Giving the Gift of Knowledge

Saving for a child's post-secondary education

There's Wealth in Our Approach.™

RBC Wealth Management

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The Value of Education

Of all the factors that can influence a child's future employment status, earning power and level of career satisfaction, few are as significant as a post-secondary education.

Today in Canada, earnings of university and college graduates are 39% higher than the earnings of high-school graduates.[1] According to Statistics Canada, workers with a post-secondary education can expect to see their wages grow much faster than workers with only a high-school diploma. Post-secondary education is also associated with more years of coverage in an employer-sponsored pension plan and fewer layoffs than a high school diploma.[2]

Considering that 70% of jobs today require a post-secondary education,[3] we can only anticipate the value of education to be just as important — if not more important — in the future.

These striking statistics underline the many real-world advantages for people who receive a higher education. Educated workers tend to enjoy greater self-esteem, a more challenging and rewarding career and the peace of mind that comes from having options in today's fast-moving economy.

A Challenge Worth Meeting

But while the rapid increase in enrolment rates across Canada shows a growing demand for post-secondary education, costs continue to climb just as quickly.

With tuition fees quadrupling over the past 20 years[4] and other expenses spiralling upward, Employment and Social Development Canada (ESDC) predicts that in 2032 a student's annual average expenses including tuition fees, books, shelter, food and transportation will be $32,800.[5]

The challenge for parents and students is clear: the value of education is too great to ignore, yet the costs can be high.

If you want your children to be able to get the education they need, without being hampered by financial concerns, this guidebook is for you. It explains some of the most effective ways to save and invest, so that you can give your child the truly priceless gift of knowledge.

Education by the numbers

97%

Percentage of parents in Canada with children in grade 4 who want their children to achieve a post-secondary education.[6]

$90,000

Estimated cost of a four-year university education away from home for students admitted in 2020.[7]

70%

Percentage of parents who have a savings plan devoted specifically to paying for college or university expenses.[8]

6.3% per year

Average annual increase in university tuition costs and other compulsory fees since 1990-1991.[4]

$12,972

Average amount borrowers owed the Canada Student Loans Program at completion of studies in the 2011-2012 school year.[9]

The Registered Education Savings Plan (RESP)

The Foundation of Your Education Savings Strategy — There are several different ways you can save for a family member's education — but a Registered Education Savings Plan (RESP) offers many important advantages. An RESP combines flexibility, tax-deferred investment growth and direct government assistance to help you reach your education savings goals. Here's how it works:

Opening an RESP

At RBC Wealth Management, we offer a type of RESP called a Family Plan, which can be set up for various family members, including children, grandchildren and even siblings (by blood or adoption).

The "subscriber" to the plan is the individual who opens the plan and makes contributions to it. The "beneficiary" of the plan is the individual or individuals who are designated to receive the funds for the purpose of pursuing post-secondary education. The beneficiary must be a Canadian resident and have a Social Insurance Number (SIN).

A Family Plan offers several advantages, including the ability to name one or more beneficiaries in the same plan. In addition, the funds in the plan do not have to be shared equally among the beneficiaries, giving you more flexibility when it comes to making withdrawals.

Making Contributions

Any subscriber can contribute to an RESP, subject to a lifetime limit established for the beneficiaries. Although you cannot deduct the contributions made to an RESP from your taxable income, the subsequent investment earnings on RESP contributions are tax-deferred. Qualifying investments include GICs, stocks, bonds, mutual funds and professionally managed investments. At RBC Wealth Management, we offer the full range of investment options for your Family RESP.

If the plan earnings are ultimately withdrawn to cover qualifying post-secondary education expenses, they are taxable to the beneficiary, not to the subscriber.

There are no limits on the number of plans subscribers can establish, or the number of RESPs a beneficiary may have. However, the limit on lifetime contributions for any one beneficiary is $50,000. Overcontributions are subject to a penalty of 1% per month.

Note that the lifetime limit applies to the total contributions, by all subscribers, to all plans in the name of the beneficiary. As a result, if you contribute to a plan for your child, and your child's grandparents also contribute to a plan, you will need to co-ordinate your contributions so as not to exceed the $50,000 maximum.

You can make lump-sum contributions at any time. You can also make contributions monthly or quarterly through a Pre-Authorized Contribution (PAC) program, which automatically transfers funds from your bank account.

