



Creditor-Proofing Your RRSP

When doing your estate planning, you should review your retirement program, which includes your RRSP and RRIF investments. As a self-employed businessperson, engaged in a professional activity that includes considerable financial risk, you need to examine your potential liability situation. You may maintain a substantial level of professional liability insurance but you may still have a level of personal liability. In addition, you may be concerned for the total value of your investments. This last year has created losses in many mutual fund and self-administrated RRSP and RRIF plans. So the question is, how can you protect your funds from these two problems?

In recent years, the insurance industry has presented us with the “segregated fund” plan. By investing your retirement funds in segregated funds, you can accomplish protection from both of these risk factors. Your investments in the segregated funds can be similar or even the same as before, but with additional protection.

First, your capital investment is guaranteed. If you invest \$25,000 in a fund today, it is guaranteed by the insurance company (and the government, up to \$60,000) that when you close the fund, you will receive no

less than \$25,000. Second, because it is an insurance product, the funds are creditor-proof, provided you have irrevocably designated the beneficiary as someone other than your estate.

As a self-employed businessperson...you need to examine your potential liability situation.

It all sounds pretty good, but some factors should be considered. A segregated fund must be purchased for a fixed period of time (renewable, of course), usually 10 years, and your only guarantee is the face amount. On the other hand, even in these low-interest days, a 10-year term deposit is guaranteed for the principal and 4 to 5 percent interest. In addition, the government guarantee of up to \$60,000 also applies to the term deposit. Compounded over 10 years, the interest on a \$25,000 term deposit at 4 percent would amount to \$12,270.

The beneficiary of the segregated fund must be an immediate family member such as a spouse, child, parent, or grandparent. Bankruptcy legislation

will still hold precedence; transfers will automatically be voided if made within one year of bankruptcy, or if you were insolvent when making the transfer if within five years of bankruptcy.

In British Columbia, the law excludes RRSPs and RRIFs from the estate, provided an irrevocable beneficiary designation was made. This can, unfortunately, create a problem to the estate because it is taxable on the proceeds unless they are paid to an RRSP or RRIF plan of the deceased person's spouse.

If you are concerned about the vulnerability of retirement savings, either from creditors or from the vagaries of the financial markets, then the segregated funds may be for you. And if you are not, but wish to take reasonable precaution, then be sure to have made the proper beneficiary designations on your RRSP and RRIF. Keep your investments under \$60,000 in each institution (\$100,000 in credit unions), and rest easy. ▲

William N. Perrault, FCGA, is a Notary Public and partner in EPR North Vancouver, one of Canada's largest CGA accounting firms.

Voice: 604 987-8101
wperrault@eprnv.ca

Kathryn Edwards



Estate Planning and Tax Implications Upon Death

As we, our parents, and society in general continue to age, professionals are more frequently finding themselves addressing the estate planning concerns of their clients. In this regard, this article is intended to provide you with a general understanding of the basic tax implications to consider during the estate planning process.

“Estate planning” is the process of planning for the disposition and allocation of a person’s estate upon death. It is just one component of the more comprehensive process of “financial planning,” which includes planning and management of your finances throughout the course of your life. Common estate planning objectives include:

- minimizing income tax upon death;
- minimizing probate fees upon death;
- simplifying your affairs to reduce the burden on surviving family members; and
- planning for the distribution of assets in accordance with your wishes.

While each individual will weigh these objectives differently, individuals embarking on the estate planning process would be well advised to familiarize themselves with the tax implications that would arise upon death. This is the focus of this article.

Income Tax Implications upon Death

In general, when a person passes away, all owned assets are deemed to be disposed of

at their fair market values (“FMV”). Further, the FMV of RIFs and RRSPs or similar registered funds are deemed to be paid out at that time. As a result, the final personal tax return of the deceased can reflect a significant amount of additional income, thereby resulting in unusually high income taxes for that year. An exception to these rules arises when assets are left by one spouse to the other. In that case, the assets are generally deemed to transfer at their cost bases for tax purposes. In these circumstances, the additional income tax would not arise until the second spouse passes away.

...individuals embarking on the estate planning process would be well advised to familiarize themselves with the tax implications... .

Example

Let’s assume Uncle Bill passed away November 30. A widower at the time of his death, he left all his assets to his three adult children. He owned his own home (FMV \$300,000); had a RIF valued at \$145,000; owned a piece of vacant land in Qualicum (FMV \$130,000), which he had purchased 20 years ago for \$20,000; and had \$60,000 cash in the bank.

When Uncle Bill’s final personal tax return is filed, the following income would be reported on his return, *in addition* to his “normal” income, received up to the date of death.

Uncle Bill’s Final Tax Return

Capital Gain on Home	Not taxable; qualifies as Principal Residence
RIF Deemed Redemption (FMV of RIF)	\$145,000
Capital Gain on Vacant Land	\$130,000 FMV - \$20,000 cost base x 50% Capital Gains Inclusion Rate \$55,000
Total Additional Income to Report	\$200,000
Assume Taxed at Top Rate for 2002	x 43.7%
Total Additional Tax in Year of Death	\$87,400

Managing Taxes that Arise upon Death

The \$87,400 of additional taxes that would arise upon the death of Uncle Bill would be payable when his final personal tax return is due—in general, the later of April 30 of the following year, or six months from the date of death. One concern held by many individuals is “how to pay for the additional tax.” In Uncle Bill’s case, there is clearly sufficient cash on hand to cover the tax liability. In other cases, however, the assets on hand may not be liquid in nature; funds may not be readily available to pay