Giving the Gift of Knowledge

Your guide to saving for a child's post-secondary education

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RBC Dominion Securities

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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.

A university graduate can expect to earn $1 million more during a 43-year career than someone who only completes high school, according to Statistics Canada.[1] Post-secondary graduates are also less likely to find themselves out of work — 2.7 times less likely according to the Canadian Council on Social Development — than are young people who have only a grade-school education.[2] Looking ahead, Human Resources and Social Development Canada (HRSDC) anticipates that almost two-thirds of new jobs will require some form of post-secondary education.[3]

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

The demand for post-secondary education can be seen in rapidly increasing enrolment rates across Canada. At the same time, however, costs are increasing even more rapidly.

By some estimates, tuition fees have almost tripled over the last 15 years.[4] With government support dwindling and costs continuing to spiral upward, HRSDC predicts that by 2019, a four-year undergraduate program away from home could cost more than $100,000.[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

› 93%
Percentage of parents with children aged 18 and under who want their children to achieve a post-secondary education, according to a 2002 Statistics Canada survey.[6]

› $71,980
Current average cost of a four-year university education away from home (HRSDC).[7]

› 50%
Percentage of parents who have a savings plan devoted specifically to paying for college or university expenses, according to a 2002 Statistics Canada survey.[8]

› 5.3% per year
Average increase in university tuition costs since 2000 (HRSDC).[9]

› $19,500
Average amount owed in government student loans by class of 2000 bachelor degree students when they graduated (Statistics Canada).[10]

› $32 billion
Total amount Canadian parents have saved for their children's post-secondary education costs, as of October 2002 (Statistics Canada).[11]

› 60%
Proportion of Canadians in the highest income bracket who possess a post-secondary degree, according to the 2001 Census (Statistics Canada).[12]

The Registered Education Savings Plan

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 Dominion Securities, 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 Dominion Securities, 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.

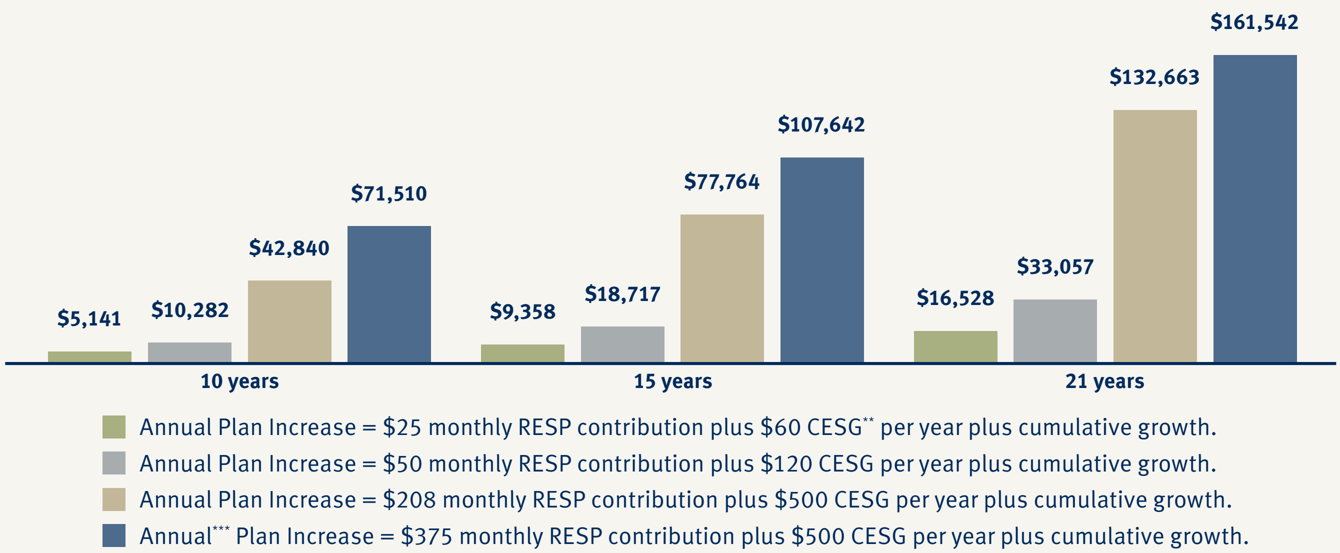
You can make lump-sum contributions at any time. You can also make contributions monthly or quarterly through a Pre-Authorized Contribution (PAC) program, which automatically transfers funds from your bank account.

You may make contributions to an RESP for up to 21 years and the plan can remain open for up to 25 years in total.

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).

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 7% 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 7% 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.

GOVERNMENT RESOURCES ONLINE

- The HRSDC site has information on saving for education: www.hrsdc.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/tax/individuals/topics/resp

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. 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 HRSDC 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 (RSP) or your spousal RSP. You must have available RSP 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

Establishing an RESP is an excellent way to save for a family member's post-secondary education. However, there are other strategies you may wish to consider, including saving through a non-registered account or creating a formal trust.

