are only responsible for making the pre-determined contribution.

Since payments to DCRPPs are fixed, your monthly expenses are easier to calculate. You always know how much you will need to make your contributions.

In 1996, a change in legislation provided additional deductions under certain circumstances for contributions with respect to service before 1990. Members of RPP’s should be able to obtain details of their deductible contributions from their employer or pension administrator.
Depending on the type of RPP, member contributions will be used directly or indirectly by the employer in computing the individual's "pension adjustment". This pension adjustment is a limiting factor in determining an individual's maximum RRSP deductible contribution for the next calendar year.

**Employee-directed investments in DC plans**

More and more DC plans allow employees to select investments for defined contribution accounts. Usually, the employer selects the basket of investment funds from which the employee may choose.

**Employer contributions**

In a DC plan, the amount the employer contributes is specified by the pension plan. Usually, these contributions will be equal to a certain percentage of the employee's earnings. The employer makes these contributions to the fund each month.

The provisions of the Canada Income Tax Act require employers to contribute at least 1% of the employees' salary for the plan to be recognized as a registered retirement plan.

**Investment fund selection**

Since the amount of an employee's pension will be affected by how successfully their contributions are invested, it is important that they make informed investment decisions.

Although the legislation does not specify what information and investment options they should receive, *it is prudent that an administrator provide them with at least the following:*  

- sufficient information to make informed investment decisions  
- investment options that provide diversification  
- regular statements that show how investments are performing

**Participation in the plan**

In most provinces an employee's eligibility is mandatory once he/she has earned 35% of the maximum pensionable earnings during the year of his/her application. The employer will inform an employee as soon as he/she becomes eligible.
The choice of eligibility and enrolment are left to the discretion of the plan provided these requirements meet minimum pension legislation.

**Plan registration**

A defined contribution plan must be registered with the provincial body in charge of monitoring pension plans (or the Office of the Superintendent of Financial Institutions (OSFI) in the case of employers governed under Federal legislation) and the Canada Revenue Agency. Insurance companies will ensure that the necessary registration is completed.

Subject to the maximums established under the Income Tax Act, contributions to a defined plan are tax deductible if the plan is registered with the Canada Revenue Agency.

**Contributions to a defined contribution plan**

The total of the employee, employer and voluntary contributions cannot exceed the lesser of the following amounts:

- The defined contribution limit for the year as determined under the Canada Income Tax Act, and
- 18% of the employee's salary determined under the plan.

Defined contribution plans are gaining in popularity because they are easier to understand and administer than a defined benefit pension plan.

**Contributions are "locked in"**

"Locked in" means the money in the employee's account cannot be removed prior to retirement. This is a big advantage over Group Registered Retirement Savings plans where often employees cannot resist their access to cash for some personal expenditure.

**Retirement income options**

There are several retirement income options to choose from. The amount in each income option will depend on factors such as:

- The amount of money in the investment account upon retirement
- The interest rate at the time of retirement
Features and Advantages of a DCRPP

Lower Payroll Taxes

Contributions to a DCRPP are not subject to Canada Pension Plan, Employment Insurance or any other applicable provincial payroll taxes.

Employee Retention

Employees may become vested after as many as 24 months of plan membership.

Contributions Are "Locked In"

Contributions to a DCRPP are 'locked-in' until retirement. Because the funds are only available upon retirement, the plan may engender more of a long-term commitment to your company.

Easy to Understand

DCRPP contributions are defined. The employee can always see what their current pension benefit is.

Creditor Protection

Creditors cannot seize registered Pension Plan contributions.

Additional RRSP Contributions

A DCRPP allows continued contributions to an individual RRSP, up to the allowable annual limit. The contributions of the employee and employer to the DCRPP in the previous year will create a pension adjustment in the current year.

Required Employer Contributions

Employer contributions are mandatory; employee contributions are optional, depending on the plan.

An easy way to remember Defined Contribution plans

Defined contribution type of plans is like going into the gas station and telling the attendant to fill it up, and you pay for it by credit card. You do not know how much gas you are going to get until he fills up the tank.
These types of plans provide a lump sum accumulation benefit, and when you retire, you buy your income at that time.

How does the defined benefit (DB) pension plan model compare against the defined contribution (DC) pension plan model?

A comparison of Defined benefit vs. defined contribution at a glance

<table>
<thead>
<tr>
<th></th>
<th>Defined Benefit (DB)</th>
<th>Defined Contribution (DC)</th>
<th>The DB Advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Philosophy</td>
<td>To provide members with lifetime retirement income.</td>
<td>To help individuals accumulate retirement savings during their active career.</td>
<td>The security of regular monthly income rather than savings.</td>
</tr>
<tr>
<td>Contributions</td>
<td>Typically, members and employers contribute a set percentage of the member’s salary.</td>
<td>Typically, individuals and employers contribute a set percentage of the individual’s salary.</td>
<td>In most DB plans, employers shoulder the investment risk.</td>
</tr>
<tr>
<td></td>
<td>Member and employer contributions are invested in a pension fund and used to pay the member’s lifetime pensions.</td>
<td>Monies are deposited in a personal account set up in the individual's name.</td>
<td>Under a DC plan, the individual takes on all the investment risk.</td>
</tr>
<tr>
<td>Investment Decisions</td>
<td>Professionals manage all investments based on strict guidelines established to protect plan members.</td>
<td>Individuals decide how their money is invested, usually based on a range of available investment options.</td>
<td>With a DB plan, members don't have to worry about making investment decisions or tracking investments because a highly qualified investment professional is doing it for them.</td>
</tr>
<tr>
<td>Income at retirement</td>
<td>Pension income is based on earnings and service in the plan — the more service, the bigger the pension will be.</td>
<td>The money in the individual’s account is used to buy an annuity or transfer to a RRIF (a monthly income stream).</td>
<td>With a DB plan, members can estimate, in advance, what their pension will be. Benefits are pre-defined - members know what they are going to receive.</td>
</tr>
</tbody>
</table>
Ancillary benefits

| Many DB plans, offer additional benefits such as: |
| inflation protection |
| early retirement benefits |
| survivor benefits |
| disability benefits |

| At retirement, individuals may be able to buy a lifetime annuity that includes some additional benefits such as inflation protection — but these extras tend to be expensive, which reduces the amount they'll have available to provide an income stream. |

| With a DB plan, the additional benefits are built in and members don't have to worry about the additional cost of shopping around or an annuity that includes them. |

### DEFERRED PROFIT SHARING PLANS (DPSPs)

DPSPs can be used as a pension plan or as a supplement to a company's Group RRSP. Like a registered pension plan, a deferred profit sharing plan must be registered with Revenue Canada and must comply with the terms and provisions of the Income Tax Act and regulations.

The employer may contribute an amount "out of profits," or related to profits, into a trust fund that will accumulate sheltered from income tax. The employer's contributions are tax deductible and are not taxable to the employee until paid out. Employee contributions are not permitted. Employer contributions must be considered in computing the individual's pension adjustment amount used in establishing the following year's RRSP limit.

Amounts allocated to a member's account must vest to the member after two years of membership in the plan, or earlier if the plan allows for it.

Any non-vested amount forfeited by a terminating employee must either be allocated to other plan members or refunded to the employer no later than the end of the year following the year in which the amount was forfeited.

