

ADVANCING *Issues*

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Happy 1st Birthday to CPA (*well, sort of*)!

By David Vicic, Senior Vice President, Corporate Planning Associates

I was sitting in my office a couple of weeks ago when somebody pointed out to me that it was May 12th, 2006. Somehow, that date resonated in my mind but I couldn't figure out why that date seemed important until that same person advised that precisely one year earlier, CPA Securities Inc. had finally received its approval for membership in the Investment Dealers Association of Canada. After a year long battle with lawyers and regulators, we were finally in! It seemed as though the day would never come, and we believed that the hardest part was behind us.

One of my responsibilities at Corporate Planning Associates is to oversee the administration of the securities portion of our business. As part of this mandate, I was responsible for the transition of our investment business from the world of the mutual fund dealer to that of the broader investment dealer world. It was our hope that

this transition would be a smooth one for all interested parties: regulators, staff, mutual fund companies, our carrying broker, and most importantly, our clients. Well, as I sit in my office and think about what the past year has been like, I can unequivocally state that we were dead wrong – the hardest part was still ahead of us!



When we received our acceptance into the IDA, our clients' accounts totaled roughly \$300 million in aggregate and represented approximately five thousand individual mutual fund positions. Under normal circumstances, each and every one of these accounts would have to be transferred by means of a transfer form, signed by the client. We wanted to keep the amount of paperwork required to a minimum so we approached the regulators with a plan that many insiders advised was "unique and groundbreaking" (editor's note: these three

words began to take on new meaning within the CPA's securities administration department and eventually came to mean that trouble was around the corner). The regulators approved our plan to move assets that were "off-book" or in client name by means of a negative response letter. Many, many hours and spreadsheet after spreadsheet later, we were able to create accounts in bulk and then with careful cross-referencing of these new accounts to our clients' existing accounts, we were able to move approximately \$250 million of client assets over the span of 2 weeks. Unfortunately, some of the fund companies would only move assets if a client signed a transfer form; approximately \$6 million remains in client name with the fund companies. Interestingly, less than 3% of clients holding assets with CPA declined the invitation to move their accounts to our new world.

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Our move to the IDA and more specifically to our carrying broker NBCN, would require the “papering” of each and every client account that was held with our various mutual fund partners. I shudder to think about the number of trees that were felled to produce the application forms, locking-in agreements, account supplements et cetera et cetera that have been completed over the last year. Our staff and I daresay our clients have been, at times, overwhelmed by the sheer volume of paper produced. At this point, I would be remiss if I did not send out a note of thanks to all of CPA’s investment clients for their patience and understanding during this transitional period in CPA’s history.

Another of our “unique and ground-breaking” issues revolved around the fact that some of our clients rely

on their investments to produce a stream of income. It had become apparent that this move to NBCN would cause all systematic withdrawal plans to be stopped when funds were transferred. We were told by all of the fund companies that there was no way to keep these plans alive without submitting the appropriate paperwork. Undaunted, we went back to the drawing board and devised a plan where systematic withdrawal plans would continue throughout the transfer process. Apart from a couple of hiccups along the way, our “unique and ground-breaking” approach worked.

This first year has been very interesting indeed. We have all learned a lot and if we were to do it again, I am sure that some things would have been done differently. However, as much as it has been a tough process, we have no doubt

that it was the right decision to become an investment dealer. We believe that, both in the short term and in the long term, our clients will benefit from a greater selection of investment products, a fully integrated managed accounts platform, the ability to consolidate all of their investment accounts in one place and a reduction in management fees.



So, I raise a glass to CPA on its second first birthday and as we look forward to the future, I can see bigger and better things to come. Stay tuned...

Critical Illness Insurance – What is it? Do you need it?

By *Duncan McEachran, Senior Vice President, Corporate Planning Associates*

Although still fairly new to Canada, this is a concept that was originally developed in South Africa in the mid 1980’s by Dr. Marius Barnard, who saw first-hand the potentially devastating affects of a critical illness. In short, Critical Illness Insurance is a

form of living benefit, whereby an insurance contract pays out a benefit to an insured while they are still living, but have been diagnosed with a critical illness.

