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GUARANTEED INVESTMENT FUNDS

Taxation

Desjardins Insurance
Life • Health • Retirement

Desjardins Insurance refers to Desjardins Financial Security Life Assurance Company.

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Caution

This document is provided for your convenience and for information purposes only. It does not constitute advice of any kind. The general information contained herein is subject to change without notice. This information is not to be relied upon for tax planning purposes.
We strongly suggest that you consult your legal and tax advisors to discuss the laws and regulations and how they apply to your particular circumstances. Desjardins Insurance will not be held responsible for any unwanted tax liability.

Unit holder / Contract owner

For simplicity purposes, the term unit holder is used in this document, whether we are referring to guaranteed investment funds or mutual funds. However, we would like to remind you that, unlike mutual funds, for guaranteed investment funds, a client owns a contract. Fund units are attributed to the contract, not to the client.

SECTION 1

Income allocation

Allocation rules for guaranteed investment fund income

Under the *Income Tax Act*, when the value of an insurer's life insurance reserves varies depending on the fair market value of a group of properties (commonly referred to as a segregated fund or guaranteed investment fund), a trust is created with respect to these funds. The properties and the income generated by these properties belong to the trust, not the insurer. The trust allocates the income and the gains it realizes over the course of a year to the contract owners. This income and these gains are reported on T3 tax slips (Relevé 16 in Quebec).

Unless otherwise indicated, the tax aspects and examples presented in this document refer to non-registered contracts.

For registered contracts (RRSPs or RRIFs), holders are taxed only when they withdraw from their contract, either partially or totally, or upon their death. However, contracts registered as TFSAs are treated differently: income and gains aren't taxable, unless earned after the holder's death.

A. Impacts for the contract owner

The income from a guaranteed Investment fund isn't allocated in cash or in units. The income is held by the fund, and the unit holder benefits in the form of changes to the value of their units. That means the number of units remains the same, unless more units are purchased or some are withdrawn.

The nature of the trust's income remains intact upon allocation. That means, for example, that interest income remains interest income. Interest income, dividends, foreign income, capital gains and capital losses are taxed as though they had been received directly by the unit holder. The units of a guaranteed investment fund trust are considered capital property for tax purposes; therefore, a capital gain or loss is calculated when units are disposed of, taking into account their adjusted cost base.

Here's how the **adjusted cost base (ACB)** is calculated each year, for each fund:

Purchase price of units

- \+ Income allocated (interest, foreign income and dividends) by the fund
- \+ Capital gains allocated by the fund (excluding capital gains on withdrawals)
- – Capital losses allocated by the fund (excluding capital losses on withdrawals)
- \+ Additional deposits
- – Cost of withdrawal

Unrealized gains[1] have no impact on the fund's ACB.

ACB – SO EASY TO CALCULATE!

You can obtain the ACB for units of a fund held by your clients on their semi-annual statement under Your DFS Guaranteed Investment Funds section.

[1] Increase in the value of the fund for a period with no corresponding income or capital gain at the tax level. This increase would become taxable, in the form of a capital gain, upon withdrawal or liquidation of the fund.

EXEMPLE[2]

Julia invests $100,000 in a non-registered guaranteed Investment fund contract and chooses a balanced fund. At the time of the investment, the adjusted cost base of her units equals the value of the investment (i.e., $100,000).

At the end of the year 1

The market value of Julia's contract is $110,000.[2]

The fund allocated the following income to her:[3]

- $1,000 in interest
- $1,000 in dividends
- $3,500 in realized capital gains (excluding capital gain on withdrawals)

Julia's ACB is now $105,500, calculated as follows: 100,000 + 1,000 + 1,000 + 3,500.

Since Julia has a non-registered contract, she receives a T3 (Relevé 16 in Quebec) tax slip allocating her portion of the fund's income.

Tax on allocated income and gains

TAX ON INTEREST:
$1,000 × 45% = $450

TAX ON DIVIDENDS:
$1,000 × 29% = $290

TAX ON CAPITAL GAINS:
$3,500 × 50% × 45% = $788

Total Tax = $1,528

So for Year 1, Julia will have to pay $1,528 in tax on the allocated income and gains.

2 Assuming a positive annual return for the first two years and a negative return for the third year, a marginal tax rate of 45% and a marginal tax rate of 29% (for eligible dividends). The contract's market value can go up or down based on the value of the funds and the guarantee chosen by your client. Please refer to section 4 of the Contract and Information Folder for more information on the calculation of the market value.

3 For more information about fund income allocation rules, refer to Part B in this section.

Year 2[4]

January 5

Julia redeems $4,202.50. After the partial withdrawal of units of her contract, the market value (MV) of her units is $110,000 – $4,202.50 = $105,797.50. The ACB must also be adjusted:

$$\begin{aligned} \text{ACB} &= \text{ACB prior to withdrawal} - \text{withdrawal-related adjustment} \\ &= 105{,}500 - \text{withdrawal} \times (\text{ACB}^{\text{prior to withdrawal}} / \text{MV}^{\text{prior to withdrawal}}) \\ &= 105{,}500 - 4{,}202.50 \times (105{,}500 / 110{,}000) \\ &= 105{,}500 - 4{,}031 \end{aligned}$$

ACB = $101,469

TAX RELATED TO WITHDRAWAL
Gain realized on withdrawal × 50% × 45% (4,202.50 – 4,031) × 50% × 45% = $39

At the end of the year

The market value of Julia's contract is $114,750.