### Features and Advantages of a DPSP

1. **Opportunity to thank employees**

   Sharing company profits usually instills a sense of company ownership which may have spin-off benefits: higher efficiency, higher morale, and higher profits.

   This plan can be used to retain key employees. The vesting provision helps retain staff and reduce turnover.
2. **Flexibility**

There is no defined formula to DPSPs, so contributions can be tailored to better reflect business revenues, market conditions, or other intangible factors.

The company is not obliged to contribute, so the amount and frequency are left to the discretion of the employer.

3. **Cost effectiveness**

Employer contributions are exempt from federal payroll taxes, including CPP, EI and other applicable provincial payroll taxes. This may help you offset plan costs. DPSPs are a perfect complement to a voluntary group RRSP.

Unlike pension plans, which are provincially regulated and governed by the Pension Benefits Act, DPSPs are registered with the Canada Customs and Revenue Agency and governed by the Income Tax Act.

Unlike a Group RRSP or pension plan, only employer contributions are allowed under a DPSP. Most employers use a DPSP as a complement to a non-contributory Group RRSP - i.e. an RRSP with no employer contributions.

**Note**

Connected persons are not eligible to participate in DPSPs.

Employer contributions into a DPSP are limited to the lesser of 18% of the employee’s compensations of the year from the employer or a dollar limit equal to one half of the defined contribution pension plan limit as follows:

Deferred Profit Sharing Plans are not regulated by pension legislation but are registered under and must comply with the Income Tax Act.
A DPSP may provide that, on election by the beneficiary, all or any part of the amounts payable to the beneficiary may be paid:

- S. 147(2)(k)(v) in equal instalments payable not less frequently than annually over a period not exceeding 10 years from the day on which the amount became payable, or
- S. 147(2)(k)(v) in equal instalments payable not less frequently than annually over a period not exceeding 10 years from the day on which the amount became payable, or
- 147(2)(k)(vi) to a licensed annuities provider to purchase an annuity for the beneficiary, where:
  - annuity payments begin no later than the end of the year in which the beneficiary attains 71 years of age, and
  - the guaranteed term, if any, of the annuity does not exceed 15 years.

DPSP lump sum payments can be transferred tax-free to an RPP, RRSP, or RRIF

**Deductible Contributions**

The amount that can be deducted as an annual contribution to a money purchase RPP and a DPSP is subject to a limit. There is no limit for contributions to a defined benefit RPP for which the maximum benefits are limited.

**From 2017 to 2019, the limits are:**

<table>
<thead>
<tr>
<th>Year</th>
<th>Benefits limit – defined benefits RPP</th>
<th>Contribution limits</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Money purchase RPP</td>
</tr>
<tr>
<td></td>
<td></td>
<td>DPSP</td>
</tr>
<tr>
<td>2017</td>
<td>2914</td>
<td>26010</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$13115</td>
</tr>
<tr>
<td>2018</td>
<td>$2944</td>
<td>$26,230</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$13250</td>
</tr>
<tr>
<td>2019</td>
<td>$1/9 Money purchase limit</td>
<td>26500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>½ money purchase limit</td>
</tr>
</tbody>
</table>
Characteristics of RPPs and DPSPs

Each of these plans has its own specific tax characteristics, which are summarized in the following table:

<table>
<thead>
<tr>
<th>Characteristics of RPPs and DPSPs</th>
<th>Defined benefit RPP</th>
<th>Money purchase RPP</th>
<th>DPSP</th>
</tr>
</thead>
</table>
| Payment of contributions         | • Employer and employee; or  
                                 | • Employer only     | • Employer only |
| Maximum annual contributions     | • Based on actuarial needs  
                                 | • No annual limit 5  | Lesser of:  
                                 | Lesser of:           | Lesser of:           |
|                                  | 18% of income        | Annual limit       | • 18% of income |
|                                  | Annual limit         |                    | • Annual limit |
| Retirement benefits              | • Predetermined amount  
                                 | • Maximum benefits limit  
                                 | Determined based on amounts invested in name of employee and pension fund’s returns during life of plan |
|                                  | applicable per years of service | | • Based on amounts invested  
                                 | | • Lump-sum withdrawal allowed (unlike RPP) | |
| Deductibility of contributions   | Fully deductible for payer | Deductible in accordance with annual contribution limits | Fully deductible for employer |

EMPLOYEE STOCK OPTION PLANS (ESOP)

An Employee Share Ownership Plan (ESOP) allows employees, who qualify, to purchase shares in their employer’s company, with or without the monetary assistance from the company.

Employees can acquire shares and ownership through an ESOP that can range from one percent to 100 percent. The key aspect is that employees have an ownership stake in the company they work for, and share in the risks and rewards that accrue to it.
The use of equity compensation as an incentive to improve employee performance has come under much scrutiny in the recent past. Notably, Microsoft's announcement in mid-2003 to replace their stock option plan with a restricted stock scheme, and changes to the general accounting rules that deal with employee option benefits are just two examples of how the landscape in equity compensation is changing.

Many factors need to be considered when an organization is designing and implementing an effective incentive plan for employees including the personal-tax questions raised by such plans.

In this section we will review the implications of the various equity compensation alternatives utilized by the corporate community. The plans discussed include stock options, restricted stock and employee stock purchase plans. Phantom stock plans will also be discussed.

Stock Option Plans

For Canadian income tax purposes, the granting and vesting of employee options do not result in any immediate tax consequences for employees. An employment benefit equal to the difference between the fair-market value at the date of exercise and the exercise price will generally result at the date of exercise. There are exceptions to this timing however.

If the options are granted by a Canadian Controlled Private Corporation ("CCPC"), then any employment benefit is automatically deferred until the year the optioned shares are disposed of. A CCPC is generally a non-public company that is not controlled by a public company, non-resident or any combination of the two. Within limits, and provided certain conditions are met, an employee may also opt to defer the resulting employment benefit on public company stock until the year of disposition.

Four key points are worth highlighting:

1. Deferral of the option benefit is only available if the employee holds the shares after exercising. Many employees exercise and sell right away. Of course, the deferral would not be available in such circumstances.
2. The option benefit is fixed as at the date of exercise based on the fair market value at that date. The deferral of the benefit to another year will not affect the amount of the benefit, only the timing.
3. The employment benefit is added to the adjusted cost base of the shares. Any fluctuations in the fair-market value of the shares after exercise will result in either a capital gain or loss in the year the shares are disposed of.
4. Finally, if the employee becomes a non-resident, any option benefit on public company stock that is deferred, must be reported and taxed in the year of departure from Canada.

Deduction entitlements equal to 50 per cent of the option employment benefit resulting from the option exercise are available.

To qualify, certain criteria must be met by the employee, including the condition that the amount paid to acquire the shares was not less than the fair-market value of the shares when the option was granted. To meet the criteria for a 50-per-cent deduction on CCPC option benefits, it is not necessary to meet this condition provided the shares acquired pursuant to the option agreement are held for at least two years before being disposed of.

