Tax, Retirement & Estate Planning Services

Tax Managed Strategy #26

Using corporate money to fund your retirement

Many individuals have built up significant cash or liquid assets within their corporation but the tax cost of withdrawing those funds is often prohibitive, resulting in the corporation itself looking to purchase the investments directly.[1]

How Manulife RetirementPlus® can help

Manulife RetirementPlus may be an appropriate investment particularly where the corporation wants to have a guaranteed income stream either now, or in the future. For example, where an individual intends to use the corporate assets to help fund their retirement income.

Manulife RetirementPlus may be especially attractive to owners sensitive to protecting their assets and who are currently invested in fixed income investments such as GICs[2] or bonds.

The guarantees offered by Manulife RetirementPlus help ensure lifetime income that the owner can never outlive. In addition, it provides the opportunity to invest in the market and take advantage of tax deferral and more tax efficient income when saving for retirement, as well as the potential for greater investment growth.[3]

Meet Christine

Christine, 45, is a successful businesswoman with $3 million in her corporation and plans to retire in 20 years when she is 65. She doesn't have a pension plan, and although she has maximized her Registered Retirement Savings Plan (RRSP) contributions, she needs the corporation's assets to supplement her retirement income.

[1] This piece assumes the corporation is a Canadian Controlled Private Corporation (CCPC).
[2] For this article GIC refers to both Insurance company issued Guaranteed Interest Contracts as well as Guaranteed Investment Certificates issued by other financial institutions.
[3] For a more detailed explanation see "Tax Treatment of Manulife RetirementPlus" MK2872.

Christine has taken a conservative approach to investing the assets of her corporation and is invested exclusively in GICs, bonds and high interest savings accounts. Now, she is looking for higher potential returns, moreover she is not happy that half of the growth is being lost to taxes.

Let's assume she uses $1 million of that $3 million to purchase Manulife RetirementPlus, deferring income for 20 years. Compare that with investing $1 million in a GIC or bond for 20 years, assuming no withdrawals.

Christine's portfolio after 20 years

After 20 years, assuming a five per cent rate of return on her investment in Manulife RetirementPlus, she would have approximately $864,000 more than had she invested in a GIC/Bond (assuming a three per cent rate of return). The corporation would have paid approximately $50,000 more in taxes; however, this includes approximately $295,000 of taxes paid on capital gains at the time of Transition.[4] While this Transition does realize taxes upfront, it also creates a significant increase to the Capital Dividend Account (CDA) of almost $580,000. Consequently, the corporation has a balance of $764,650 that it can pay out tax-free to Christine as a "capital" dividend.[5]

Furthermore, starting in year 21 (when Christine is 65), with Manulife RetirementPlus the corporation is guaranteed to receive an annual income of $126,431 a year for every year that Christine is alive.[6] With the GIC the same amount of gross income is being withdrawn, however, this includes a return of capital component to make up the interest income shortfall.

Accumulation stage – snapshot after 20 years

	GIC/Bond 3.0% ROR[7] ($)	Manulife RetirementPlus 5.0% ROR[8] ($)
Fair Market Value	1,789,249	2,653,298
Income Credits Transitioned[9]	0	700,321
Amount Added to CDA	0	764,650
Tax paid Years 1-20	402,517	453,210

For illustration purposes only.

Christine's after-tax income in years 21-46

Starting in year 21 when she needs the income from her corporation to fund her retirement, Christine's after-tax income with Manulife RetirementPlus, assuming a two per cent rate of return, is substantially higher than with the GIC/Bond. In fact, Christine receives more than one and a half times the after-tax income between the ages of 65 and 90 from Manulife RetirementPlus compared to a GIC.

This is because when the GIC's market value is depleted at year 39, it can no longer pay any more return of capital (ROC) or interest income.

