



## FINDING BETTER CHOICES FOR YOUR MATURING GICs

During the economic turmoil of 2007-2009, many investors took refuge in the safety of Guaranteed Investment Certificates (GICs). Despite the low GIC rates, these “GIC refugees” could at least take some comfort in the fact that they weren’t losing any money. But now, with their GICs maturing, GIC refugees are considering their options – and they may not like what they see. However, there are still opportunities to enhance your after-tax investment income – they are just harder to find.

### GET TAX-SMART

You may not have much control over what a certain investment returns to you – before tax. But you can do something about how much of it you keep after tax.

#### FUND TAX-FREE ACCOUNTS FOR YOUR FAMILY

With a TFSA, you can contribute up to your contribution limit each year (\$5,000 for years 2009-2012, and \$5,500 for 2013 and 2014), earn tax-free investment income including interest, dividends and capital gains, and even make withdrawals – at any time, for any reason – without paying tax. With the contribution room from 2009 through 2014, you may be able to contribute up to \$31,000 to your TFSA if you haven’t opened yours yet.

#### ALLOCATE YOUR ASSETS FOR MAXIMUM TAX EFFICIENCY

Because investments generating dividends and capital gains are already tax-efficient, consider allocating

more of them to your regular taxable accounts. Then, allocate more of your interest-bearing investments to your registered accounts (RRSPs, RRIFs) where they are sheltered from annual accrual taxation.

#### SPLIT INVESTMENT INCOME WITH LOWER-INCOME FAMILY MEMBERS

By transferring investment income from your higher tax rate to a family member’s lower tax rate, you can reduce your family’s overall taxes. There are several ways you can do this, but one that’s especially timely is the spousal loan strategy. You make a bona fide, legally documented loan to your lower-income spouse at an interest rate prescribed by the Canada Revenue Agency (CRA). Your spouse must pay you the required annual interest every year. Your spouse then uses the full loan amount to invest in an investment portfolio held in their name and the investment income is taxable at their lower marginal tax rate.

#### GET MORE FROM YOUR LOW-INTEREST INVESTMENTS

Lower rates on GICs and bonds are frustrating, but they have an important role to play in your portfolio because they add stability. And there are ways you can squeeze a bit more from them in addition to sheltering them in your registered accounts:

- Ladder your fixed-income investments. “Laddering” is simply staggering your bond or GIC holdings by maturity dates. So with a five-year ladder, you start with roughly equal amounts in a one-, two-, three-, four- and five-year bond/GIC. Each year, you roll into a new five-year bond/GIC. At the end of five years, you own only original five-year bonds/GICs.

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## INVESTMENT ALTERNATIVES FOR YOUR MATURING GICs

GIC refugees have many different investment choices above and beyond low-interest GICs. The following table highlights many of these investment choices from more stable, but lower-yielding investments like GICs and bonds to higher-yielding investments like preferred shares.