With respect to the stock option deduction five points are also worth highlighting

1. It is the employer's responsibility to ensure that both the employment benefit and the deduction are reported appropriately on the T4 supplementary issued to the employee. The employer's withholding obligations must also be considered.
2. One hundred percent of the employment benefit, which is added to the employee's adjusted cost base of the shares, is used for determining any capital gain or loss on a subsequent disposition of the shares.
3. The stock-option deduction, in effect, taxes the employee in a similar manner to a capital gain, which is 50-per-cent taxable. It is important to note, however, that the option-employment benefit is not a capital gain and, therefore, cannot be reduced by capital losses experienced by the employee.
4. Changes an employer makes to the stock options granted to employees may adversely affect the employee's entitlement to claim the stock option deduction. Such changes could include re-pricing and exchanges for other options or consideration.
5. The availability of the 50-per-cent stock-option deduction makes this type of equity compensation very attractive to the employee.

Restricted Stock Plans

Equity compensation plans that include the awarding of shares by an employer to an employee that are subject to certain restrictions are referred to as restricted stock plans. The employee receives legal title and assumes most other risks and benefits of ownership at the award date but is generally subject to restrictions with respect to selling, voting, and/or pledging of the shares.
The restrictions are normally eliminated over time provided the individual remains employed with the company.

The employment benefit is generally calculated when the employee has many of the rights and benefits of ownership; namely, on the date the restricted stock is awarded. The taxable employment benefit is equal to the fair-market value of the stock at that date.

For shares of non-CCPCs, the fair market value is included in the employee’s income at that time. For CCPCs, the benefit is automatically deferred until the year the shares are disposed of like the deferral under stock option plans. There is no 50-per-cent stock benefit deduction for non-CCPC share awards since the conditions for such a deduction cannot be met. In the CCPC situation, the 50-per-cent stock benefit deduction may be available if the shares are held for two years or more before disposal. Again, it is the employer’s responsibility to properly report the employment benefit and, if applicable, the deduction on the employee’s T4 supplementary. Employee withholding responsibilities must also be considered.

A few points that should be highlighted:

1. As previously mentioned, the employment benefit is based on the fair-market value of the stock at date of award. Such stock is not freely tradable at that date. For this purpose, an appropriate discount should be applied in arriving at fair-market value, one that considers the stock restrictions that exist at the date of the award. While there are several methods that may be applicable in determining the appropriate discount, to date, none have been prescribed by the Canada Revenue Agency.
2. Any dividends received before these restrictions are lifted would be treated as dividend income.
3. If at a future date, the employment requirements are not met, and the shares are forfeited, the employee will realize a capital loss equal to the difference between the employment benefit and the proceeds received because of the forfeiture. The resulting capital loss may be applied against capital gains realized in the year.
4. To the extent the capital loss is not utilized in the current year, it can be carried back three years or forward indefinitely to offset capital gains realized in those years. In isolated circumstances for CCPC shares, any resulting allowable capital loss (50-per-cent of the capital loss) may be available to offset other income in the year.
Employee Stock Purchase Plans (ESPP)

What is an ESPP? A compensation plan typically designed to provide employees with a means of purchasing company shares, as well as an incentive for purchasing those shares.

Plans that provide the employee with the option to acquire shares at a discount from the current publicly traded price are generally referred to as employee stock purchase plans.

Such plans are generally more popular with U.S. corporate employers. The resulting benefit is afforded preferential treatment under the U.S. tax system, provided certain conditions are met and the price is not less than the lesser of 85 per cent of the fair-market value on the date of grant and 85 per cent of the fair-market value of the shares on date of purchase.

For Canadian tax purposes, the discount would generally be treated as an employment benefit and included in income when the employee acquires the shares. In the rare situation where a CCPC has an employee stock purchase plan, any purchase discount would generally be included in income in the year of disposition.

Again, to the extent the shares of the CCPC were held for two years or more, the employee may qualify for a stock benefit deduction equal to 50 per cent of the purchase discount.

How does it work? Many companies will offer some sort of financial incentive to purchase shares; two of the most common incentives are contribution matching and discounts.

Contribution matching is where an employer will fund a portion of the employee’s contribution. For example, with every two shares an employee buys, the company will buy one share for that employee. Discounts are where the company allows the employee to buy shares at a portion of the actual share price. There are tax stipulations for these plans.

There are two main ways in which a company encourages ESPP contributions. Firstly, regular payroll deductions, which make it easy for employees to schedule contributions in increments that are affordable, and scheduled contribution dates throughout the year, which allow employees to purchase a certain number of shares at regular intervals, i.e., quarterly or annually.
The plans usually require employees to hold the purchased shares for a minimum period, such as one year (referred to as vesting). Requiring a minimum share-holding period encourages retention and ensures employees are not unfairly trading their shares.

**What are the advantages?**

Among the many advantages of offering ESPPs to employees are an alignment of the interests of shareholders and employees, and the organizational pride it instils in employees as they will behave more like owners.

Employees who are shareholders may also feel more commitment and loyalty to their employer, which will likely reduce turnover. And, if employees understand the value of the plan as a long-term investment, it might also reduce turnover.

Another benefit is that the investment is not subject to the transaction or management fees usually charged, as most administrative fees are paid by the employer.

**What are the disadvantages?**

Despite the numerous advantages of ESPPs, employers must also be aware of some disadvantages:

- Professional fees associated with the legal, administrative and tax issues to set up a plan;
- Human resources dedicated to the administration of the plan;
- The cost of the employer’s contribution;
- Ensuring the plan is compliant with security and tax laws; and
- If share price decreases, it can turn into a negative company morale issue.

Companies offering ESPPs to employees have seen the positive effects on attraction and retention of talent. They have also experienced increased employee engagement. Overall, if the plan is set up well from the start, the positive results of an ESPP creates “ownership thinking” among employees, which has a financial benefit for shareholders, the employer and the employee.

**Phantom Stock Plan (PSP)**

Savvy business owners go to great effort to hire the right staff. The inevitable scenario can then arise as to how to retain and motivate those exceptional employees who rise to the top.
Key employees can lose focus and ultimately leave because they have no ‘skin in the game’. At a certain point, a star employee(s) may see more opportunity elsewhere or think that ownership is crucial to being a part of the company’s long-term future. Further bonuses or salary increases may not make sense for the company and/or fail to properly motivate the employee.

From an owner’s perspective, relinquishing control of the company comes with its own set of problems. Adding shareholders can:

- add complexity to the ownership structure;
- make the company less attractive to prospective purchasers; make it more difficult to run the company and
- expose the financial details of the company, which may be sensitive.

Fortunately, there is an alternate option:

**A Phantom Share Plan** (a “PSP”) allows an employee to share in the company’s future growth without the principals giving up ownership in the company.

**What is a PSP?**

A PSP is a contractual arrangement between an employer and an employee, whereby the employee is granted so-called units (also known as phantom shares), the value of which are closely linked to the value of the company. The employer can draft the terms in the PSP to suit its own commercial needs and goals.

PSP’s are not regulated by specific legislation and are basically a contractual bonus scheme. However, unlike stock options, it pays cash instead of shares.