The income allocated to Julia for year 2 (not including the capital gain arising from the withdrawal) is as follows:

- $1,000 in interest
- $1,000 in dividends
- $3,500 in realized capital gains

Julia's ACB is now $106,969, calculated as follows: 101,469 + 1,000 + 1,000 + 3,500.

Tax on allocated income and gains

TAX ON INTEREST:
$1,000 × 45% = $450

TAX ON DIVIDENDS:
$1,000 × 29% = $290

TAX ON CAPITAL GAINS:
$3,500 × 50% × 45% = $788

Tax = $1,528

That means **for year 2, Julia's total tax bill comes to $1,567**, i.e., $39 in tax on the withdrawal and $1,528 in tax on allocated income and capital gains. The capital gain arising from the withdrawal and the other income and capital gains allocated by the fund will be reported on the T3 slips issued to Julia (Relevé 16 in Quebec).

[4] When a unit holder realizes a capital gain from withdrawing their units and the segregated fund trust has capital gains to allocate, the trust's capital gains are first allocated to unit holders who have requested a withdrawal of units. If there is a balance remaining to be allocated, it is allocated to unit holders in accordance with the fund's allocation method (explained later on in this Guide). That's why capital gains arising from withdrawals are also reported on T3 slips (Relevé 16 in Quebec). For more information, see Part B in this section.

Year 3

At the beginning of the year

Julia deposits $50,000.

Further to this deposit, the market value of her contract is $164,750 (114,750 + 50,000) and her ACB is $156,969, calculated as follows: 106,969 + 50,000.

At the end of the year

The market value of Julia's contract is $174,750.

The only income allocated to Julia (not including the capital gain arising from the withdrawal below) is $10,000 in interest income. Her ACB is $166,969 (156,969 + 10,000).

Julia redeems all of her investment ($174,750).

Given the difference between the market value of the units and the ACB (174,750 – 166,969), Julia will receive a capital gain of $7,781. Her T3 (Relevé 16 in Quebec) slip will show interest income of $10,000 and a capital gain of $7,781.

Tax on allocated income and gains

TAX ON INTEREST:
$10,000 × 45% = $4,500

TAX ON CAPITAL GAINS:
$7,781 × 50% × 45% = $1,751

Total tax = $6,251

After redeeming all units in her contract, the market value and the ACB of Julia's fund revert to 0.

NEGATIVE RETURN, CAPITAL LOSS... AND CAPITAL GAIN

Remember, a fund can post a negative return even while it generates income, including gains realized on transactions. Unit holders will note that losses are allocated to them on their tax slips.

In addition, **some funds may also generate capital gains, despite a negative annual return**. Capital gains will therefore be reported on the T3 (Relevé 16 in Quebec) tax slips of unit holders who invested in these funds.

B. How does a fund allocate its income and gains?

As mentioned in the previous example, guaranteed Investment fund income is allocated to the unit holders each year as prescribed by the *Income Tax Act*. This law doesn't stipulate any income allocation method. Tax authorities assume that insurance companies will use a reasonable method.

The method used by several insurers, including Desjardins Assurances, is based on the number of units held at the end of each month (interest and dividend income) and the number of units held at the end of the year (capital gain and loss).

Income is allocated in two stages, based on the type of income:

- STAGE 1: **Allocation of interest and dividend income**
- STAGE 2: **Allocation of capital gains and losses**

Here is the example of fund XYZ, which is about to allocate the income generated during the year to unit holders.

FUND XYZ – ALLOCATION OF INCOME AND GAINS

	Daniel	Larry	Lucy	Ann	Patrick	TOTAL
Balance - January 1						
Units	1,000	1,000	1,000	1,000	-	4,000
ACB	$90,000	$100,000	$110,000	$100,000	-	$400,000
Sale - July 15						
Units				-1,000		
Proceeds from sale				$106,000		
Purchase - November 15						
Units					1,000	
ACB					$106,000	
Balance - December 31						
Units	1,000	1,000	1,000	-	1,000	4,000
ACB	$90,000	$100,000	$110,000	-	$106,000	$406,000
Market value	$106,000	$106,000	$106,000	-	$106,000	$424,000
Time-weighted Units (income)	12,000	12,000	12,000	6,000	2,000	44,000

The fund generated the following income:[5]

Interest	**$6,000**
Dividends[6]	**$2,000**
Capital gains	**$24,000**
Capital losses	**$4,000**

[5] We have assumed that the fund does not earn foreign income.

[6] We have assumed that all dividends received by this fund were eligible dividends.

STAGE 1: INTEREST AND DIVIDEND INCOME ALLOCATIONS

Interest and dividend income are allocated to all clients who held units at the end of each month during the year. Therefore, clients who redeemed units are allocated interest and dividend income even if he still doesn't hold units at year end.

