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Tax, Retirement & Estate Planning Services

Tax Managed Strategy 2

Fight the clawbacks – reduce line 234

Dividend income can be the least "income-friendly" to retirees because the grossed-up amount is reported on their tax returns. Although the dividend tax credit provides preferential tax treatment, the grossed-up amount exaggerates the total income on line 234.

Canadians age 65 and older may qualify for many valuable government benefits – Old Age Security and the Age Credit, are examples. However, if the income reported on line 234 of the Federal Income Tax Form is too high, these benefits can be clawed back and, in some cases, forfeited altogether. This can result in the loss of thousands of dollars in benefits.

An in-depth look at the issue... and the opportunities

Avoiding clawbacks takes more than simply creating tax credits – which reduce the taxes owing. It is important to look at ways to actually reduce reported income. However, when retirement arrives, most of the familiar deductions (RRSP, pension, child care, union dues, etc.) are no longer available.

Following are two solutions for achieving this goal

1

Carefully structure your non-registered income

Active management of income-generating investments can significantly affect the way income is taxed, and may help reduce clawbacks. The following example, based on $10,000 of non-registered investment income, shows the impact of different types of investment income.

Consider the amount reported on your tax return

Income of $10,000

Source	Included on tax return (%)	Amount reported ($)
Elgible Dividends[1]	138	13,800
GIC/Bonds	100	10,000
Capital Gains	50	5,000
Prescribed Life Annuity	15[2]	1,500
Mutual/Segregated Fund Withdrawals	2.5[3]	250
Series T Mutual Fund	0[4]	0

1. Dividends paid by public corporations qualify as "eligible dividends" and are included at 138%. Non-eligible dividends are included at 117%.
2. Taxable percentage approximated for a 65 year old female.
3. Taxable percentage in year one, grows to 20% in year 10. Assumes a 5% rate of return on an investment of $200,000. Does not take into account year end distributions or allocations.
4. Income is considered return of capital until the adjusted cost base falls to zero at which point it is considered capital gains. Does not take into account year end distributions.

2

Create dollar-for-dollar tax deductions

When retirement arrives, most of the familiar deductions (RRSP, pension, child care, union dues, etc.) are no longer available. However, there are still some appealing options.

RRSP top-up: Those with unused RRSP room should make a lump sum final contribution prior to converting to a RRIF. The resulting deductions can then be spread over several years. For more information, see Tax Managed Strategy #4 (MK1393E).

Borrow-to-invest: By using RRIF or other discretionary income to pay the interest on funds borrowed to invest, a tax deduction can be created. This strategy is for investors with discretionary income not needed for living expenses. For more information, see Tax Managed Strategy #3 (MK1380E).

Ideal candidates

Investors who:

- Are retired or near retirement
- Seek to maximize their government benefits

Take action

To maximize benefits and retirement income:

- Identify investments that could be re-structured or more favourable tax treatment
- Make withdrawals from a mutual or segregated fund where a large portion of the payment is considered a return of capital and the balance is capital gains
- Consider the tax efficiencies of Series T mutual funds
- Make a lump sum RRSP contribution prior to converting to a RRIF
- Consider a "borrowing to invest" strategy

Investment options with Manulife

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

Mutual funds from Manulife Investments can help meet your specific financial needs, throughout your life. Whether you are just starting out, accumulating wealth or are nearing/in retirement, mutual funds offered by Manulife Investments, can provide you with solutions to help build a portfolio that meets your needs. Manulife utilizes four principal asset management firms to oversee its extensive fund family. Each firm is recognized for its strength and depth of experience in various asset classes and investment styles. Manulife is committed to providing quality investment products and services so you can enjoy life and worry less.

Manulife Segregated Fund Contracts combine the growth potential offered by a broad range of investment funds, with the unique wealth protection features of an insurance contract. Through Manulife segregated fund contracts, investors can 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.

The Manulife Investments Guaranteed Interest Contract (GIC) offers competitive rates plus investment options that include Basic, Escalating Rate and Laddered GIC Accounts. Investors benefit from consistent returns and from several different investment options that can diversify and add flexibility to their portfolio. A Manulife Investments GIC can be an ideal solution for conservative investors looking to help grow their wealth, but who are also concerned about minimizing risk.

Manulife Bank's Investment Loan programs are available for Manulife Mutual Fund accounts and Manulife Segregated Fund contracts. Investment loans feature interest-only or principle and interest payments and no margin-calls due to market fluctuations.

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

Borrowing to invest may be appropriate only for investors with higher risk tolerance. You should be fully aware of the risks and benefits associated with investment loans since losses as well as gains may be magnified. Preferred candidates are those willing to invest for the long term and not averse to increased risk. The value of your investment will vary and is not guaranteed however you must meet your loan and income tax obligations and repay the loan in full. Please ensure you read the terms of your loan agreement and the investment details for important information. The dealer and advisor are responsible for determining the appropriateness of investments for their clients and informing them of the risks associated with borrowing to invest.

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