**Generally, PSPs have the following characteristics:**

- Units are issued to an employee that mirror the value of the share equity of the company;
- Units have only the rights provided in the PSP;
- Typically, units have an issuance price that is equal to the fair market value (“FMV”) of the company’s shares at the time they are granted to the employee. The employee does not pay for units received;
- The company redeems units from the employee upon the occurrence of certain triggering events. Triggering events typically include the sale of the business or the death or permanent disability of the employee; and
Employees who have units are generally entitled to two forms of payment:

1. **Distributions**: Employees may receive distributions set at the sole discretion of the company, similar in concept to issuing a dividend; and

2. **Redeeming of units**: Units are redeemed by the company on the occurrence of triggering events as specifically agreed in the PSP. Upon redemption the employee will be entitled to receive the difference between the units’ value on the date that they were granted to the employee and the value of the company’s shares on the date of the triggering event.

**Retaining Key Employees: The Case for Phantom Shares**

For example, assume a company implements a PSP and grants an employee ten (10) units. The PSP states that units must be redeemed by the company if the company is sold.

On the date the units are issued, the company’s shares have a FMV of $5.00 each. Three years later, the company is sold to an unrelated buyer for $12.00 a share.

This is a so-called “triggering event”, and the employee would be entitled to receive $7.00 per unit; the difference between the phantom shares’ grant value and the value of the share at the date of the triggering event.

**Why implement a PSP?**

Employees who receive units under a PSP participate in the future growth of the company. Their goals can now be aligned with the company’s long-term goals in a manner that normal salary and bonuses cannot achieve.

**Benefits for the employer include:**

1. **No transfer of ownership** – A unit is not a share of the company’s stock. Units carry no voting rights and do not dilute ownership of the company;

2. **Customized and simple to implement** – PSPs are a contractual agreement. An owner has flexibility to incorporate terms such as: which employees participate, how many units to issue, when the units are redeemed and what happens to the units if the employee is no longer employed by the company.

3. PSPs avoid a lot of the additional paperwork and complexity associated with issuing actual shares and do not require a shareholder’s agreement;
4. Employee motivation and retention – Employees with units will directly benefit from the success of the company.

5. Minimal Upfront Costs – The only initial cash outlay is the administrative costs to implement the plan; and

6. Deferred taxation – Payments made by the company in relation to the units are treated as employment income for tax purposes and are only taxed when the employee receives payment. Also, if the PSP is properly designed and implemented, an employee will not be taxed for receiving units.

Indicators that a PSP is right for the Company

PSPs can be a powerful source of employee motivation and retention. However, not every company is ideally suited to implement a PSP. Consider these factors to determine whether a PSP is right for your company:

- The company has a small number of shareholders.
- There are a small number of key employees. For a PSP to be effective, the employee who receives units should be integral to the future value of the company. Companies typically only reward management and senior employees who are key to the company’s success and growth;
- The company is increasing its employees’ responsibilities and does not want to increase salaries directly; and
- The company is in good financial position and is likely to continue to grow. A motivational tool is only effective if benefits are likely to be realized.

Conclusions

The personal tax implications of equity compensation plans for employees can be substantially different depending on the type of plan being implemented and the Canadian tax status of the company implementing the plan.

To establish an effective equity compensation plan for Canadian employees, it is important that plan designers be fully aware of the personal tax implications for employees. A plan can then be designed to minimize negative personal tax implications and, hopefully, maximize the positive impact such plans are intended to provide.
The tax results under different scenarios are summarized in this chart:

<table>
<thead>
<tr>
<th>Event</th>
<th>Tax result to employee</th>
<th>Amount included in employee’s income</th>
</tr>
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</table>
| Stock option granted
Option exercised, and shares are immediately sold | - Employment benefit, subject to 50% employee stock option deduction  
- Amount of benefit is added to cost of shares  
- Taxable capital gain or loss should be nil | (Fair market value of shares on date acquired less exercise price of the options) × 50% |
| Option exercised, and shares kept; employee elects to defer the benefit | - Employment benefit, subject to 50% employee stock option deduction, is calculated but not included in income until year of sale  
- Amount is reported on employee’s T4 slip as a deferred benefit  
- Amount of benefit is added to cost of shares | None |
| Shares on which deferral election is made are sold in a later year | - Inclusion of deferred employment benefit, subject to 50% employee stock option deduction, and  
- Taxable capital gain or loss | (Fair market value of shares on date acquired less exercise price of the options) × 50%, and  
(Sale proceeds less cost of shares) × 50% capital gains inclusion rate |
INDIVIDUAL PENSION PLANS (IPPs)

An individual pension plan (IPP) is simply a defined benefit pension plan for one member. IPPs specifically benefit owners of companies or executives of incorporated companies who do not participate in an employer pension plan and who have annual earnings more than $120,000. Ideally, individuals should be 50 years of age to derive the maximum benefits from the plan. However, such plans have been set up by persons as young as 40. The contribution advantage of using an IPP vs. an RRSP increases with age.

These plans can be either 100% funded by the employer or employer/employee-funded. In general, you won’t be able to fund more than 50% of the cost of the pension.

Subject to certain limitations, a defined benefit plan will provide for an annual pension equal to a percentage of your highest earnings over a given period. One of the main benefits of these plans has been the possibility of making significant contributions for past service. They were also promoted on the basis that they could potentially defer the receipt of retirement income for a longer period than was generally possible with other types of retirement plans.

However, for service contributions made after March 22, 2011, the cost of the past service must first be satisfied by transfers from RRSP assets (as well as money purchase registered pension plan assets) belonging to the IPP member or a reduction in the member’s unused RRSP contribution room before new past service contributions are permitted.

Also, the rules now provide for minimum withdrawal amounts from an IPP, like those that currently apply to RRIFs.

These two changes, which were aimed at making IPPs more comparable to other retirement savings vehicles, have eliminated many of the advantages that IPPs have had over other plans.

IPPs are not for everyone. It’s an individual decision based on several factors—your age, current and projected income level, the rate of return earned on the plan’s assets, whether you’re an owner-manager or an arm’s-length executive and several other considerations.

An individual pension plan (IPP) A retirement savings plan that allows bigger tax-deductible contributions than an RRSP.
It is designed for people with higher incomes. It works like a defined benefit plan and must follow Canada’s pension plan rules. Typically, the company makes all contributions.

**Advantages of IPPs**

- **Potential for greater tax-sheltered savings** - The maximum contribution to an IPP each year can exceed the amount an individual can contribute to an RRSP on their own, especially at later ages (age 50 or older).

- **Creditor protection** - Like other DB benefits, IPP benefits are fully protected from creditors. RRSP savings may not be.

**Disadvantages of IPPs**

- **Minimal RRSP contribution room** - IPPs are designed to maximize tax-sheltered benefits, so the individual’s RRSP contribution room each year is reduced to near zero by a pension adjustment (which equals the value of the IPP benefit earned in the previous year).

- **Less flexible retirement income options** - Provincial and federal pension laws apply to IPPs – and can restrict flexibility in retirement income planning.

- **Cost and complexity**: IPPs have higher set up costs and greater complexity than RRSPs, with the need for ongoing administrative tasks such as annual reporting and regular actuarial valuations.

**Maximizing IPP benefits**

To maximize the benefits of an IPP, the owner or executive typically:

- is in their 40s or 50s when the IPP is set up, to ensure that IPP contributions can exceed the amount the individual could save on their own through an RRSP, and
- has a high annual salary ($120,000 or more), so that the company can maximize its IPP contributions.