INTEREST AND DIVIDENDS

On the Canada Revenue Agency T3 slip, interest income is reported in box 26 and dividend income in box 23 (for non-eligible dividends) or in box 49 (for eligible dividends). Foreign income will instead be entered in boxes 25 and 34.[7]

Daniel
Interest: $6,000 × 12,000 / 44,000 = $1,636
Dividends: $2,000 × 12,000 / 44,000 = $545

Larry
Interest: $6,000 × 12,000 / 44,000 = $1,636
Dividends: $2,000 × 12,000 / 44,000 = $545

Lucy
Interest: $6,000 × 12,000 / 44,000 = $1,636
Dividends: $2,000 × 12,000 / 44,000 = $545

Ann
Interest: $6,000 × 6,000 / 44,000 = $818
Dividends: $2,000 × 6,000 / 44,000 = $273

Patrick
Interest: $6,000 × 2,000 / 44,000 = $273
Dividends: $2,000 × 2,000 / 44,000 = $91

Calculating adjusted cost base (ACB) after stage 1

Stage 1 - Allocation of income	Daniel	Larry	Lucy	Ann	Patrick	TOTAL
Income (interest + dividends)	2,181	2,181	2,181	1,091	364	8,000
ACB	92,181	102,181	112,181	101,091	106,364	412,907

STAGE 2: ALLOCATION OF CAPITAL GAINS AND LOSSES

Stage two of the allocation of guaranteed Investment fund income consists of allocating the capital gains and losses. This stage has two distinct phases.

PHASE 1: Gains and losses realized by unit holders

Capital gains and losses are first allocated to clients who redeemed their units and correspond to the gains or losses they realized at that time.

Thus, a capital loss is reported on the tax slip of clients who realized a loss on withdrawal. Similarly, a capital gain is reported on the tax slip of a client who disposed of units whose value was greater than the adjusted cost base.

[7] Taxable amount (grossed-up) of the dividend is included in income, but a dividend tax credit is avaible. For an eligible dividend, these amounts are respectivley in boxes 50 and 51 of the T3 (boxes 32 and 39 of the T3 for dividends other than eligible dividends).

PHASE 1: Gains and losses realized by the client

Ann sold her units for $106,000.

Her ACB was $101,091 after the allocation of interest and dividends (Stage 1).

Proceeds from withdrawal	$106,000
ACB	– $101,091
Capital gains	**$4,909**

Calculation of available gains for remaining units

Realized capital gains	$24,000
Capital gains allocated to Ann	– $4,909
Unallocated capital gains	**$19,091**

Calculation of available losses for remaining units

Realized capital losses	$4,000
Allocated capital losses	$0
Unallocated capital losses	**$4,000**

The next phase of the allocation of capital gains and losses consists of allocating these to **all clients who hold units at December 31**. These gains and losses were generated by transactions made by the fund managers.

PHASE 2: Gains and losses realized by the fund

Gains or losses that remain after Phase 1 are allocated to all clients who hold units at December 31, based on the number of units they hold.

Daniel
Gains: $19,091 × 1,000 / 4,000 = $4,773
Losses: $4,000 × 1,000 / 4,000 = $1,000

Larry
Gains: $19,091 × 1,000 / 4,000 = $4,773
Losses: $4,000 × 1,000 / 4,000 = $1,000

Lucy
Gains: $19,091 × 1,000 / 4,000 = $4,773
Losses: $4,000 × 1,000 / 4,000 = $1,000

Ann
Gains: $19,091 × 0 / 4,000 = $0
Losses: $4,000 × 0 / 4,000 = $0

Patrick
Gains: $19,091 × 1,000 / 4,000 = $4,773
Losses: $4,000 × 1,000 / 4,000 = $1,000

Stage 2: Allocation of capital gains and losses	Daniel	Larry	Lucy	Ann	Patrick	TOTAL
ACB after stage 1	$92,181	$102,181	$112,181	-	$106,364	$412,907
Gain	$4,773	$4,773	$4,773	-	$4,773	$19,091
Loss	$1,000	$1,000	$1,000	-	$1,000	$4,000
Year-end ACB	$95,955	$105,955	$115,955	-	$110,136	$428,000

CAPITAL GAINS AND LOSSES

On the Canada Revenue Agency T3 slip, capital gains are reported in box 21 and capital losses in box 37. In Quebec, the net amount of capital gains and losses are reported in box A of the Relevé 16 slip.