You may make contributions to an RESP for up to 31 years and the plan can remain open for up to 36 years in total. Special rules apply where the beneficiary of the RESP is disabled. In that case, contributions can be made for a maximum of 35 years and the plan can remain open for up to 40 years.

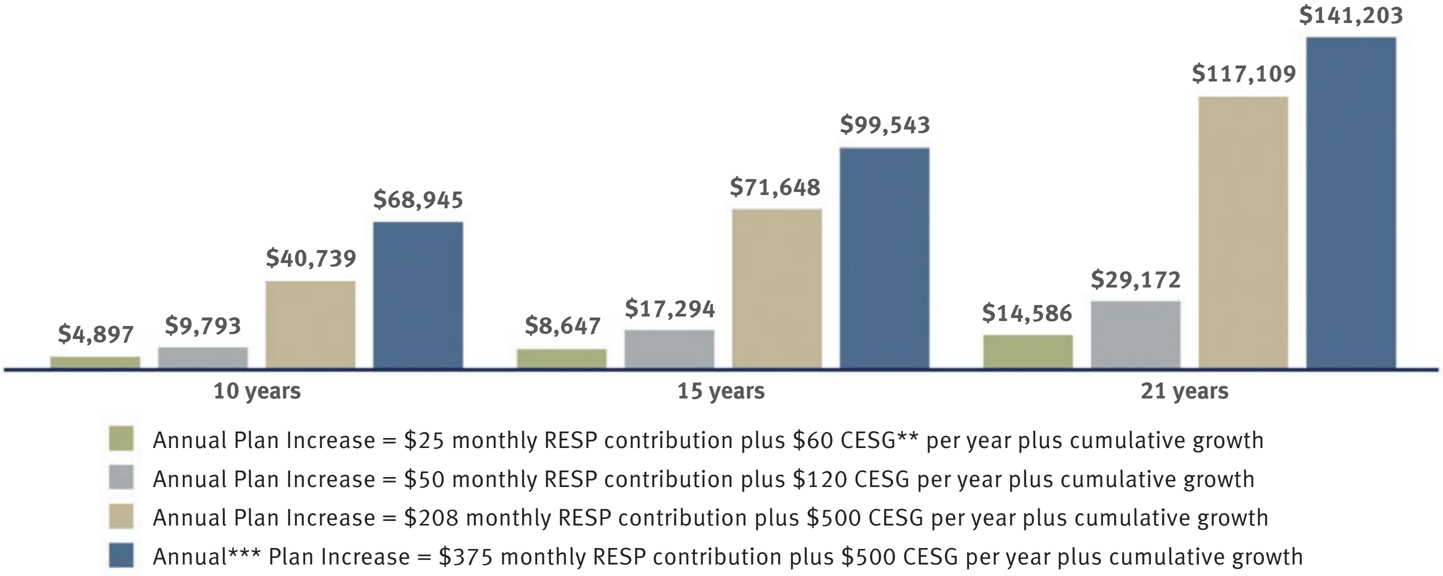
Pre-Authorized Contributions

A PAC program is one way to make sure that your child's RESP savings never take a back seat. As the chart* (following page) illustrates, even small monthly PAC contributions add up quickly over periods of 10, 15 and 21 years when they are supplemented by the Canada Education Savings Grant (CESG).

Government Resources Online

- The ESDC site has information on saving for education: www.esdc.gc.ca
- To download a form to apply for a SIN for your child, go to Service Canada: www.servicecanada.gc.ca
- For more information about RESPs, download the Canada Revenue Agency (CRA) guide on RESPs: www.cra-arc.gc.ca/tx/ndvdls/tpcs/resp-reee/menu-eng.html

EVEN SMALL CONTRIBUTIONS ADD UP QUICKLY



* Calculations are for illustrative purposes only, and are not intended to reflect future values or returns on investment. Based on 6 % annual return for contributions made at the beginning of each month. These calculations also assume that the contributions are made at the beginning of every month, up to a lifetime maximum of $50,000 per child.

** Under the CESG program, the federal government will match 20% of the first $2,500 contributed annually to an RESP for a beneficiary under the age of 18. If you don't contribute enough to get the maximum $500 grant in a given year, the unused entitlement can be carried forward to the next year. The maximum CESG payment in any year is $1,000. The maximum cumulative grant over the life of the RESP is $7,200.

