INSIGHT
Into Financial Planning

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HELPING OUR READERS MINIMIZE TAXES AND INCREASE THEIR NET WORTH
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When to review your insurance coverage…

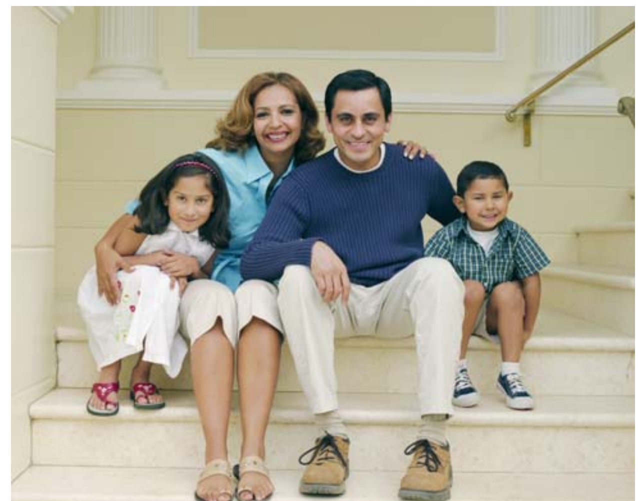
How do you know whether your existing life and health insurance policies are adequate for your financial needs? When, if at all, should changes be made to them?

Insurance can become outdated or inadequate as you move through life. Life events like marriage, having children and purchasing a home, as well as changing income, financial affairs and even the rising cost of living can make policies that years ago looked generous seem inadequate today. That's why you should review your coverage annually, and make changes when necessary.

Take life insurance, for example. If you have too little, your family could suffer financially when you die. Your insurance should provide enough coverage to replace the income you generate while you're alive, and to maintain your dependents' lifestyles. Also, consider the nature of your life insurance needs and how they relate to your long-term financial goals. Are your protection needs temporary or permanent? This will determine the type of coverage you require.

How will you know whether you have enough life insurance? You may want to predict the financial impact of your death on your family. Calculate how much money will be needed to replace your annual income. Tax liabilities may arise upon death. Consider the impact these may have on the final value of your estate. Also take into account liabilities, such as your mortgage or debts that must be taken care of by your heirs when you die. Then determine the wealth that will be available to your family or beneficiaries in the form of savings and investments. Your financial advisor has the tools at their disposal that can help determine the amount and type of coverage that suits your unique situation.

Critical Illness insurance protection is another area that deserves scrutiny. Thanks to recent medical advances, the chances of surviving a critical illness like a heart attack, stroke, or cancer are greater than ever before. Sometimes referred to as 'life insurance for the living', critical illness insurance provides a lump-sum benefit (following the survival period) after diagnosis of one of the plan's covered conditions. The lump sum benefit can be used to ensure your finances are protected at a critical time.



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The group life and health benefits provided by your employer should also be reviewed. Details of the plan such as coverage amounts and limits should be reviewed and incorporated into your overall financial plan. While group coverage may be an economical way to provide for your protection needs there is no guarantee that your employer will continue to offer the benefits you are currently receiving. Your benefits will also very likely cease should you change employers or be laid off. Many group plans allow you to convert your existing group life insurance coverage to an individual plan without evidence of insurability within a fixed period of time, usually 30 days, when leaving your employer. Your financial advisor can assist you in deciphering the details of your employer's group benefit offerings.

Of course, don't wait for an annual review if there have been major changes in your life…such as the birth of a child, marriage, divorce or substantial change in income or lifestyle. If one parent decides to stay at home to look after children, don't overlook the need to insure that parent. Quality child-care and domestic help that will be required in the event of that parent's death can be expensive.

Ensuring you and your family have the appropriate life and health insurance coverage in place is one of the cornerstones of a sound long-term financial plan. For more information on how Equitable Life® can help provide a lifetime solution to your life and health protection needs, talk to your financial advisor.

Insuring Your Retirement

Wayne and Carol Smith are looking forward to a long, comfortable, and healthy retirement. While their dream is still many years away, they want to ensure they are doing everything possible to ensure their savings last. Wayne and Carol, both 40, are in the top marginal tax bracket and plan to continue maximizing their RRSPs until retirement at age 65. Like many Canadians, they want to make sure their financial future is structured as tax-efficiently as possible. They understand that their registered investments will be fully taxable upon withdrawal and while they have non-registered savings, they also realize that a portion of the earnings on these investments is taxable every year, not to mention the deferred gains taxes owing upon withdrawal from these investments.