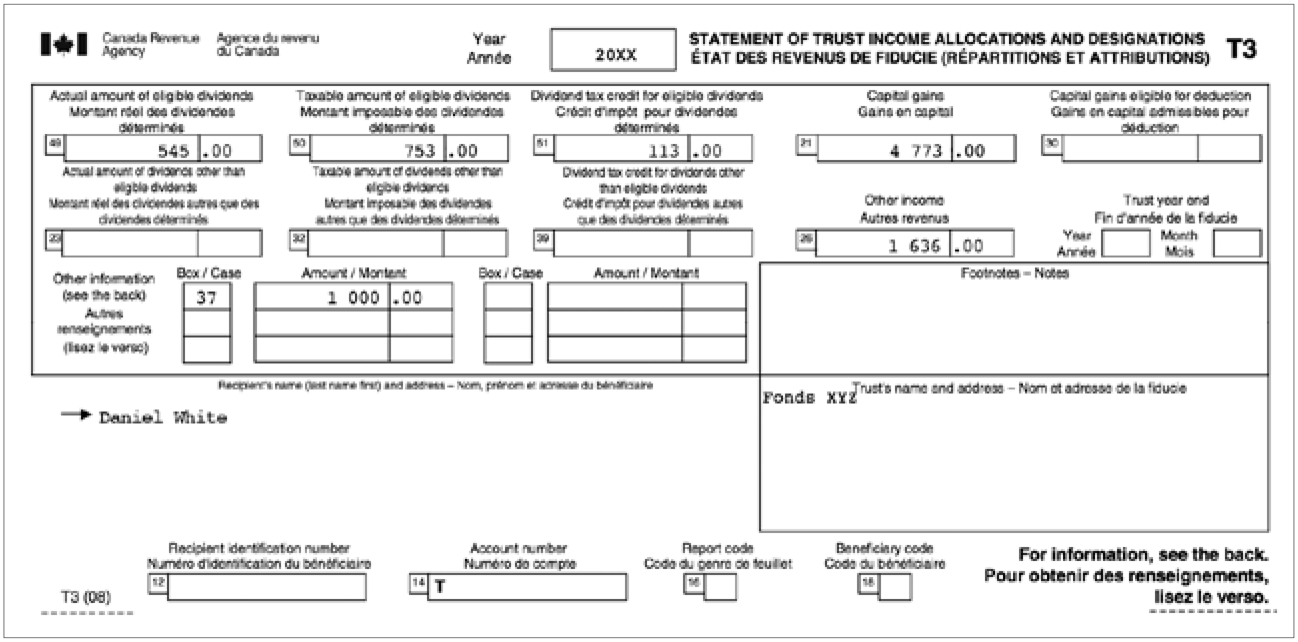
Summary

The income and gains to be allocated to each client at year end are as follows:

	Daniel	Larry	Lucy	Ann	Patrick	TOTAL
Interest	1,636	1,636	1,636	818	273	6,000
Dividends	545	545	545	273	91	2,000
Capital gains	4,773	4,773	4,773	4,909	4,773	24,000
Capital losses	1,000	1,000	1,000	0	1,000	4,000

As the above table shows, Daniel, Larry and Lucy were allocated the most income, since they held their units for the whole year. Ann and Patrick received a portion of this income depending on the number of months they held their shares. In addition, a capital gain was allocated to Ann following the sale of her units, and the other clients received the excess gains and losses based on the number of units they held at December 31.

Here is the T3 slip that will be sent to Daniel by the fund XYZ administrator.


Canada Revenue Agency / Agence du revenu du Canada
Year / Année: 20XX
STATEMENT OF TRUST INCOME ALLOCATIONS AND DESIGNATIONS / ÉTAT DES REVENUS DE FIDUCIE (RÉPARTITIONS ET ATTRIBUTIONS) — T3

49	Actual amount of eligible dividends / Montant réel des dividendes déterminés	545.00
50	Taxable amount of eligible dividends / Montant imposable des dividendes déterminés	753.00
51	Dividend tax credit for eligible dividends / Crédit d'impôt pour dividendes déterminés	113.00
21	Capital gains / Gains en capital	4 773.00
30	Capital gains eligible for deduction / Gains en capital admissibles pour déduction	
23	Actual amount of dividends other than eligible dividends / Montant réel des dividendes autres que des dividendes déterminés	
32	Taxable amount of dividends other than eligible dividends / Montant imposable des dividendes autres que des dividendes déterminés	
39	Dividend tax credit for dividends other than eligible dividends / Crédit d'impôt pour dividendes autres que des dividendes déterminés	
26	Other income / Autres revenus	1 636.00

Trust year end / Fin d'année de la fiducie — Year / Année; Month / Mois

Other information (see the back) / Autres renseignements (lisez le verso)

Box / Case	Amount / Montant	Box / Case	Amount / Montant
37	1 000.00		

Footnotes – Notes

Recipient's name (last name first) and address – Nom, prénom et adresse du bénéficiaire: Daniel White

Trust's name and address – Nom et adresse de la fiducie: Fonds XYZ

Recipient identification number / Numéro d'identification du bénéficiaire (12)
Account number / Numéro de compte (14): T
Report code / Code du genre de feuillet (16)
Beneficiary code / Code du bénéficiaire (18)

T3 (08)

For information, see the back. Pour obtenir des renseignements, lisez le verso.

USING CAPITAL LOSSES STRATEGICALLY

With GIFs, unlike mutual funds, capital losses that exceed realized capital gains can be allocated and used strategically. Unit holders can choose the best time to apply their losses (net of realized gains in the current taxation year) in order to offset their other capital gains, either:

- or one of the last three fiscal years; or
- for a subsequent fiscal year, indefinitely.

SECTION 2

Taxation of guarantees

Tax treatment of GIF contracts[8]

GIFs are sold as contracts that include maturity and death benefits.

These contracts offer a minimum maturity and death benefits equal to 75% of the deposits made in the contract. In addition to maturity and death benefits, GIF contracts also offer options that guarantee the payment of a stable income.

Even though the specific features of one contract may vary from the next, the basic tax principles remain the same.[9]

TAX INFORMATION DOCUMENT

For holders of **non-registered** contracts, any gains or losses not reported on a T3 slip (Relevé 16 in Quebec) will be detailed in a tax information document.

Tax information documents include the details of various gains and/or losses not allocated by the fund in relation to the following:

A. **Guarantee payments**
B. **Sales charges**
C. **Surrender charges**
D. **Guarantee fees (additional guarantee fees)**

Tax information documents are only sent to unit holders who have gains or losses related to one or more of the items above for a given fiscal year. They'll receive the document along with their T3 slips (Relevé 16 in Quebec). Holders of registered contracts won't receive one, since the tax treatment of their contracts is different.

[8] The examples in this section assume a marginal tax rate of 45%.