Because of the complexities of an IPP, you may want to get professional advice to determine if an IPP is an appropriate strategy for you.
Funding IPPs for past service

A company can fund an IPP to provide a benefit for the owner’s or executive’s previous years of employment with the company. However, the cost of this must first come through a transfer of the individual’s RRSP and DC pension plan savings – plus a reduction in any unused RRSP contribution room – before the company can contribute to fund this benefit.

Due to their complex nature, as well as the recent changes to the rules, it’s recommended that you consult your tax or financial adviser if you have any questions as to whether an IPP is a viable retirement savings vehicle for you.

An annual filing with Canada Revenue Agency is required for IPPs. However, in recent years the market for IPPs has become more competitive and the costs associated with establishing and maintaining an IPP have been reduced.

SALARY DEFERRAL ARRANGEMENTS (SDAs)

If an employee is entitled at the end of the year to receive an amount in a future year and one of the main purposes for this arrangement is to defer or postpone taxation, the amount will be taxed as a benefit to the employee in the current year. This is called a salary deferral arrangement.

Some plans are excluded from this classification, such as arrangements to fund certain employee leaves of absence. As well, the rules will not apply to bonuses that are paid within three years following the end of the year in which the amount became payable. However, if the bonus is not paid within 179 days from the end of the employer’s taxation year, the employer will not be able to deduct the amount until the year it’s paid.

Tax tip: If your corporation’s year-end comes after July 6, it can deduct the bonus in the current year and the employee doesn’t have to report the amount as income until the next year. However, the corporation must declare the bonus as of its year-end but not pay it out until after December 31 and within 179 days of the year-end.

Could some corporate pension options be considered a Salary Deferral Arrangement?

Depending on the design and nature of the plan, it may or may not be considered a salary deferral arrangement (“SDA”) for Canadian income tax purposes.
Example of CRA rules on a Phantom Stock Plan for a Canadian wholly-owned subsidiary of a non-resident company... from the CRA 2015 Ruling

CRA provided a ruling (albeit, guarded in its wording), that a phantom stock plan provided by a wholly-owned sub of a non-resident SA to five of its key employees would not be treated as a salary deferral arrangement. Speaking generally, the plan provided that on the occurrence of a “Triggering Event” an employee would receive a cash payment equal to the excess of the “Market Value” of the employer’s shares on the Triggering Event over their Market Value on grant.

Except where the Triggering Event was one which disclosed a value (namely, an acquisition of control, amalgamation, business sale or IPO), the “Market Value” was computed as nine times the average adjusted EBITDA for the previous two fiscal years plus working capital, as adjusted, and minus long-term debt. In addition to the “Material Change” Triggering Events referenced above, a Triggering Event included the employee’s death, departure or retirement, and termination of employment for any reason other than for things like theft.

THE VALUE OF LIFE INSURANCE AS A FUNDING VEHICLE

Many companies use life insurance as a funding vehicle for their retirement plans, and understandably so. By doing so, companies can often recover most of the costs of establishing and maintaining their plan.

Corporate Cash Surrender value from Key Persons Insurance plans, Buy Sell Agreements and Split Dollar plans can be part of a Corporate / Employee Retirement Agreement. It is important to realize that those people looking for tax shelters or deferral avenues should explore the benefits that can be derived from an “exempt” life insurance policy. While professional advice is usually needed, it is to be noted that a substantial portion of the income from such investments may accumulate free of tax. This income can also be used before death, and the proceeds are usually not subject to tax on death. If the insurance is surrendered or loses its “exempt” status, tax may be payable. These policies can be a very useful tool in tax planning.
RETIREMENT COMPENSATION AGREEMENTS (RCAs)

In the right circumstances a Retirement Compensation Arrangement, or RCA, could save you income taxes, provide golden handcuffs, retirement funding and/or help protect your assets.

Typical employee benefits plan’s only address the first $150,000 of employment income and may lack the desired flexibility to create meaningful long-term incentives. RCAs may be helpful solutions for enhancing retirement savings, employee benefits, creating incentives, and funding for employee severance for high income earners.

A Retirement Compensation Arrangement (RCA) represents the highest level of retirement program available in Canada. Defined under section 248(1) of the Income Tax Act, an RCA allows a company to make tax-deductible contributions on behalf of key employees for purposes of retirement to the maximum level allowable.

Eligibility

An RCA is ideally suited for high-income earners ($150,000+) such as business owners, athletes, executives, and incorporated professionals who wish to sustain their standard of living into retirement. The flexibility of the RCA allows it to be adapted to many business and tax strategies. The RCA requires a sponsoring company to set it up.

How an RCA works

A company establishes an RCA to provide retirement benefits for its employees. Deductible contributions are made from the company into the RCA and are held in trust for the beneficiaries.

Funding Methods

Cash funding

The company makes cash contributions to the RCA trust. One-half is used to pay the special refundable tax and the other half is invested. The RCA can loan the after-tax amount back to the company at a reasonable interest rate and with reasonable security. This can be a win-win situation for both parties. The company obtains financing at less than bank rates and the RCA earns interest at better than market rates.
In some cases, arrangements can be made by the RCA to borrow against the refundable taxes and loan the proceeds to the company. In such cases the RCA loan arrangement has significant cash flow advantages over the traditional bonus and loan arrangements entered by many owner–managers.

Insurance funding

The company funds a split-dollar life insurance policy under which the company is the beneficiary of the insurance policy and the RCA is the beneficiary of the investment component or tax-exempt surplus. Special refundable taxes must be remitted equal to the amount of the annual premium attributed to the tax-exempt surplus.

The benefit of this arrangement is that the investment income earned within the insurance policy is tax exempt and not subject to the 50 per cent refundable tax.

As such, the investment compounds at pre-tax rates. The death benefit received by the RCA will be subject to tax unless it is paid out to RCA beneficiaries in the year received. Under this arrangement the RCA funds benefit from policy loans and death benefits received. The fact that these investments are secure from business risks is also attractive.

Funding from future cash flow

The company can undertake to fund the RCA out of future cash flow as the RCA’s benefit obligations come due. This arrangement provides limited current tax benefit to the company and can leave the employees at risk unless the company provides the RCA with some form of security. However, caution must be used when setting the security.

The Canada Revenue Agency holds the view that the company has contributed if it provides the RCA with a letter of credit under which the bank encumbers specific corporate assets. This will result in a refundable tax liability equal to the amount of the encumbrance.

On the other hand, a letter of credit secured by a floating charge on assets will result in a notional contribution equal to twice the annual fee.

As noted earlier, RCAs can be a useful component of a company’s retirement package by providing flexibility and cash-flow benefits.
No required retirement date

Provided there is a change of employment status the member of the RCA may begin withdrawals from their RCA at any age they wish. By the same token, there is no requirement to begin withdrawals at age 71, such as applies to Registered Plans. The assets of the RCA may remain in the Trust Fund throughout the lifetime of the member and may subsequently be used for the benefit of spouses and beneficiaries.

TAXATION OF AN RCA

The employer can generally deduct 100% of their RCA contributions. There is no specific limit to the amount of contributions an employer can make to an RCA, if the amounts are “reasonable” and not excessive relative to the target retirement compensation to be provided.

The Income Tax Act (ITA) also allows tax-deductible contributions by the employee. However, employee contributions cannot exceed those of the employer and the employee must be required, under the terms of employment, to contribute to the RCA.