*** Under this scenario, above calculations assume lifetime contribution maximum of $50,000 will be reached early in the 11th year ($375/month x 12 months x 11.1 years =$50,000). Once this limit is reached, contributions and CESG payments will stop, with the annual increase in plan assets driven by 6% annual return assumption.

The Canada Education Savings Grant: A Potential 20% Return on Investment

Perhaps the biggest advantage to contributing to an RESP is the CESG — a powerful incentive from the federal government.

With the basic CESG, for an eligible beneficiary under the age of 18, the government will add 20% annually to the first $2,500 contributed to an RESP. That adds up to $500 per year. The maximum CESG over the life of the plan is $7,200 per beneficiary. The grant proceeds are invested along with your contributions, further enhancing the benefits of tax-deferred, compound-investment growth within your plan.

If you don't contribute enough to warrant the maximum grant in a given year, the unused entitlement can be carried forward to the next year. The maximum payable in any one year, however, is $1,000.

Special rules apply when the beneficiary is 16 or 17 years old. In order to receive the CESG, contributions to all RESPs for the child must have totalled at least $2,000 before the year in which the child turns 16, or there must have been contributions of at least $100 a year in any four years before the year in which the child turns 16.

Going to School

Receiving Educational Assistance Payments — Once the student is enrolled in a qualifying post-secondary education or training program, the funds within the RESP can be paid out as Educational Assistance Payments (EAPs) at the discretion of the subscriber. These funds may be used for any education-related expenses, such as books, housing and tuition at a qualifying school.

Most Canadian universities, colleges and other educational institutions qualify for the purpose of EAPs. In fact, many institutions outside of Canada also qualify. Part-time students can access up to $2,500 in EAPs for each 13-week semester of study, provided they spend at least 12 hours a month on courses and the courses last at least three consecutive weeks. Full-time students can generally access up to $5,000 in EAPs during the first 13 weeks of enrolment, and thereafter there is no limit on the EAP amount. A student can access EAPs for up to six months after ceasing enrollment, provided that the payments would have qualified as EAPs while the student was still enrolled. You can consult your local Canada Revenue Agency (CRA) office to find out if a specific institution qualifies.

With a Family Plan, you can decide how to allocate the RESP funds among more than one beneficiary. This way, you can direct more to a beneficiary whose educational expenses are higher. The maximum CESG that can be received by any one beneficiary is $7,200.

To elect an EAP, the subscriber must sign a withdrawal form, and the beneficiary must provide proof of enrolment in a qualifying program. The funds must be used to cover the beneficiary's education expenses, and ESDC may request supporting information for EAPs of unusually large amounts.

All EAPs are taxable in the hands of the plan's beneficiary Usually, this results in little or no tax payable by the student.

What Happens if a Child Doesn't Pursue Post-Secondary Education?

If the child who is named as beneficiary of the RESP decides not to pursue post-secondary education, you have several options:

- With a Family Plan, you can designate another beneficiary to receive the contributions, government grants (to a maximum of $7,200 per beneficiary) and earnings.
- If the beneficiary is 21 and the plan is at least 10 years old, the earnings can be withdrawn by the subscriber, subject to a penalty tax; the amounts will also enter into taxable income.
- It may be possible to transfer up to $50,000 of the plan's growth (or earnings) tax-free into your Retirement Savings Plan (RRSP) or your spousal RRSP. You must have available RRSP contribution room to do this. You can withdraw the initial contribution with no tax consequences (since you contributed tax-paid dollars).

In all instances, the original principal you contributed will be returned to you tax-free. Any CESG paid into the plan that cannot be transferred to an alternate beneficiary must be returned to the government. However, interest or investment growth earned on grant money does not have to be paid to the government.