[9] Please refer to the contract and information folder for contracts issued by Desjardins Insurance for more information about the maturity and death benefits provided under these contracts.

A. Guarantee payments

Important

Tax authorities haven't yet ruled on the tax treatment of Guaranteed Lifetime Withdrawal Benefits (GLWBs), Guaranteed Minimum Withdrawal Benefits (GMWBs) or similar guarantee payments made under GIF contracts after all units in contract have been withdrawn. We believe our proposed tax treatment is appropriate. However, unit holders are responsible for ensuring that any such payments are properly reported on their income tax returns and that all associated taxes are paid. Desjardins Insurance cannot be held liable for any consequences relating to the tax treatment of these payments should the authorities decide on a different treatment. Please consult your tax advisor.

Guarantee payments include any payments made by the company in relation to a guarantee offered under a contract. They must be reported on the unit holder's income tax return, even if a T3 slip (Relevé 16 in Quebec) isn't issued for them.

Any non-GLWB Guarantee payments made in the unit holder's lifetime[10] (e.g., benefits paid under a 75/100 i or 100/100 r guarantee or fee refunds for the 100/100 r guarantee) will affect the adjusted cost base (ACB), just like any other deposit.

Unless otherwise indicated, the examples in this guide are based on the following:

Unit holder	**Mary, age 65**
Contract	**Helios2**
Guarantee	**Helios2 – 75/100 i**
Deposit amount	**$100,000**
Contract type	**Non-registered**
Beneficiary	**Her husband, Thomas**
Fund	**DFS GIF – Balanced**

[10] The assumption is that the contract owner and the annuitant are the same person.

MATURITY BENEFIT

As a general rule, the maturity benefit of a contract (or a deposit) is a percentage of the initial value of each deposit made into the contract. It is paid out at a time specified in the contract. For Helios 2 – 75/100 i, the maturity benefit is 75% of the initial value of each deposit on the annuitant's 105th birthday.

The maturity benefit is paid to the contract owner in the form of a top-up (units added to their contract), thereby increasing the contract value and the ACB of the units.

If the contract is **not registered**, the top-up must be treated as a capital gain (subject to a 50% tax rate) for the fiscal year in which it was received. For example, if the market value of Mary's contract was $65,000 at maturity, Desjardins Insurance would add additional units equaling to $10,000 [($100,000 × 75%) – $65,000] to her contract. Mary would receive a tax information document reporting this capital gain, which she would need to include in her income for the year. As you will see later, the tax information document will also indicate a capital loss resulting from the additional guarantee fees that Mary paid and which will then be deductible against this capital gain.

However, if the contract is **registered** (as an RRSP or RRIF), the top-up wouldn't have an immediate tax impact, since taxation only occurs if funds are withdrawn or at the time of death. For a contract registered as a TFSA, the top-up wouldn't be taxable.

Case study: Helios contract with a guarantee 100/100 r[11]

With the guarantee 100/100 r, a portion of the maturity benefit fees will be refunded if the deposit's market value exceeds its guaranteed value at maturity. The refund is paid to the holder in the form of units added to the contract. However, if the market value is lower than the guaranteed value, a benefit will be paid at maturity. For more information about this guarantee, please consult webi.ca.

[11] This example does not take into consideration income and other capital gains and losses that could have been allocated by the funds in the year.

a. If the market value is lower than the guaranteed value

Date	Transaction	Market value before transaction	Market value after transaction	ACB before transaction	ACB after transaction	Capital gains (losses) arising from withdrawals made to pay additional guarantee fees	Accumulated additional guarantee fees	Capital gains arising from guarantee payments
20XX-08-31	$110 in additional guarantee fees	$110,000	$109,890	$120,000	$119,880	loss of ($10)	$11,110	**$0**
20XX-09-30	$100 in additional guarantee fees	$100,000	$99,900	$119,880	$119,760	loss of ($20)	$11,210	**$0**
20XX-10-12	Maturity benefit of guarantee 100/100 r ($27,318 in the form of a deposit)	$102,682	$130,000	$119,760	$147,078	$0	$0	**$27,318**
20XX-10-31	$135 in additional guarantee fees	$135,000	$134,865	$147,078	$146,931	loss of ($12)	$135	**$0**
20XX-11-30	$132 in additional guarantee fees	$132,000	$131,868	$146,931	$146,784	loss of ($15)	$267	**$0**
20XX-12-31	$130 in additional guarantee fees	$130,000	$129,870	$146,784	$146,637	loss of ($17)	$397	**$0**

Capital gain for 20XX arising from the guarantee payment (taxable capital gain of $13,659)		**$27,318**
Capital loss for 20XX arising from additional guarantee fees (net capital loss of $5,605)		**($11,210)**
Capital loss for 20XX arising from withdrawals to pay additional guarantee fees (net capital loss of $37)		**($74)**

For 20XX, the unit holder has to include the $27,318 capital gain arising from the guarantee payment. However, as will be explained later, he can deduct from this gain the $11,210 capital loss arising from additional guarantee fees and the $74 capital loss ($10 + $20 + $12 + $15 + $17) arising from the withdrawals made to pay these fees.

b. If the market value is higher than the guaranteed value

Mark invested $100,000 in a non-registered Helios contract. He chose the guarantee 100/100 r, which gives him a guaranteed value of $100,000 at maturity.