After-tax income to Christine[10]

	GIC/Bond 3.0% ROR ($)	Fair Market Value ($)	Manulife RetirementPlus 2.0% ROR ($)	Fair Market Value ($)
Year 21 (age 65)	59,433	1,716,495	112,109	2,562,709
Year 26 (age 70)	101,078	1,318,649	107,894	2,171,486
Year 31 (age 75)	72,887	857,436	107,893	1,739,544
Year 36 (age 80)	74,870	322,764	74,748	1,262,645
Year 41 (age 85)	0	0	75,646	736,110
Year 46 (age 90)	0	0	76,408	154,773
Total (yrs 21-46)	1,524,423	0	2,402,514	0

For illustration purposes only.

[4] The process of moving market value and Accumulated Income Credits from the Savings Phase to the Preservation or Income Phases in a Manulife RetirementPlus contract.

[5] The CDA is a notional account that includes the non-taxable 50% of all capital gains. Corporations can elect to pay a "capital" dividend up to the balance in the CDA and the dividend is received tax-free by the shareholder. For more information on CDA, see "Taxation of investment income within a corporation" MK2665.

[6] Assumes Christine is the annuitant and, at age 65, has elected the Total Income Amount at a 3.77% Income Rate and no excess withdrawals are made. For current rates please visit manulife.ca/investments.

[7] Rate of return (ROR)

[8] During the Savings Phase assumes a 30% taxable portion on the fund return (75% capital gains & 25% interest) and a 2.07% income credit rate. The corporate tax rate is 51% (25.5% on capital gains).

[9] Income Credits are not cash deposits, they increase the basis for calculating future guaranteed income. The Income Credit Rate is subject to change. For the current rate please visit manulife.ca/investments or speak with your advisor.

[10] Assumes a corporate tax rate of 51%, year-end allocations equal to 80% of fund return comprised 90% interest and 10% capital gains. The taxable dividends paid to Christine are non-eligible dividends taxed at 40%. Takes into account and maximizes the use of the Refundable Dividend Tax on Hand (RDTOH) account and CDA where possible. Based on a Single Life Payout Option.

The advantage of Manulife RetirementPlus

With Manulife RetirementPlus, the benefit is its ability to provide a guaranteed lifetime income to help manage longevity risk. Even if the market value were to become depleted, the investment enters the Guaranteed Payment Phase[11] and would continue to pay Christine a guaranteed income stream.

By shifting part of the corporation's portfolio from fixed income investments to Manulife RetirementPlus, the total after-tax income Christine receives from her corporation during the Income Phase may be significantly higher leaving her feeling much better about her retirement plans.[12]

Ideal candidates

Individuals:

- With cash in their corporation that they are looking to invest
- With corporate assets currently invested in fixed income investments
- Who will rely on corporate assets to help fund their retirement income
- Who are looking for tax deferral, more tax efficient income and a guaranteed income stream

Take action

- Determine the amount of guaranteed income you are looking for from these corporate assets
- Consider using Manulife RetirementPlus to fund part or all of that guaranteed income stream

Investment options with Manulife

Manulife and its subsidiaries provide a range of investments and services including:

Manulife Segregated Fund Contracts that combine the growth potential offered by a broad range of investment funds with the unique wealth protection features of an insurance contract. With Manulife segregated fund contracts, investors can help minimize their exposure to risk through income, death and maturity guarantees, potential creditor protection features, and estate planning benefits – all from a single product or insurance contract.

[11] The Guaranteed Payment Phase (GPP) occurs when the fair market value is $0 but there is a positive Total Income Amount or Eligible Total Income Amount. The taxation of these payments is not certain at this time. Please consult your tax advisor for further information. We will report any payments during the GPP based on our understanding of tax legislation and CRA assessing practices at that time. The policyowner is responsible for any tax liabilities arising from any change in law, interpretation, or Canada Revenue Agency (CRA) assessing practices.

[12] Investing with a corporation can be complex. A thorough review of all of the issues is beyond the scope of this piece. Please consult with your tax advisor about the applicability of such a strategy.

Manulife

For more information contact your Advisor or visit **manulife.ca/investments**

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