Other Ways to Save For a Family Member's Education

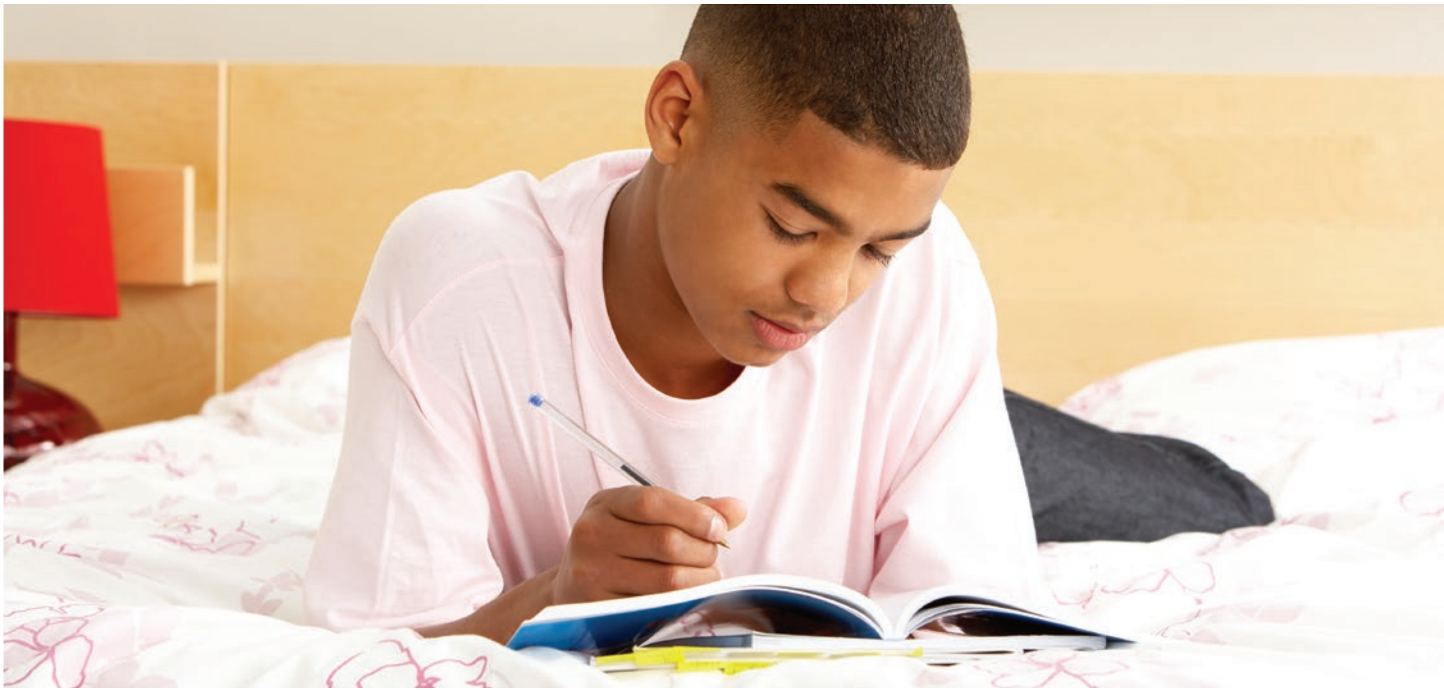
If you're a parent who is currently maximizing your RESP contributions, or looking for alternatives, you may wish to consider the following options.

Open a separate savings or investment account. While earmarking this account for education is easy and allows you maximum control and flexibility, keep in mind any investment income you earn will be taxable in your hands in the year you earn it. This means you could miss out on the benefit of tax-deferred growth.

Use your Tax-Free Savings Account (TFSA). Unlike RESP contributions, amounts you contribute to a TFSA are not eligible for the CESG. However, both earnings and withdrawals are tax-free. You could make withdrawals and either pay your child's school fees directly or give the money to your child, if you prefer.

Set up a trust. In general, a trust is a relationship in which one person, the trustee, holds title to property, subject to an obligation to keep or use the property for the benefit of another person or persons, known as the beneficiary(ies). It is important to set up the trust properly, using a written legal agreement that clearly provides the terms and conditions. A trust can be structured to be a tax-efficient supplement to an RESP and still allow you to have access to the monies you used to fund the trust. Although contributions to the trust will not be eligible for the CESG, a trust is more flexible than a RESP in terms of funding limits and the type and timing of expenses for which the funds in the trust may be used.

Use corporate funds. If you are an owner-manager of a corporation, consider loaning corporate funds to your adult children to finance their education costs. The loan is considered taxable income to the adult child, however the tax payable on this income may be very low or even nil due to the child's basic personal, tuition and education tax credits. When your child repays the loan to the corporation in a future year when they are working and earning income, they will receive a personal tax deduction. Alternatively, if your adult child is a shareholder, consider paying them corporate dividends.