After 10 years, the market value of his contract is $120,000 and his ACB is $110,000. He has paid $11,000 in fees related for this guarantee. Since his contract's market value exceeds the guaranteed value, Mark is entitled to a 30% refund of the 100/100 r guarantee's maturity benefit fees (50% of the total fees).

As a result, $1,650 ($11,000 × 50% × 30%) worth of units is added to his contract, bringing the market value of his contract to $121,650 and his ACB to $111,650.

Mark will receive a tax information document reporting a $1,650 capital gain and a $1,650 capital loss related to a portion of the Guarantee fees he's paid since his contract was first set up (discussed later). **Even though he'll need to report both of those amounts on his income tax return, Mark won't have to pay any tax on the fee refund.**

DEATH BENEFIT

In addition to the maturity benefit, GIF contracts also include a guaranteed value that is paid to the beneficiary upon the annuitant's death. The Helios2 – 75/100 i death benefit is 100% of the initial value of each deposit. Up to the annuitant's 75th birthday, the death benefit is also reset every year to the higher of the market value, inflation-adjusted value or the initial value of the deposits.

Under the *Income Tax Act*, the deceased is deemed to have disposed of their contract at its fair market value at the time of their death. The value of the disposition is the higher of the contract's market value at death or the guaranteed death benefit. The gain arising from the disposition is taxed in the hands of the unit holder,[12] and the contract is closed.

Let's assume that when Mary dies, the market value of her contract is $80,000, her guaranteed minimum death benefit is $110,000[13] and the ACB of her contract is $90,000. Because the market value of the contract is lower than its guaranteed value, the $110,000 death benefit is paid to the beneficiary.

Mary's final income tax returns will need to include the impact of the presumed disposition of her contract at fair market value, which breaks down as follows:

A capital loss attributable to the decrease in the market value of the contract when the units were withdrawn[14] will be reported on T3 slips (Relevé 16 in Quebec) along with the other income and capital gains/losses allocated by the fund. The amount of the loss will be $10,000, which is the contract's market value less its ACB ($80,000 – $90,000).

The capital gain attributable to the guarantee payment will be reported on the tax information document. It will be $30,000, which is the amount of the guaranteed minimum death benefit less the market value of the contract ($110,000 – $80,000).

As will be explained later, the tax information document will also include a capital loss arising from the additional guarantee fees that Mary paid, which will be deductible. This is assuming that Mary paid $10,000 in additional guarantee fees that she hadn't previously deducted.

[12] It is the unit holder, not the designated beneficiary, who is taxed. It is assumed in this case that the unit holder and the annuitant are the same person. Any income generated by the contract between when the unit holder dies and when the units are withdrawn is taxable in the hands of the beneficiary.

[13] Please refer to the Contract and Information Folder for more information about the death benefit under Helios2 – 75/100 i.

[14] Any income generated by the contract after the unit holder's death has to be reported in the beneficiary's income.

That all boils down to a net capital gain of $10,000 (–$10,000 + $30,000 – $10,000). The tax owed by Mary on that net capital gain is calculated as follows:
TAX = $10,000 × 50% × 45% = $2,250

However, there will be no tax impact for her beneficiary, Thomas, apart from taxes owed on any income generated by the contract after Mary's death.[15]

Registered contracts

The example we just looked at involved a non-registered contract. What about registered contracts?

The guarantee works the same way and the death benefit is paid to the beneficiary.

However, for an RRSP or RRIF, if the beneficiary isn't an eligible beneficiary (the spouse or common-law partner or a dependent child or grandchild of the contract owner), the higher of the market value of the contract at death[16] or the minimum guaranteed death benefit will be added to the taxable income reported on the deceased's final income tax return.

Example: Taxes owing upon death on an RRSP or RRIF

Market value of the RRSP at death = $300,000
Minimum guaranteed death benefit = $250,000
Marginal tax rate = 45%

- **Scenario 1: Death with no eligible beneficiary**
  Since an eligible beneficiary wasn't designated, the market value of the RRSP at death is added to the deceased's taxable income.
  TAX OWING BY THE DECEASED 45% × the market value of the RRSP at death 45% × $300,000 = $135,000
- **Scenario 2: Death with a spouse or common-law partner as the sole beneficiary**
  The deceased's RRSP is transferred tax-free to the spouse or common-law partner's RRSP.
  TAX OWING BY THE DECEASED = $0

Example: Taxes owing upon death on a TFSA

There is no tax payable on the higher of the market value of the contract at death[17] or the minimum guaranteed death benefit. Where the spouse or common-law partner is the beneficiary of the contract, the fair market value at the time of death may be transferred to a TFSA without reducing the contribution room, provided the prescribed conditions are met and the CRA's form is completed.

GUARANTEED LIFETIME WITHDRAWAL BENEFIT

In addition to the maturity and death benefits, Helios2 – 75/100 GLWB offers a guaranteed lifetime withdrawal benefit.

As a general rule, with non-registered contracts, a withdrawal made under a guaranteed withdrawal benefit is considered a regular withdrawal from the contract. That means it's necessary to determine whether it generates a capital gain or a capital loss.

However, bear in mind that the fund's income and gains will continue to be allocated annually to contracts to which a guaranteed withdrawal benefit has been added.

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[15] Any income generated by the contract after the unit holder's death has to be reported in the beneficiary's income.

[16] Any income generated by the contract after the unit holder's death is taxable in the hands of the beneficiary. For registered contracts, tax slips will be issued for this income.