Reasonable contributions

The Canada Revenue Agency (CRA) may disallow the employer’s deduction for contributions to an RCA if the amount is not “reasonable”. The ITA does not define what is considered reasonable contributions to an RCA. The CRA may take the view that benefits are not reasonable if they are greater than benefits that would be appropriate for the employee’s position, salary and service or where the RCA does not consider benefits that are provided through other registered plans, such as a registered pension plan. Instead, the RCA should provide a normal level of benefits which the CRA described as follows:

“A normal level of benefits would be the same benefit provided under a registered pension plan without regard to the Revenue Canada maximum. This would be 2% x years of service x final five-year average earning or about 70% of pre-retirement income for an employee with 35 years of service.” (CRA Roundtable discussion, 1998)

In other words, the CRA allows the formula generally used for defined benefit pensions to be used for the purposes of determining RCA retirement benefits but ignoring the tax maximums imposed on defined benefit pension plans by the ITA.
This continues to be CRAs position with respect to reasonable contributions to an RCA. A qualified actuary can help you determine a reasonable RCA contribution.

**Refundable Tax Account**

When a contribution is made to an RCA, only half of the contribution is deposited with the custodian of the RCA trust. The other half is deposited with the CRA into the RTA as a payment of the 50% refundable tax. The RTA is a non-interest-bearing account. It accumulates the refundable tax until distributions are made from the RCA. When a distribution is made from the RCA, the CRA will refund some of the tax to the RCA.

In addition, 50% of all income earned and capital gains realized in the RCA trust must be remitted to the RTA on an annual basis. Unlike investment income earned in a personal nonregistered investment account or regular trust account, Canadian dividends and capital gains do not receive preferential tax treatment in an RCA. In other words, the entire capital gain is subject to the 50% refundable tax and the RCA does not receive a dividend tax credit on taxable Canadian dividends.

When the RCA makes distributions to the beneficiary $1 is refunded from the RTA to the RCA trust for every $2 distributed. It is possible to recover 100% of the RTA balance if the RCA is completely paid out to the beneficiary.

**Termination of RCA or death of beneficiary**

The custodian holds the RCA funds with the intent of eventually distributing them to the employee, former employee or other beneficiary on or after an employee’s retirement, loss of an office or employment or any substantial change in the services the employee provides. When one of these triggering events occurs, depending on the design of the RCA plan, distributions can be made either periodically or in a lump-sum.

RCAs are generally more flexible than registered pension plans and other types of registered plans in terms of when and how much can be paid out of the plan to the beneficiary.

For example, you do not necessarily have to start taking payments out of an RCA when you turn a certain age especially if you are still working for your employer and there has not been a substantial change in the services you provide to them.
Compare this to a registered pension plan or an RRSP which must start an income stream to the plan member or annuitant after the year in which they turn 71.

Examples of some situations where the RCA may be terminated, in accordance with the RCA agreement, is when you sell your business before your planned retirement age and your business sponsored an RCA for you, if you leave Canada to a low or no tax jurisdiction or in the event of death of the RCA beneficiary. Of course, the beneficiary is taxed as funds are distributed, and the RCA receives the refundable tax from the CRA at that time. If you decide to wind up the RCA, and the RCA agreement allows for early termination, the whole RTA may be refunded to the RCA plan.

Generally Canadian residents, that are non-U.S. persons, are only subject to U.S. estate tax on death on their U.S. situs assets. U.S. assets held in an RCA could potentially be included as the RCA member’s U.S. situs assets on death for the purposes of calculating their U.S. estate tax liability, depending on the design and terms of the RCA.

The entitlement to the RCA benefits on the death of the plan member is determined by the terms of the RCA agreement. The sponsoring company may impose certain terms and conditions which will vary by plan.

For example, if the plan designates the spouse as the beneficiary after the death of the RCA member, the RCA benefits may be transferred to the member’s surviving spouse on a tax-deferred basis. In this case, the surviving spouse will be taxable on distributions made to them from the RCA in the year the distributions are received. If there is no surviving spouse, the plan member’s RCA entitlement may have to be included as income on their final return (or on a “right or thing” return). The RCA benefits can then be distributed to the decease’s estate.

The terms of an RCA agreement dealing with the death of the RCA member are not specifically restricted or governed by law. The terms can be determined by negotiation between the RCA member and their employer.

Because of all the taxation etc., it is important to consult with a qualified tax and/or legal advisor to understand the RCA benefits at death and the tax implications.
Non-resident tax treatment

The plan administrator may withhold 25% when making payments to a non-resident beneficiary. However, if the payments qualify as “periodic pension payments” the withholding tax rate may be reduced if the beneficiary is a resident in a country that has a tax treaty with Canada and the treaty allows for a reduced rate. Distributions from an RCA will be considered “periodic pension payments” if the total payments in the year do not exceed a certain dollar limit.

The tax treatment of RCA income and RCA payments in the beneficiary’s country of residence depends on their local tax rules. If you do not live in Canada and you are the beneficiary of an RCA, speak with a qualified tax advisor in your country of residence for more information.

There are special planning considerations when setting up an RCA for a Canadian resident that is also a U.S. person (U.S. citizen or green card holder). If you are a U.S. person, speak to a qualified crossborder tax advisor.

U.S. Estate Tax

Generally Canadian residents, that are non-U.S. persons, are only subject to U.S. estate tax on death on their U.S. situs assets. U.S. assets held in an RCA could potentially be included as the RCA member’s U.S. situs assets on death for the purposes of calculating their U.S. estate tax liability, depending on the design and terms of the RCA. You should consult with a qualified Canada/U.S. cross-border tax advisor to determine whether your U.S. assets held in your RCA would be included as part of your estate for U.S. estate tax purposes.

Is an RCA right for your company?

You should consider discussing the use of an RCA with your professional advisers if:

- You are a shareholder in a private company with a history of income above the Canadian small business deduction.
- Your company has the liquidity to pay bonuses or RCA contributions.
- Your company wants access to more capital.
- Your company wants to reward key employees who have worked for the company for several years.
- You want to create a pension and grow it by reinvesting it in your business.
The RCA rules do not cover unfunded arrangements. However, indirect funding arrangements may be caught under the RCA umbrella.

It is important to note that any arrangement for the deferral of employment of income is likely to be caught by provisions relating to “salary deferral arrangements” which in general provide for immediate taxation to the employee and immediate deduction to the employer.

Some RCA advantages include:

- Tax deductible and tax deferred contributions
- Taxation subject to jurisdiction
- Greater contribution room compared to registered plans (RRSP, RPP, DPSP)
- Past service funding available for prior years of employment
- Flexible investment options
- Member retains their RRSP room
- Creditor protection

Depending on the circumstances, other possible benefits include:

- Probate fee savings, since pension benefits do not flow through the estate
- Tax savings if an employee ceases to be a Canadian resident after retirement
- Flexibility in timing of contributions, allowing contributions to track profitability
- Assistance in succession planning by ensuring retiring shareholders have sufficient retirement income

Disadvantages

- Since contributions to an RCA and any income or realized capital gains in the RCA are subject to a refundable tax of 50%, the amount of funds available for investment is significantly less in the RCA than if the funds are left in the corporation to invest.
- The 50% refundable tax is credited to the Refundable Tax Account (RTA) which is a non-interest-bearing account.
- There are initial setup fees, and ongoing management and administration fees.
- The custodian will need to file a T3-RCA tax return each year, even if there has been no activity in the RCA trust in the year.
The RCA as a possible solution

RCAs may be useful in a variety of planning scenarios:

- Integration with an existing employee retirement plan
- Using RCA to reward long-term employees & retain top executives
- Funding for employee severance
- Retirement planning for professional athletes
- Retaining foreign workers in Canada
- If you or your employee are planning on moving outside Canada to a location with a lower tax rate.
- If a sale of the business is planned, you may want to consider using an RCA to reduce the value of the business, hence reducing the capital gain.