Investment Solutions

Whether you're investing inside or outside of a registered plan, working with your Investment Advisor is the key to optimizing performance and ensuring that your child has sufficient funds to pay for post-secondary education. These are some time-tested investment fundamentals that should guide your decisions.

Diversify According to Your Time Horizon

Diversification means spreading your investment dollars among a variety of investment types and asset classes — cash, fixed income and equity. Since each of these asset classes will perform differently at different times, broad diversification tends to smooth out the bumps in the market.

The way you diversify your investments depends on your tolerance for risk and your investment objectives. If you are contributing to an RESP for a newborn child, you may wish to place a significant portion of your savings in equity-oriented investments. This is because you can take advantage of their long-term growth potential, without having to worry too much about year-to-year fluctuations in value.

On the other hand, if you are saving for a child who is expected to need the funds in seven years or less, it may be more prudent to stick with fixed-income investments, or other guaranteed investments such as GICs, to reduce the risk of an unexpected loss in market value too close to the time at which the funds will be required.

Ideally, the asset mix of your portfolio should change as your child grows, focusing on growth in the early years, and shifting toward capital preservation as the goal date nears. In general, the more time you have to save, the more growth-oriented your portfolio can be.

Professional Money Management

One of the easiest and most cost-effective ways to implement a diversification strategy is to take advantage of professional money management. The benefits of professional management include:

- **Diversification** — Your education savings are diversified among many different investments to help reduce risk.
- **Professional management** — Your education savings are managed by experts, freeing your time to focus on other priorities.

With a professionally managed RESP, you can build your education savings with confidence. And with the added boost of tax-deferred compound growth, augmented by the CESG, it can also help you meet the challenge of rising education costs.

Committing to Your Child's Future

One of the most effective ways to reach your goals — and ensure that your child's education savings receive the priority they deserve — is to commit to a regular, periodic investment plan.

There are three key benefits to this approach:

- It's a convenient, yet disciplined way to save.
- It gets your money working for you right away to maximize your opportunity for returns.
- With dollar-cost averaging, you don't need to worry about the "right time" to contribute because you're always investing.

Encourage Your Kids to Help

Encourage your children to save their earnings and cash gifts from relatives in a special savings account. Not only will they help accelerate their savings this way, they will also learn a valuable lesson about the power of long-term investment growth.

Take the First Step

- Whether you're investing inside or outside of an RESP, we offer a wide range of education savings options. For more information about how we can help you build an education savings portfolio, please speak with your RBC advisor.

1 *Education at a Glance 2013: Highlights for Canada*, Council of Ministers of Education, Canada, June 25, 2013.

2 Marc Frenette, *An Investment of a Lifetime? The Long-term Labour Market Premiums Associated with a Postsecondary Education*, Social Analysis Division, Statistics Canada, 2014.

3 Canadian Occupational Projection System 2011 Projections, *Imbalances Between Labour Demand and Supply (2011-2020)*, Employment and Social Development Canada, www23.hrsdc.gc.ca/w.2lc.4me@-eng.jsp (accessed May 21, 2014).

4 Erika Shaker and David Macdonald with Neil Wodrich, *Degrees of Uncertainty, Navigating the Changing Terrain of University Finance*, Canadian Centre for Policy Alternatives, September 2013.

5 *Actuarial Report on the Canada Student Loans Program as at 31 July 2011*, Office of the Chief Actuary, Office of the Superintendent of Financial Institutions Canada, 2012.

6 *Assessment Matters!, Council of Ministers of Education*, Canada, No 4, 2013.

7 *Tuition and Living Accommodation Costs for Full-Time Students at Canadian Degree-Granting Institutions Survey*, Statistics Canada, 2009/2010. Projected costs are based on 2009/2010 Canadian average with an annual increase of 4.4% for tuition and 2% inflation on all other education related costs.

8 Stephen Arrowsmith and Jean Pignal, *Initial Findings from the 2009 Canadian Financial Capability Survey*, Statistics Canada, 2010.

9 *Canada Student Loans Program Statistical Review 2011-2012*, Employment and Social Development Canada, 2013.

For more information, please speak with your RBC advisor

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