[17] Any income generated by the contract after the unit holder's death is taxable in the hands of the beneficiary. The necessary tax slips will be issued.

Mary, age 65, chose the Helios2 – 75/100 GLWB precisely for the guaranteed withdrawal benefit. When her contract was set up, the GLWB protected value, the GLWB bonus base and her ACB were all $100,000. She made no withdrawals in Year 1 of her contract.

December 31 (Year 1)

The market value of Mary's contract is $110,000. The fund allocated the following income to her:

- $1,000 in interest
- $1,000 in dividends
- $3,500 in realized capital gains

Mary's ACB is now $105,500, calculated as follows: $100,000 + $1,000 + $1,000 + $3,500.

Since Mary made no withdrawals, she's entitled to a GLWB bonus equal to 2.5% of the GLWB bonus base, or 2.5% of $100,000, which raises the GLWB protected value to $102,500. Since Mary's contract isn't registered, she'll receive T3 tax slips (Relevé 16 in Quebec) allocating her share of income from the fund.

WILL A BONUS TRIGGER A TAX PAYMENT?

Adding a bonus to the protected value or **resetting** the protected value has **no tax impact** at the time the event occurs.

Tax on allocated income and gains

TAX ON INTEREST:
$1,000 × 45% = $450

TAX ON DIVIDENDS:
$1,000 × 29% = $290

TAX ON CAPITAL GAINS:
$3,500 × 50% × 45% = $788

Total tax = $1,528

Year 2

January 5

Mary wants to make her first withdrawal. The market value of Mary's contract is still $110,000. She recently turned 65, and her annual GLWB withdrawal percentage is 4.1%. Mary decides to withdraw her full GLWB maximum amount: $4,202.50 (4.1% × $102,500). Mary will have to include the gain realized on the withdrawal in her income tax return.[18]

[18] When a unit holder realizes a capital gain from withdrawing their units and the segregated fund trust has capital gains to allocate, the trust's capital gains are first allocated to unit holders who have requested a withdrawal of units. If there is a balance, it is allocated to unit holders in accordance with the fund's allocation method (explained earlier on in this guide). That's why capital gains arising from withdrawals are also reported on T3 slips.

TAX RELATED TO THE WITHDRAWAL
Gain realized upon withdrawal × 50% × 45%
= \$4,202.50 × (1 – ACB$^{\text{prior to withdrawal}}$ / MV$^{\text{prior to withdrawal}}$) × 50% × 45%
= \$4,202.50 × (1 – \$105,500 /÷ \$110,000) × 50% × 45%
= \$39

The market value of Mary's contract is now \$105,797.50 and its GLWB protected value remains \$102,500.

The withdrawal means a change to her ACB:

ACB = ACB prior to withdrawal – withdrawal-related adjustment
= \$105,500 – withdrawal × (ACB$^{\text{prior to withdrawal}}$ / MV$^{\text{prior to withdrawal}}$)
= \$105,500 – \$4,202.50 × (\$105,500 / \$110,000)

ACB = \$101,469

At year-end

The market value of Mary's contract is \$114,750.

The income attributed to Mary for year 2, in addition to the capital gain arising from the withdrawal, is as follows:

- \$1,000 in interest
- \$1,000 in dividends
- \$3,500 in realized capital gains

Mary's ACB is now \$106,969, calculated as follows: \$101,469 + \$1,000 + \$1,000 + \$3,500.

Tax on allocated income and gains

TAX ON INTEREST:
\$1,000 × 45% = \$450

TAX ON DIVIDENDS:
\$1,000 × 29% = \$290

TAX ON CAPITAL GAINS:
\$3,500 × 50% × 45% = \$788

Tax = \$1,528

So for year 2, Mary's total bill comes to \$1567 (\$39 in tax on the withdrawal and \$1528 in tax on allocated income and capital gains).

The capital gain arising from the withdrawal and the other income and capital gains allocated by the fund will be reported on the T3 slips (Relevé 16 in Quebec) issued to Mary.

Recap

Let's compare with the example in section 1, where Julia made a withdrawal from a contract that didn't have a GLWB.

	Julia (withdrawal without GLWB)	Mary (withdrawal with GLWB)
Amount withdrawn	$4,202.50	$4,202.50
Tax on withdrawal	$39	$39
Tax on allocated income and gains	$1,528	$1,528
Total tax	$1,567	$1,567

Julia and Mary will have the same tax bill for year 2.

B. Sales charges[19]

Some Contracts come with a negotiable sales charge option.[20] Unlike mutual fund fees, these charges won't increase the ACB of the units in a GIF contract. They're deductible as capital losses in years where the unit holder makes a withdrawal from their contract.[21]

THE CAPITAL LOSS IS THE LESSER OF:

1. **Accumulated sales charges × (withdrawal/market value prior to withdrawal)**
2. **Sales charges not deducted prior to the withdrawal (in other words: accumulated sales charges – deductions for previous withdrawals)**