It can provide a lump-sum, tax-free payment of up to \$2M depending on the policy, after 30 days of being

diagnosed with a particular critical illness. These illnesses are defined in the policy and can include the common ones, such as cancer, stroke and heart attack. There is no requirement that the illness actually lead to a disability, permanent or otherwise. Since there are no

restrictions on how the money is spent, it can provide a funding source for whatever financial requirements may arise as a result of the illness. Paying off debts, providing for additional health benefits beyond government-funded programs, modifications to a home, and supplemental income beyond any disability income plans are some of the potential uses for the benefit payment.

Policies are available that provide for a benefit payment upon diagnosis of a range of particular illnesses. They are available on a basis where the premiums remain the same for

either 10 or 20 years, as well as ones where the premiums do not change and end at age 100. They can also provide for a payment anytime up to either age 65 for a more economical premium, or if coverage is needed later in life, to age 75. There are also additional features that can provide for a return of premiums paid if a covered illness does not occur within either 10 or 15 years of coverage, or at ages 65 or 75. As well, premiums can also be returned to an insured's estate if they were to die and were not eligible for a critical illness benefit payment. These are several potential

ways to get your premiums returned if the coverage was not needed, something we all hope is the case.

Whether or not this type of insurance is required depends of course on one's financial circumstances, and whether or not a potential illness could provide undue hardship. Critical illness insurance does not replace life insurance, nor does it replace disability income insurance. It should be considered a complement to these more common forms of insurance, one that can provide benefits when the others won't.

Elections Not to Receive Income of a Testamentary Spousal Trust – Timing is Everything

By *Bernadette Dietrich, Angela Ross*

Recent pronouncements by the Canada Revenue Agency (the CRA) have complicated the method by which a spouse can elect not to receive the income of a testamentary spousal trust. If done incorrectly, the testamentary nature of the spousal trust, and its graduated income tax rate, are both at risk.

The CRA maintains its long-standing position that the spouse beneficiary of a spousal trust can elect not to receive the income of the trust and, instead, have that income added to the capital of the trust. That said, for testamentary spousal trusts, if such an election is made at a time when the income of the trust is payable to the spouse beneficiary, the spouse

beneficiary will be considered to have already received such an amount and made a contribution to the trust, thereby tainting the testamentary nature of the trust.

Until these recent CRA pronouncements, it was long understood that a spouse beneficiary of either a testamentary or inter vivos spousal trust could elect at any time not to receive income earned, but not yet distributed, by the trust. Where such an election was made and communicated to the trustees of the trust, the income of the trust would be considered to be payable to the spouse (because, under the terms of the spousal trust, the spouse will be entitled to all of the income of the

trust until death) and, unless the trustees made an election to have the income taxed in the trust's hands, the spouse would be taxed on the income. This position appears to continue to apply in respect of inter vivos spousal trusts.

For testamentary spousal trusts, however, the CRA now takes the position that an election not to receive income of the trust must be made before such income becomes payable to the spouse. If an election is made not to receive income of the trust that is already payable to the spouse, this action will be considered a contribution to the trust by the spouse during his or her lifetime. By definition, a "testamentary trust"

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under the Income Tax Act (Canada) (the ITA) will not be a testamentary trust if property is received from anyone other than a deceased person as a result of his or her death. If the spousal trust loses its characterization as a testamentary trust, it will no longer benefit from the graduated income tax rates afforded to it under the ITA. Rather, it will be taxed on all of its income at the highest marginal income tax rate for individuals.

This does not mean that the spouse beneficiary of a testamentary spousal trust cannot make an election not to receive the income of the trust. It does, however, mean that such an election must be made at a time when the income is not

payable to the spouse. Generally, the income of a spousal trust will be considered payable to the spouse as it is earned. As a result, an election not to receive the income of a testamentary spousal trust should be made by the spouse prior to the income being earned.

Because the timing of an election not to receive the income of a testamentary spousal trust is now a critical factor, any such election should be made in writing and dated. In most circumstances, the spouse should make the decision, and provide the trustees with a written election not to receive the income of the testamentary spousal trust for a particular taxation year prior to the beginning of that

taxation year. There may, however, be limited circumstances under which an election can be made during a taxation year.

In addition, because the election not to receive the income must be made prior to the income becoming payable to the spouse (in essence, a temporary renunciation of the income), renounced income must not be included in the income of the spouse for tax purposes, but included in the income of the trust. If you would like more information on this subject, please contact one of our lawyers listed below.

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