Investment	What it is	Why choose it	What to consider	How to use it
Government bond	<ul style="list-style-type: none"> <li>■ A certificate issued by government as evidence of debt it promises to repay in full at a certain date and rate of interest</li> </ul>	<ul style="list-style-type: none"> <li>■ Loan returned in full at maturity</li> <li>■ Guaranteed semi-annual interest typically higher than GICs</li> <li>■ Easy to sell before maturity if needed or for potential capital gains</li> </ul>	<ul style="list-style-type: none"> <li>■ Lower interest rates erode purchasing power</li> <li>■ Interest fully taxable at your marginal tax rate</li> </ul>	<ul style="list-style-type: none"> <li>■ Generate semi-annual income</li> <li>■ Add stability to overall portfolio</li> <li>■ Increase yield by laddering</li> </ul>
Real-return bond (or Treasury Inflation Protected Security in the U.S.)	<ul style="list-style-type: none"> <li>■ A government bond indexed to the Consumer Price Index (CPI)</li> </ul>	<ul style="list-style-type: none"> <li>■ Protects purchasing power from inflation by increasing principal in line with CPI</li> <li>■ Pays semi-annual indexed interest similar to a conventional bond</li> </ul>	<ul style="list-style-type: none"> <li>■ Interest payments fully taxable</li> <li>■ Accrued principal taxed as interest</li> <li>■ Less liquid than conventional bonds</li> </ul>	<ul style="list-style-type: none"> <li>■ Hedge portfolio against inflation while generating income</li> <li>■ Better suited to non-taxable accounts due to structure of taxation</li> </ul>
Guaranteed Investment Certificate (GIC)	<ul style="list-style-type: none"> <li>■ A deposit instrument available from banks and trust companies</li> </ul>	<ul style="list-style-type: none"> <li>■ Initial deposit returned in full at maturity</li> <li>■ Guaranteed interest payable monthly, semi-annually, annually or compound</li> <li>■ Up to \$100,000 CDIC insurance (per GIC issuer)</li> </ul>	<ul style="list-style-type: none"> <li>■ Low interest rates erode purchasing power</li> <li>■ Interest fully taxable at your marginal tax rate</li> </ul>	<ul style="list-style-type: none"> <li>■ Add stability to overall portfolio</li> <li>■ Increase yield by laddering (staggered maturity dates)</li> <li>■ Gain CDIC insurance for GIC assets above \$100,000 by diversifying</li> </ul>
Guaranteed Interest Annuity (GIA)	<ul style="list-style-type: none"> <li>■ The insurance industry's version of a GIC</li> </ul>	<ul style="list-style-type: none"> <li>■ May offer higher income than GICs</li> <li>■ Initial deposit returned in full at maturity or death</li> <li>■ May offer creditor protection</li> <li>■ Death benefit can bypass probate</li> </ul>	<ul style="list-style-type: none"> <li>■ Low interest rates erode purchasing power</li> <li>■ Interest is fully taxable at your marginal tax rate</li> </ul>	<ul style="list-style-type: none"> <li>■ Add stability to overall portfolio</li> <li>■ Provide estate-planning benefits through beneficiary designation</li> <li>■ Eligible for pension income splitting at age 65+</li> <li>■ Eligible for Pension Income Tax Credit</li> </ul>
Segregated fund (Guaranteed Minimum Withdrawal Benefits)	<ul style="list-style-type: none"> <li>■ An insurance contract paying guaranteed lifetime income and a death benefit guarantee (reduced proportionally by withdrawals)</li> </ul>	<ul style="list-style-type: none"> <li>■ Potential creditor protection</li> <li>■ Guaranteed lifetime income</li> <li>■ Ability to reset guaranteed amount higher if market value increases</li> </ul>	<ul style="list-style-type: none"> <li>■ Sales charges apply if liquidated</li> <li>■ Guarantees reduced proportionally by withdrawals</li> </ul>	<ul style="list-style-type: none"> <li>■ Add highly predictable income stream</li> <li>■ Suitable as part of a diversified fixed-income portfolio</li> </ul>
Annuity	<ul style="list-style-type: none"> <li>■ An insurance contract offering guaranteed income for life or for a fixed number of years</li> <li>■ Select to guarantee the income stream for a fixed number of years</li> <li>■ Annuity income is comprised of taxable interest and return of capital</li> </ul>	<ul style="list-style-type: none"> <li>■ Higher yields than regular GICs/ bonds</li> <li>■ Can create a tax-efficient income stream since only a portion of the income received is taxable</li> <li>■ Can provide continued income payments to your estate/ beneficiary for full fixed term</li> <li>■ Can provide a full return of your initial capital to your estate/ beneficiary (must qualify for life insurance)</li> </ul>	<ul style="list-style-type: none"> <li>■ Permanently locked in at current rates</li> <li>■ Annuity income terminates at death if there is no guarantee period or if the guarantee period has expired</li> <li>■ Must qualify for insurance for return of capital death benefit</li> </ul>	<ul style="list-style-type: none"> <li>■ Generate higher income</li> <li>■ Reduce taxation</li> <li>■ Eligible for federal income splitting</li> <li>■ Select an income stream for either a fixed period or for life, depending on your needs</li> <li>■ Suitable as part of a diversified fixed-income portfolio</li> </ul>

