IG WEALTH MANAGEMENT

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Hello everyone,

As a follow-up to the RTOERO webinar, I wanted to provide the specific example that I briefly discussed. Several people in the chat had asked for more information.

There is a strategy to help you avoid capital gains, create some tax credits, generate an income you can never outlive, and it allows you to give to your favourite charity. This strategy involves appreciated securities, that are excess funds to you. If you were to sell these assets, you would trigger capital gains and pay the capital gains tax. This basically becomes locked-up capital. I see this happen all too often. Some people miss out on significant profits because of their desire to avoid capital gains tax, interfering with making good investment decisions.

There are three strategies I'll illustrate here:

## Strategy #1

This scenario uses assets where half the gain is taxed. We're using appreciated securities. Half of the appreciated stock is sold, and the proceeds are retained for your personal use. And half is donated to charity. As a result, 100% of your taxes are eliminated.

Here is an example:

My clients bought stock for $20,000, and it had grown to $100,000. This gave them an unrealized capital gain of $80,000. If they sold that stock, half of that gain ($40,000) is added to their other taxable income. Assuming a 50% marginal tax bracket, the additional tax liability would be $20,000.
So, what can you do here, instead of just selling it outright?
They took that $100,000 of appreciated securities and donated half, in kind (which means the stock wasn't sold), to their favourite charity. That gives them a charitable tax credit of about $25,000. Now the other half is sold. After the tax of $10,000 they netted $40,000 for their personal use. Now, add that to the $25,000 tax credit, and it nets them $65,000.

The advantage of using a donation of securities in-kind, is amazing. It's really quite remarkable.

Using this example here, the after-tax cost to them is $15,000 and the charity received $50,000. So, their gift is actually 3.3 times the amount that came out of their pocket. It's much better than writing a cheque. This is where it gets really interesting… They took the $65,000 and purchased a joint life annuity. An annuity is similar to a private pension. You give the insurance company your money upfront, and they'll provide you with a guaranteed income stream. In this case, for as long as either of them is alive. Together with my clients, we found an insurer that would provide them with $2,600 income for life. This is where I intervened, and I suggested they take $1,000 per year.

They were confused… What about the other $1,600? I responded with… “What about your kids?”
We used that other $1,600 per year to purchase a $100,000 joint life, last-to-die insurance policy, naming the kids as beneficiaries. Because it’s life insurance, it quickly goes to your kids, completely tax-free and probate-free.

A summary, blending all the results:
When you just sell all the stock… the $100,000… you would pay $20,000 in taxes. There is no change to your income, the charity got nothing, and you end up with $80,000 after-tax.

Here is the new result implementing this strategy:
Taxes go to zero, and income goes up $1,000 annually. That’s $30,000 over the next 30 years… $50,000 goes to the charity… and the kids receive $100,000 tax-free.
By putting to work the $100,000 excess capital, using this strategy, you are able to do a lot.
You’re keeping the kids happy… you’re avoiding capital gains tax… you’re creating some tax credits… and you’re able to make a significant gift to charity, after receiving an income that you can’t outlive.

This is just one strategy. Let’s look at another one:

## Strategy #2

We’ll use the same $100,000 example of excess capital. In this example, the assets are taxed at 100%.
In this strategy, we’ll be multiplying the amount of your donation.
Some of the money is in GICs and High Interest Savings… so that is taxed at 100%. You’re earning minimal interest. Like in the previous example, you are purchasing an annuity, but you’re using ALL of the annuity income to purchase an insurance policy. This time, instead of your children, you name a charity as your beneficiary.

Step #1: is to take the $100,000 of cash;

Step #2: use the full amount and shop around for the best annuity for the full $100,000. For a couple, both age 60, we found an insurance company that will guarantee an annual income of $4,100 per year. How much insurance will that purchase? In this example, they can get joint, last-to-die coverage for $270,000. So this is now a self-funding insurance policy. Money goes into your bank account from the annuity, and then goes back out to fund the insurance premium. When the last of this couple passes away, the proceeds of the insurance goes to their chosen charity.

From a financial perspective, what has happened this time? When the second person dies, the charity receives $270,000 directly from the insurance company. And that prompts the charity to send a charitable tax receipt for that gift to the estate executor. When the executor files the final tax return, the tax bill drops by $135,000 which means the estate gets an additional $135,000. So, even when we consider the initial $100,000 in cash used by the annuity, the estate is still $35,000 ahead. ALL parties benefit!

That $100,000 of excess capital today, ends up benefiting the charity by $270,000 and the children receive $135,000. So that is more than 4 times the current investment value. Plus, once this strategy is in place, it’s all risk-free.

If you are a bit older than this couple, your insurance premiums will be a little higher, and it still might make sense, because your annuity income will also be higher.  Both of these insurance strategies are great, yet very different.

With all of this said, insurance is not for everyone. If you have any health conditions that make you uninsurable, there are still other strategies that could work for you.

**<u>Strategy #3</u>** Here is a third strategy, without using insurance:

This is effective and very simple.
Request an RRSP or RRIF beneficiary designation change at your financial institution; Add your favourite charity or charities, as 1 or more of the beneficiaries.
There are many benefits. First of all, there is no cost to implement this strategy. You don't need a lawyer. There is no probate fee because it bypasses your Will. That's a big benefit to your executor. Amounts are paid quickly and directly to the charity. The tax receipt is received long before the final tax return needs to be filed. And finally, it's flexible.

In determining which option is best for you, that will depend on some other financial factors that are unique to you. It is important that you sit down with a financial professional to discuss your goals and the options available to you.

I am happy to answer any questions that you may have. We can schedule a time to talk on the phone, or a Zoom call, or we can meet in-person if you are close to Oakville and the surrounding area.

Sincerely,

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