NON-REGISTERED SAVINGS

Parents sometimes simply choose to set up a separate savings or investment account of their own and "earmark" it for education. While this is easy, and allows you maximum control and flexibility, it has a number of drawbacks:

- All investment income is taxable in your hands. Therefore, there are no tax benefits to this approach to education savings.
- You will not receive the CESG or any other form of government assistance. You may be forfeiting thousands of dollars worth of grants over a period of years.
- It can be easier to put off contributions to a regular savings or investment account, or to make withdrawals for any number of "emergencies" that might come along.

If you are willing to forgo tax benefits and government grants to have this control and flexibility, it's important to be disciplined and resist the temptation to use the money for anything other than its original purpose: your child's education.

ESTABLISHING A FORMAL TRUST

In certain situations, it may be appropriate to consider an irrevocable "living" trust in addition to (or as an alternative to) an RESP.

This is a formal trust arrangement in which you (the "settlor") transfer one or more assets into a trust and provide instructions to those managing the trust (the "trustees") on how the assets will be used for the beneficiaries of the trust, e.g. your children. If the trust terms allow, other individuals may contribute assets to the trust. They are referred to as "contributors."

Formal trusts are becoming increasingly popular with grandparents who want to help their grandchildren financially, but also want to have a say in how the money is ultimately spent. You can establish a living trust for the benefit of anyone, including your children, grandchildren, nieces, nephews or family friends.

The main advantages of the formal trust structure are control, certainty of terms and the ability to deal with changing circumstances (such as the death of a trustee or beneficiary).

The trust document can stipulate that the money is to be paid out only for specific purposes, such as post-secondary education, or it may set out a distribution schedule that can span several years. Investments in the trust are managed by the trustee(s). For large trust accounts, appointing a corporate trustee (such as Royal Trust Corporation of Canada) ensures professional management and continuity for as long as the trust exists.

As the name suggests, an irrevocable trust cannot be changed or cancelled once you have set it up. While living trusts can be revocable, only irrevocable trusts benefit from advantageous tax treatment. Investment income earned by the trust and distributed to beneficiaries over the age of 18 will be taxable to them (typically at their lower tax rate). When the beneficiary who receives distributions from the trust is younger than 18, realized capital gains and second generation income will be taxable to him or her. Any other type of investment income will be attributed to the contributor of the trust. Investment income that is retained within the trust is taxed at the highest marginal tax rate.

The trust agreement that you draw up can permit many types of assets to be held within the trust, including cash, bank accounts, real estate, stocks, mutual funds, bonds and even shares in your business. If you intend to transfer existing assets into the trust, the transfer will be considered a disposition for tax purposes. As a result, if the investment has appreciated in value since your initial purchase, the transfer may trigger a taxable capital gain attributable to you.

Setting up a living trust involves some legal and administrative costs, and can be complicated compared to RESPs. For example, the trust must file a tax return every year. However, as described, living trusts offer a high degree of flexibility, control and some tax benefits to enhance your savings. Where significant sums are involved, or where control is a key concern, a living trust can be a good choice.

A MATTER OF DISCRETION

A living trust can be non-discretionary or discretionary. If it is non-discretionary, the terms of the trust direct the trustee when to pay out income or capital. This allows you to arrange for the beneficiary to receive a regular income over a given period of time — such as while he or she is enrolled in school. If it is discretionary, the trustee makes some or all of these decisions.

OPTIONS AT A GLANCE

Finding the best education savings strategy depends on your personal and family circumstances. Here is an overview of some of your options.

	RESP	Non-registered savings or investment account	Formal trust
Contribution limits	$50,000 lifetime per beneficiary	No restrictions	No restrictions
Eligible investments	Cash, GICs, stocks, bonds, mutual funds, professionally managed investments, etc.	› Savings account — cash › Investment account — full range of investments, including GICs, stocks, bonds, mutual funds, etc.	› As determined by trust agreement › The following are often eligible: cash, CSBs, GICs, stocks, bonds, mutual funds, real estate, shares in a business
CESG available?	Yes	No	No
Age restrictions	› Beneficiary must be under 21 when plan is opened › No additional contributions for beneficiaries over 20	None	Set by trust agreement
Who can contribute?	Subscriber	Anyone	Anyone
Tax treatment	› Tax-deferred investment growth › Earnings taxable to student when withdrawn	Interest, dividends and capital gains taxable to account holder	› Income retained in the trust is taxed at the highest marginal rate › Distributions to beneficiaries over 18 are taxable to them › If the beneficiary is younger than 18, realized capital gains distributed will be taxable to him or her, but all other distributed investment income will be taxable to the contributor
Use of funds	Plan earnings must be withdrawn to pay educational expenses or tax penalties may apply	No restrictions	No restrictions (other than those specified in the trust agreement)
Termination	The end of the 25th year following the year the plan was opened	No restrictions	› Perpetuity period of the trust, generally 21 years from commencement › Deemed disposition after 21 years, but there is no requirement to wind up the trust unless required by the trust document

Please note: This chart is for illustrative/comparative purposes only and may not contain all the information necessary for you to make your education investment decision. For more information, please consult with your Investment Advisor.