Greater stability

Higher income potential

Investment	What it is	Why choose it	What to consider	How to use it
Corporate bond	<ul style="list-style-type: none"> <li>■ A certificate issued by a corporation as evidence of debt it promises to repay in full at a certain date and rate of interest</li> <li>■ Investment-grade bonds rated BBB- or higher</li> <li>■ High-yield bonds rated BB+ or lower</li> </ul>	<ul style="list-style-type: none"> <li>■ Generally higher interest than GICs and government bonds (semi-annual)</li> </ul>	<ul style="list-style-type: none"> <li>■ Higher risk of default than government bonds</li> <li>■ Limited availability of quality issues</li> <li>■ Limited liquidity in adverse markets</li> </ul>	<ul style="list-style-type: none"> <li>■ Generate higher income</li> <li>■ Diversify between 6-8 issuers to reduce default risk</li> <li>■ Up to 25% portfolio allocation to investment-grade bonds suitable for conservative investors</li> </ul>
Hybrid bond	<ul style="list-style-type: none"> <li>■ A capital trust security issued by a financial institution that combines the features of preferred shares and corporate bonds</li> </ul>	<ul style="list-style-type: none"> <li>■ Pays higher fixed semi-annual interest to maturity than regular bonds</li> </ul>	<ul style="list-style-type: none"> <li>■ More junior in debt ranking than corporate bonds; i.e. in the event of liquidation, bonds are paid back first, then preferred shares/hybrid bonds</li> <li>■ Interest payments fully taxable</li> </ul>	<ul style="list-style-type: none"> <li>■ Generate higher income</li> <li>■ More tax-efficient income in tax-sheltered accounts (RRSPs, RRIFs)</li> </ul>
Preferred share	<ul style="list-style-type: none"> <li>■ A non-voting, non-profit-sharing share in a corporation entitling shareholders to a stated dollar value in the event of liquidation after creditors are paid</li> </ul>	<ul style="list-style-type: none"> <li>■ Pays a fixed, generally higher dividend than other share classes</li> <li>■ Canadian dividends taxed more favourably than interest due to the Dividend Tax Credit</li> </ul>	<ul style="list-style-type: none"> <li>■ Share prices decline when interest rates rise and credit spreads increase</li> <li>■ Yields usually higher than corporate bonds on an equivalent basis</li> <li>■ Less liquid than common shares</li> </ul>	<ul style="list-style-type: none"> <li>■ Generate higher tax-efficient income</li> <li>■ Generally regarded as part of corporate bond allocation in a diversified portfolio</li> </ul>
Tax-exempt insurance	<ul style="list-style-type: none"> <li>■ A life insurance contract that shelters assets from taxation and pays a death benefit</li> <li>■ Investment options may participate in policy dividends or may include guaranteed interest options, mutual fund-type managed funds or index-linked investments</li> </ul>	<ul style="list-style-type: none"> <li>■ Investment income grows tax-deferred within policy</li> <li>■ Can use the policy values as collateral for tax-free bank loans for income</li> </ul>	<ul style="list-style-type: none"> <li>■ Cash withdrawals may be subject to early withdrawal charges and/or taxation</li> <li>■ Bank loans are repaid at death by insurance benefit</li> <li>■ You must qualify for insurance</li> </ul>	<ul style="list-style-type: none"> <li>■ Suitable for surplus assets and/or to provide tax-free supplemental retirement income</li> </ul>
Real Estate Investment Trust (REIT)	<ul style="list-style-type: none"> <li>■ An equity investment that trades on a stock exchange but, unlike a common stock, pays out the majority of its cash flow to investors</li> </ul>	<ul style="list-style-type: none"> <li>■ Typically pays larger distributions than GICs or bonds</li> <li>■ Offers exposure to a basket of real estate assets</li> </ul>	<ul style="list-style-type: none"> <li>■ Distributions/values not guaranteed</li> <li>■ Distributions limit growth potential</li> <li>■ Higher interest rates can negatively impact performance</li> </ul>	<ul style="list-style-type: none"> <li>■ Potentially enhance income</li> <li>■ Include as part of equity component of diversified portfolio — not fixed-income</li> <li>■ Choose based on merits of underlying assets</li> </ul>
Common share	<ul style="list-style-type: none"> <li>■ An equity security that provides a share of a publicly traded company, share of profits and voting rights</li> </ul>	<ul style="list-style-type: none"> <li>■ Many stocks pay a regular dividend</li> <li>■ Long-term growth potential</li> <li>■ Canadian dividends and capital gains taxed at a lower rate than interest</li> </ul>	<ul style="list-style-type: none"> <li>■ Stock values and dividends are not guaranteed</li> </ul>	<ul style="list-style-type: none"> <li>■ Balance income with capital growth</li> <li>■ Create a more tax-efficient income stream</li> <li>■ Look for Canadian stocks with a history of increasing dividends</li> </ul>

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## UNDERSTAND HOW DIFFERENT INVESTMENTS ARE TAXED

Interest income from GICs and bonds is 100% taxable at your marginal tax rate, while capital gains and Canadian dividends receive preferential tax treatment, in a regular taxable account. What's more, you can offset capital gains with capital losses to reduce your taxes.

How much you keep after tax per \$1,000				
Taxable income	Up to \$44,000 Tax rate of 26.3%	\$44,000 – \$88,000 Tax rate of 36.1%	\$88,000 – \$136,000 Tax rate of 41.2%	Over \$126,000 + Tax rate of 44.9%
Interest/foreign income	\$737	\$639	\$588	\$551
Capital gains	\$869	\$820	\$794	\$775
Canadian dividends	\$970	\$845	\$777	\$728

Illustration only. Amounts are approximations based on the average Canadian marginal tax rate across all provinces and territories.

The benefit is longer-term bonds/ GICs historically tend to pay more, and you even out the effect of fluctuating interest rates, resulting in more predictable income.

- Shop the global marketplace for the best rates. Don't settle for the regular posted rates at your local financial institution. RBC Dominion Securities has access to many different GIC (and bond) issuers and can often secure higher rates.

### CONSIDER OTHER ALTERNATIVES

GICs and bonds aren't the only choices for your "safe money." Investments that bring together stability with enhanced income/return potential include insured annuities, corporate bonds, hybrid bonds, preferred shares, income trusts, and dividend-paying Canadian corporate shares.

And it's not an all-or-nothing proposition either. You can still hold

GICs and bonds in your portfolio for the exceptional stability they provide, while diversifying with some of these other investment alternatives to enhance your return/income potential.

*Contact us today to learn more about alternatives to GIC investing.*

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