SPLIT DOLLAR LIFE INSURANCE

Permanent life insurance policies have tax-deferral advantages that make them very attractive to high income executives. However, they may not personally feel the need for insurance. Businesses, on the other hand, often want key person coverage on these individuals but do not want the expense of paying for a cash value life insurance policy.

Split dollar life insurance can be an ideal solution. The business and the executive jointly purchase a life insurance policy on the executive. The business is the owner and beneficiary of a level amount of death benefit coverage and the executive is the owner and beneficiary of the cash value of the policy.

A Split Dollar arrangement is evidenced by a formal legal agreement entered between two or more parties that specifies the sharing of the costs and benefits associated with a life insurance policy. Typically, the agreement is between two parties with one party entitled to a level amount of death benefit and the other party entitled to the remainder of the contract (the cash surrender value and any policy riders).

The business pays the cost of the insurance coverage and the executive makes contributions to the plan which accumulate on a tax-deferred basis. The executive owns the cash value portion and can use it as he/she likes, if there is enough value to keep the plan going. At retirement, the executive can use the plan to supplement retirement income or fund major expenses such as vacations or unexpected health care costs. If funds are withdrawn from the plan, they will be partially, if not entirely, taxable.
The balance continues to enjoy tax deferral. If the executive dies, the company receives a tax-free death benefit equal to the face amount of the policy and the executive’s heirs receive a tax-free death benefit equal to the plan’s cash value.

Similarly, a split dollar plan could be used with the roles reversed. The executive would pay for a level amount of insurance while the business builds up a pool of cash value. If the executive dies, his/her heirs receive a tax-free death benefit equal to the face amount of the policy and the company receives a tax-free death benefit equal to the plan’s cash value.

Allocation of Premiums

CRA has stated that each party to a Split Dollar arrangement must pay a reasonable amount of the premium for the benefit that the party receives. The concern is that in a non-arm’s length situation, a taxable benefit may be conferred on one of the parties to the arrangement unless all parties pay a cost equal to fair market value for the benefit received. Neither party should subsidize the costs of or bring about the “impoverishment” of the other party.

Pre-payment of Premiums

It is common for the party entitled to the death benefit to wish to fund or “pre-pay” their portion of the premiums rather than paying them annually for the life of the insured. In these cases, premiums are typically present valued to come up with an equivalent “quick-pay” cash flow. Although the “quick-pay” premium arrived at in this manner may be considered reasonable, there is an issue that arises with respect to the cash value. The prepayment of the premiums by the party entitled to the death benefit will increase the cash value in the contract. However, the Split Dollar agreement typically specifies that the other party to the agreement is entitled to the “cash value”.

To avoid the assessment of a taxable benefit, the party entitled to the death benefit could pay the premiums annually for the life of the insured, or the Split Dollar agreement could be written in such a way that the cash value arising from the premium pre-payments by the party entitled to the death benefit, be made payable to the party entitled to the death benefit.

Structuring the Legal Agreement

It is important to ensure that the legal structure of the Split Dollar agreement does not sever the separate interests into separate policies.
If the cash value is severed from the insurance protection it may be considered a non-exempt contract. Non-exempt contracts are subject to annual accrual taxation.

**Joint ownership of the Policy**

There are different ways to structure the ownership of a policy that is the subject of a Split Dollar agreement. The life insurance contract may be owned jointly by the parties to the agreement as joint tenants. It is important to note that the parties would enter into a legal agreement that binds them but does not bind the insurance company. The insurer is not a party to the Split Dollar agreement. A correctly documented agreement between the parties will describe the rights and obligations of each party in respect of such things as: premium payments; entitlement to cash values and death benefits; execution of beneficiary designations and the agreed upon approach to the exercise of their joint policy ownership rights. The insurer would not administer the terms of the Split Dollar agreement but would require both joint owners’ signatures to carry out transactions in respect of the policy. The Documentation and Administration Issues sections of this Tax Topic assume that the policy is jointly owned.

**Single Ownership of the Policy**

Another way to structure the ownership of the insurance that is the subject of a Split Dollar agreement is to have one of the parties as the owner of the entire contract. The owner of the policy names the other party as the irrevocable beneficiary for the level death benefit. The irrevocable beneficiary pays for the cost of insurance related to the level death benefit and the owner contributes to the cash value of the policy to build the tax-deferred investment component. Again, the insurer would not administer to the Split Dollar agreement between the two parties. In this situation, the insurer would require the owner’s signature to carry out transactions in respect of the policy. And in respect of those transactions requiring the consent of the irrevocable beneficiary, would require the irrevocable beneficiary’s signature.

For deaths on or after March 22, 2016, the 2016 Federal Budget and July 29, 2016 draft legislation would bring about the result that the CDA credit to a corporation that is a beneficiary of a level death benefit would be reduced by the ACB of a policyholder’s interest in a policy. As currently worded, the entire ACB would reduce the CDA credit.

Single ownership of a policy with an irrevocable beneficiary in favour of another party is usually structured where an employee and/or shareholder is the owner of the policy and the employer/corporation is the irrevocable beneficiary.
At some point in the future the corporation and employee may agree to a change of beneficiary, for example when the employee retires the beneficiary may be changed to the employee’s spouse. This structure could give rise to a taxable employee benefit/shareholder benefit issue or potential income inclusions.

CRA has indicated that there may be a shareholder benefit under subsection 15(1), other income inclusions (under section 9 or 12(1) (x)) or a benefit under 246(1) of the Act if the sole policy owner is a corporation and is not the beneficiary of the policy. (For example, 2009 APFF Conference Roundtable #2009-0329911C6 on October 9, 2009; 2009 Canadian Tax Foundation Annual Tax Conference #2009-0347291C6; technical interpretation #2007-0257251E5 dated November 19, 2009; Q 2 CALU CRA Roundtable #2010-0359421C6 dated May 4, 2010; and Question 9 APFF #2010-0371901C6 dated October 8, 2010).

The context of these comments was in situations where a corporation owns insurance and a different corporation is named as beneficiary under the policy. Although these comments were not in the context of a Split Dollar arrangement, they should be considered in the single ownership with irrevocable beneficiary context. For more discussion of these comments see the Tax Topic entitled “Ownership of Life Insurance – Planning Considerations.”

**Documentation**

The Split Dollar arrangement should be designed to meet the needs of all the parties to the agreement. The client’s needs and circumstances will determine the design and the ownership structure used. The documentation will therefore differ for each individual case. However, it is imperative that proper legal documentation be executed to affect the Split Dollar arrangement. As discussed in the administration section, the insurer may not be aware that there is a Split Dollar agreement with respect to the life insurance policy. The agreement would be maintained and monitored by the parties involved. Clients should seek the advice of a competent professional to ensure that the documentation reflects their objectives in their circumstances. To establish a Split Dollar arrangement a life insurance contract, a Split Dollar agreement, a Power of Attorney and a Board Resolution would generally be involved.

