

ACCESSING THE RBC AND IA TAX REFUND

HOW TO MANAGE THIS VALUABLE POLICY BENEFIT

OVERVIEW

Certain RBC and Industrial Alliance life insurance policies contain a valuable Tax Refund feature that is **not offered by any other insurers in Canada**.

Generally, the Tax Refund “tops up” a withdrawal of cash from a policy by providing the policyholder with an additional amount equal to 15% of the taxable gain associated with the withdrawal.

In some cases, the insurer may reduce the Tax Refund for a policy year to maintain the tax exempt status of the policy, with options to preserve it at some additional cost.

In the absence of any intention to withdraw policy cash value, **Westward recommends the default Minimize Refund** option to keep the policy tax exempt. If a withdrawal need arises while the Tax Refund is reduced, then the full Tax Refund benefit should be accessible on the next policy anniversary.



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What Is the Tax Refund?

For policies with the Tax Refund benefit, the insurer will top up a voluntary cash withdrawal (i.e. other than as a consequence of death or disability) with some additional cash. This top up is called the Tax Refund, because it mirrors the amount of the Investment Income Tax savings that the insurer realizes as a consequence of the withdrawal. The insurer is passing this savings on to the policyholder.

How Is the Tax Refund Calculated?

The maximum Tax Refund is **15% of the taxable portion** of the withdrawal, typically covering about 30% of the tax incurred on a withdrawal, assuming a 50% tax rate. The taxable portion is the amount of the withdrawal (including the Tax Refund) less the adjusted cost basis of the withdrawal.

■ The Tax Refund provides cash to cover about 30% of the tax triggered by a withdrawal.

How Is the Policy Kept Tax Exempt?

To remain tax exempt, the policy's cash surrender value cannot exceed a limit prescribed by a formula in the *Income Tax Act*. The Tax Refund benefit forms part of the policy's cash surrender value. If excess cash surrender value is going to cause a policy to fail the exempt test in a given policy year, the insurer has several options to resolve the problem:

- **Maximize Coverage:** Increase the insurance coverage for the policy year, with additional cost;
- **Minimize Cash Value:** Reduce premiums for the policy year; or
- **Minimize Refund:** Reduce the Tax Refund for the policy year, if applicable.

Minimize Refund is the default option used by RBC Insurance and Industrial Alliance. For example, RBC Insurance sends the policyholder a notification that the Tax Refund will be reduced to resolve the problem, and offers the policyholder time to elect into one of the other options if desired.

How Is the Tax Refund Accessed?

The insurer automatically pays the Tax Refund at the time of the policy withdrawal. If the Minimize Refund option is in effect, a policyholder should consider options to access the full Tax Refund in future policy years, and deferring the withdrawal to the next policy year.