They would like to supplement their income with a plan that provides tax-preferred savings opportunities like their RRSPs without the associated tax consequences when it comes time to take an income.

Enter the Insured Retirement Strategy. Also known as Leveraged Life Insurance or the Collateral Bank Loan concept, this strategy has the potential to provide the Smith's with exactly what they have been looking for.

The strategy involves the purchase of a permanent life insurance plan, such as Equation Generation® IV Universal Life. Deposits are made to the plan in excess of what is required to cover the cost of insurance and other policy charges. During the accumulation years the cash value continues to build and any growth is tax-sheltered. When the Smiths retire or have a supplementary income need, they can use the accumulated cash value of their life insurance plan as collateral for a loan or series of loans. Pending a suitable agreement, financial institutions will lend money up to a specified percentage of the Cash Value of the life insurance plan. The loan proceeds can be used for whatever the Smiths desire. The Canada Revenue Agency

(CRA) does not currently consider these loans to be taxable.*

Interest will accumulate on these loans and can be capitalized, meaning any accrued interest will be added to the principal balance of the loan. Interest paid on these loans is generally not tax deductible unless the borrowed funds are being used for investment purposes. When the Smiths die, the proceeds of their life insurance plan are used to pay off the loan balance, including all accumulated interest in full. Any funds remaining can be paid tax-free to their named beneficiaries.

If the Smith's were to purchase a $500,000 Joint Last to Die Equation Generation IV Universal Life plan and make contributions of $1,000 monthly for the next 20 years they would accumulate just over $590,000 inside their plan at age 65 assuming the investments achieved an average annual net rate of return of 5.25%.

Loans advances could begin at age 65 and continue for the each of the next 20 years. Loan amounts of approximately $25,000 per year could be received by the Smiths. At death, assuming the last survivor lived until age 90, the outstanding loan balance would be paid in full, with remaining proceeds in excess of $1.6 million available to be paid tax-free to the Smith's named beneficiaries. A loan interest rate of 8.25% has been assumed and a portion of the investments in the policy were transferred to guaranteed investments earning 4% upon advancement of the first loan.

So how does this strategy measure up? If the Smiths had invested in a non-registered balanced investment earning 5.25% they could still make $25,000 withdrawals for 20 years, however only about $105,000 after-tax would be available at death for their beneficiaries.

This strategy is particularly suited to individuals who have a permanent life insurance need, are accumulating funds for retirement and have their financial house fully in order. This includes maximized registered plans with no carryforward, minimal mortgage or debt (preferably none) along with non-registered savings. Individuals are ideally under the age of 55, healthy, in a high tax bracket with stable, excess cash flow.

Sound too good to be true? While this type of program offers an excellent way to 'have your cake and eat it too', there are a number of issues that one must be aware of prior to committing to a strategy such as this one.

The loan agreement is at the sole discretion of the institution advancing the funds. There is a risk that the loan could be called prior to your death. This would mean that unless you had excess funds available, you may have to surrender your life insurance policy to cover the outstanding loan balance. Surrendering the policy may result in significant tax consequences.

Interest rates also play an important factor in this strategy. The interest rate on the loan will likely be tied to the prime rate of the institution advancing the funds. Interest earned on the investments within your policy earn a rate that is linked to the performance of bond or equity indexes or guaranteed

rates such as guaranteed deposit accounts. There is a risk that the spread between the rate your investment is earning and the rate you are paying on your loan may be greater than what has been illustrated, resulting in lower than anticipated loan advances. To mitigate this risk, consider ensuring that all or a portion of your policy investments are invested in guaranteed interest accounts when loan advances begin. This will go a long way in reducing the risk that rate of return fluctuations can have on your long-term income strategy.

The Insured Retirement Concept provides you with an excellent opportunity to minimize the taxes on your investment portfolio today while maximizing your retirement income tomorrow. **Your financial advisor can provide you with complete details and advise you on the suitability of a program designed to meet your individual goals and unique financial circumstances.**

*Tax laws are subject to change.
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Tax Tip

TAX TIP: Maturing your RRSPs

Your registered savings have more time to reap the benefits of tax-sheltered growth. The Federal Budget 2007 has increased the RRSP/RPP maturation age limit to 71 years of age, effective for the 2007 and subsequent taxation years. RRIF owners must withdraw a specified minimum amount each year following the year in which the RRIF is established. This requirement will be waived for 2007, for those RRIF owners who turn 71 years of age in 2007, and for 2007 and 2008, for those RRIF owners who turn 70 years of age in 2007.

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