**Life Insurance Contract**

A life insurance contract would be issued and delivered prior to implementing the Split Dollar agreement. The documentation would not be executed until the policy has been issued. If the policy is jointly owned, the policy would be set up with all the parties to the agreement as joint owners (i.e. joint tenants).
The beneficiary designation could identify different beneficiaries for portions of the policy proceeds.

**SPLIT DOLLAR AGREEMENT**

The formal legal agreement sets out the rights and responsibilities of each party to the Split Dollar arrangement. The agreement should deal with issues including the following:

- parties to the agreement;
- ownership interests of each party in the policy;
- premium costs borne by each party;
- procedures in the event of default on the premium payment;
- right to nominate beneficiaries;
- ability to make cash withdrawals or policy loans;
- entitlement to assign cash values and death benefits;
- governance of the parties in relation to cooperating to carry out policy transactions;
- terms under which the agreement can be terminated; and
- arbitration rules to resolve disputes.

Split Dollar arrangements are a flexible method of sharing the costs and benefits of a permanent life insurance policy. There are numerous business and personal situations in which the Split Dollar concept can be a useful tool.

**Retirement Income Conclusion - The changing face of retirement in Canada**

*This is an excerpt from an article by Maclean’s posted on the internet in June 2017 that puts it all into perspective in terms that everyone can understand.*

We’re living and staying active longer. That means some people might want to work longer, just to stay busy.

It used to be Canadians pretty much shared an idea of what retirement looked like. You worked until you were 65 and then you punched your time card and went sailing or played golf. If you were lucky enough to have socked away more money, you might have quit your job five or even 10 years earlier.

Today, the definition of retirement is evolving. Why? We’re living and staying active longer. That means some people might want to work longer, just to stay busy. Another factor is many Canadians cannot count on the same generous corporate pensions their parents enjoyed. In that case, they may have to work longer whether they want to or not.
When you talk about retirement to one person, it can now mean something completely different from what retirement means to another.

Anything from fully retiring from the workforce at 55 to working part time after 65 is considered retirement. Canadians are redefining the concept of retirement with changing trends in longevity, demographics and the workplace.

A 2014 survey by Philip Cross at the Fraser Institute* confirmed there has been a marked reversal of the trend to earlier retirement. While academics and politicians debate changes to pension plan funding as the population ages, it has emerged that older Canadians are already increasing their participation in the labour force. Retirements are being postponed.

A Canada Project poll conducted early this year by *Maclean’s* revealed more about how secure Canadians feel about their retirement prospects. When asked how confident they are that they will have enough to retire on at age 65, 62 per cent of respondents said either “very confident” or “somewhat” confident. That leaves a lot of people either unprepared, or prudently tempering their optimism.

Boomers, who are closest to retirement age, were the most confident with 64 per cent responding positively. Across provincial lines, British Columbians were the most confident, at 68 per cent.

Freedom 55 is a cliché and right now, Canadians are all over the map on the topic. Sure, some want to retire early at 55, 60 or 62, but others am not inclined to retire so soon—hoping to continue working for another 10 years or so after age 65, or simply aim to work part-time for a few years to keep busy and stay engaged.

Today, for many, retirement from their full-time job simply means the beginning of a second career. Aging Canadians want to be more involved with community and are keen to stay busy pursuing other passions. No one wants to just and do nothing for 30 years,

But are Canadians financially—and psychologically—preparing themselves to retire successfully, regardless of their vision of retirement? The answer is a definite ‘yes’. In fact, according to the Fraser survey, Canadians are accumulating ample resources for their retirement; the study shoots down the notion that Canadians are not prepared.

But one thing is certain. Canadians have always adapted rapidly to the changing retirement landscape. Within three years of their introduction, one-third of tax-filers had opened a Tax-Free Savings Account (TFSA).
And as traditional pension vehicles such as employer-sponsored defined benefit plans have receded, Canadians have increased their saving elsewhere, either inside the pension system such as RRSPs, or outside, such as tax-free savings which includes the equity in their principal residence.

Other assets? Almost 70 per cent of Canadians own a home, and 10 per cent have a second home or cottage, small business, farm and saving.

On top of that, there are investments such as stocks and bonds that are outside the RRSP or TFSA. In addition, there will be inheritances and other wealth transfers.

But sometimes life gets in the way. So, while it’s easy to understand why the Maclean’s Canada Project poll noted that while 68 per cent of those without kids were confident they would have enough to retire on at age 65, that percentage decreased with families who had kids, falling to 56 per cent if they had kids under 18. This is likely because it’s hard to know where you stand financially when you’re raising kids. When they’re young there are big daycare bills but once they start elementary school and approach their teens, you start realizing how expensive kids really are.

So, while many Canadian families may have thought when their kids were younger that they’d start saving more for retirement when the kids got older, it doesn’t always happen that neatly. In fact, when Canadian families fast forward 10 years they may find that they still haven’t started. And at that point, there are additional financial hits for parents when their teens need cars, gas, cellphones, clothes and longer school trips. And all those costs are on top of the saving the parents are doing for tuition and other post-secondary education expense.

Nowadays, not everyone sees ‘retirement’ in the same way. For most, it’s just the ability to choose—maybe part-time work or a new career. So, while a lot of my professional clients may still plan on retiring at 60 or 65 with a good pension, others are coming up with their own creative ideas of how they want to spend their retirement years—and making accommodations in their budgets and work-life [balance] to make it happen.

Of all the respondents polled, three groups stood out as being least confident they could retire at 65. They are females (59 per cent), Gen-X (36 per cent), and Millennials (39 per cent).

Most assets are split about equally between non-financial assets (mostly homes and land, totalling $3.6 trillion) and financial assets (excluding RRSPs), recent reports have said.
The large amount of assets held in real estate is a rational response to the tax-exempt status of the primary residence, which essentially gives every homeowner an unlimited Tax-Free Savings Account.

Previous generations of retirees were reluctant to draw on their home equity except in a major event, such as a death of a spouse. But a big change in household finances over the past two decades shows this attitude has changed. Surveys show that prospective retirees are openly planning to downsize and use housing assets as a source of retirement income.

Still, for most Canadians, their CPP, OAS and Guaranteed Income Supplement (GIS) will form the backbone of their retirement. Whether they wish to augment these lifetime retirement payments with a small company pension, some part-time income from a side hustle or investments in the market, there’s comfort in the fact that Canadians have a lot of ways they can mix and match their retirement options to confidently shape the “retirement” they will eventually be comfortable with.

What can you do as a Financial Advisor to help your clients and prospects when it comes to helping them set aside enough money to retire?

1. Create a plan that shows them how to accomplish their goals. This may involve short-term sacrifices to ensure that the long-term goals are met. Once the plan is in place, use a system to analyze financial decisions going forward and show your clients the implications of their various choices.

2. Create an investment portfolio that is appropriate to each client situation and enable them to accomplish their goals. By “holding their hands” you can ensure that your clients stay invested in the right mix to allow them to accomplish their goals.