SAVINGS TIP

- Your child may be eligible for a scholarship. Check out some of the programs available at Scholarships Canada (www.scholarshipscanada.com) and Canadian and International Scholarships Programs (www.scholarships.gc.ca).

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:

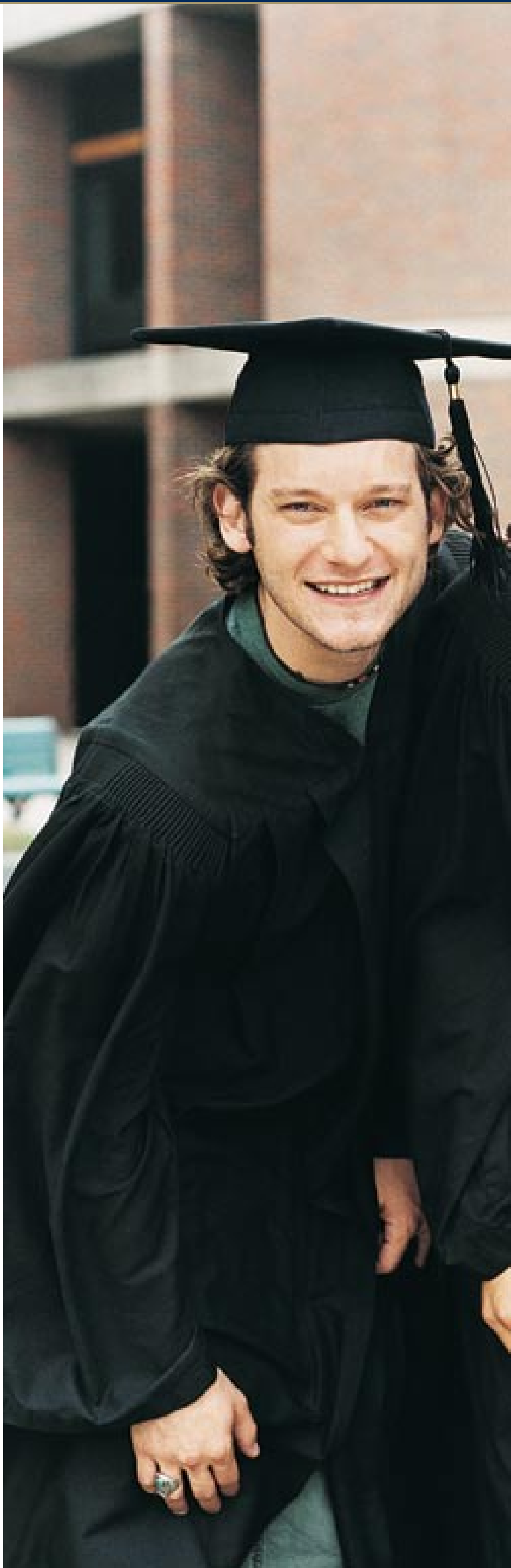
- It's a convenient, yet disciplined way to save.
- It gets your money working for you right away to maximize your opportunity for returns.
- With dollar-cost averaging, you don't need to worry about the "right time" to contribute because you're always investing.

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 Investment Advisor.



[1] Statistics Canada, 2001 Census.

[2] Canadian Council on Social Development, Labour Force Status by Education, 1996.

[3] Human Resources and Social Development Canada, Looking Ahead: A ten-year outlook for the Canadian labour market, 2004-2013 (October 2004).

[4] Statistics Canada, University Tuition Fees, Sept. 2, 2004.

[5] Calculation is based on the Human Resources and Social Development Canada (HRSDC) 2008/2009 estimated cost of $74,139 for a four-year university education away from home adjusted by HRSDC estimates of a 3% increase per year (HRSDC/CanLearn 2007).

[6] Statistics Canada, Survey of Approaches to Educational Planning, Nov. 20, 2003.

[7] HRSDC/CanLearn 2007, op.cit.

[8] Survey of Approaches to Educational Planning, op.cit.

[9] Looking Ahead: A ten-year outlook for the Canadian labour market, 2004-2013 (October 2004), op.cit.

[10] Statistics Canada, National Graduates Survey, April 26, 2004 (Report #81-595-MIE2004016, Survey #5012).

[11] Survey of Approaches to Educational Planning, op.cit.

[12] 2001 Census, op.cit.

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For more information, please speak with your Investment Advisor.

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