Date	Transaction	Market value before transaction	Market value after transaction	ACB before transaction	ACB after transaction	Capital gains (losses) arising from withdrawals	Sales charges not deducted prior to transaction	Sales charges not deducted after transaction	Accumulated sales charges	Capital losses arising from sales charges
20XX-01-01	$100,000 initial deposit Negotiated rate of 3%	$0	$97,000	$0	$97,000	$0	$0	$3,000	$3,000	**$0**
20XX-05-05	$10,000 withdrawal	$110,000	$100,000	$97,000	$88,182	$1,182	$3,000	$2,727	$3,000	**($273)[22]**
20XX-06-06	$20,000 deposit Negotiated rate of 3%	$110,000	$129,400	$88,182	$107,582	$0	$2,727	$3,327	$3,600	**$0**
20XX-09-09	$100,000 withdrawal	$115,000	$15,000	$107,582	$14,032	$6,450	$3,327	$197	$3,600	**($3,130)[23]**

Capital loss for 20XX arising from sales charges (net capital loss of $1,702)	**($3,403)**
Capital gain for 20XX arising from withdrawals (taxable capital gain of $3,816)	**$7,632**

For 20XX, the unit holder can deduct the $3,403 capital loss ($273 + $3,130) arising from sales charges from the $7,632 capital gain ($1,182 + $6,450) realized on the withdrawals.

C. Surrender charges[24]

Surrender charges paid by the unit holder on withdrawals are deductible as capital losses at the time of withdrawal.[25]

Date	Transaction	Market value before transaction	Market value after transaction	ACB before transaction	ACB after transaction	Capital gains (losses) arising from withdrawals	Surrender charges	Capital losses arising from surrender charges
20XX-01-01	$100,000 initial deposit	$0	$100,000	$0	$100,000	$0	$0	**$0**
20XX-05-05	$10,000 withdrawal (No surrender charges due to the "up to 12% of units" exemption)	$110,000	$100,000	$100,000	$90,909	$909	$0	**$0**
20XX-09-09	$100,000 withdrawal ($4,900 in surrender charges)	$115,000	$15,000	$90,909	$11,858	$20,949	$4,900	**($4,900)**

Capital loss for 20XX arising from surrender charges (deductible caPital loss of $2,450)	**($4,900)**
Capital gain for 20XX arising from withdrawals (taxable capital gain of $10,929)	**$21,858**

For 20XX, the unit holder can deduct the $4,900 capital loss arising from surrender charges from the $21,858 capital gain ($909 + $20,949) realized on the withdrawals.

19 This example does not take into consideration income and other capital gains and losses that could have been allocated by the funds in the year.

20 Series 5A, 3A and 1A.

21 Capital losses are deductible only against capital gains.

22 Lesser of 1) $3,000 × ($10,000 /÷ $110,000) = $273 or 2) $3,000 – $0 = $3,000

23 Lesser of 1) $3,600 × ($100,000 /÷ $115,000) = $3,130 or 2) $3,600 – $273 = $3,327

24 This example does not take into consideration income and other capital gains and losses that could have been allocated by the funds in the year.

25 Capital losses are deductible only against capital gains.

D. Guarantee fees (additional guarantee fees)[26]

Important

Tax authorities haven't yet ruled on the tax treatment of additional guarantee fees payable under GIF contracts. We believe our proposed tax treatment is appropriate. However, unit holders are responsible for ensuring any such fees are properly reported on their income tax returns. Desjardins Insurance cannot be held liable for any consequences relating to the tax treatment of these fees should the authorities decide on a different treatment. Please consult your tax advisor.

Additional guarantee fees paid by the unit holder after December 31, 2014, should be deductible as capital losses when a guarantee payment is made or when the contract terminates.[27]

Furthermore, additional guarantee fees paid by withdrawing units may generate capital gains or losses and will have an impact on the ACB, just like any other withdrawal.

[26] This example does not take into consideration income and other capital gains and losses that could have been allocated by the funds in the year.

[27] Capital losses are deductible only against capital gains.

Date	Transaction	Transaction value	Market value before transaction	Market value after transaction	ACB before transaction	ACB after transaction	Capital gains (losses) arising from withdrawals, including those made to pay additional guarantee fees	Accumulated additional guarantee fees	Capital losses arising from additional guarantee fees
20XX-12-01	$100,000 initial deposit	$100,000	$0	$100,000	$0	$100,000	$0	$0	**$0**
20XX-12-31	$105 in additional guarantee fees	$105	$110,000	$109,895	$100,000	$99,900	$5	$105	**$0**
20XY-01-31	$95 in additional guarantee fees	$95	$95,000	$94,905	$99,900	$99,800	-$5	$200	**$0**
20XY-02-22	Contract end (withdrawal)	$105,000	$105,000	$0	$99,800	$0	$5,200	$200	**($200)**

Capital gain for 20XX arising from withdrawals made to pay additional guarantee fees (taxable capital gain of $3)	**$5**

Capital gain for 20XY arising from withdrawal of the contract (taxable capital gain of $2,600)	**$5,200**
Capital loss for 20XY arising from additional guarantee fees (net capital loss of $100)	**($200)**
Capital loss for 20XY arising from withdrawals made to pay additional guarantee fees (net capital loss of $3)	**($5)**

For 20XX, the unit holder will need to report a capital gain of $5 arising from the withdrawals made to pay additional guarantee fees.

For 20XY, they will be able to deduct a capital loss of $205 ($200 + $5) arising from the additional guarantee fees and the withdrawals made to pay these fees from the capital gain of $5,200 on the withdrawal of the contract and any other capital gains from the year. The balance of the capital losses can then be deducted from the net capital gains either in any of the preceding three years or in any future year.

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* Desjardins internal research, September 30, 2022.

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