Planning Thoughts - Jim & Barbe

Tue, Nov 26, 2019 at 12:11 PM

My understanding is that Jim (M70, non-smoker) and Barbe (F69, non-smoker) have a non-registered investment portfolio worth about $3,000,000. You told me that this money is not required to provide a retirement income and will pass through the estate to their only child (who lives in the US). In fact

RRSP - $1,750,000
OPEN - $1,250,000 --- totally invested (assume balanced)
Pension $50,000 pre-tax per year

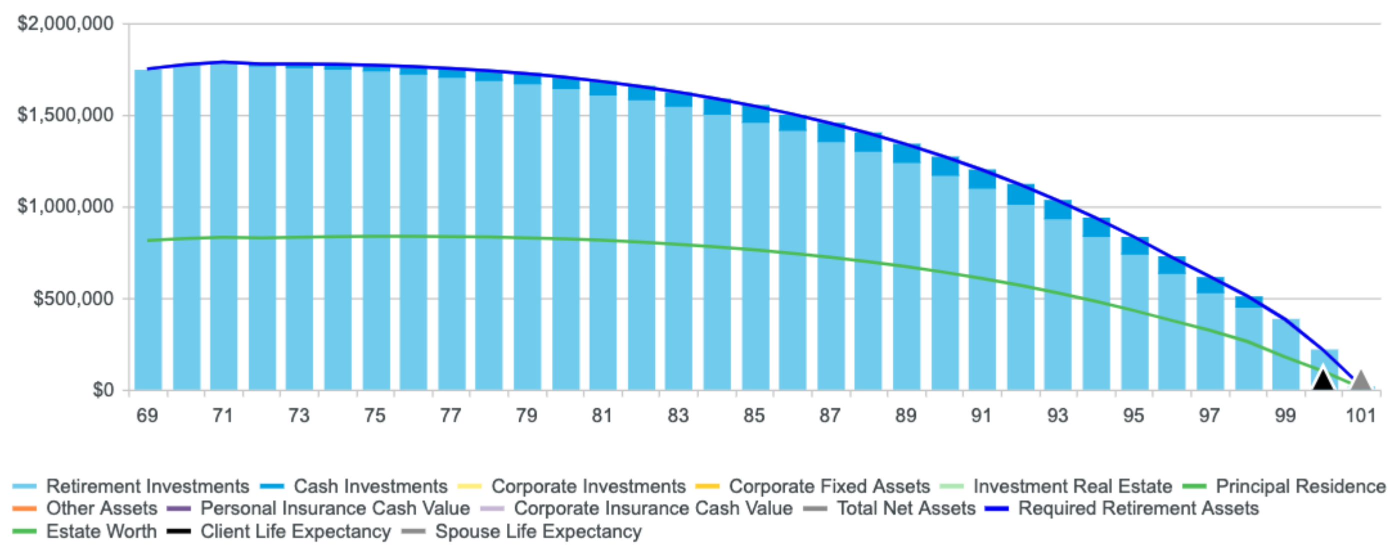
Spending probably $120,000 pre-tax (RRSP/Open/Pension)

Step #1 - How much income can only the RRSP's & Pension Provide for Life

I created a plan that completely removed the non-registered investments. Using a 5% rate of return and 2.5% inflation. To make things very conservative, I ran calculations to Barbe's age 1001.

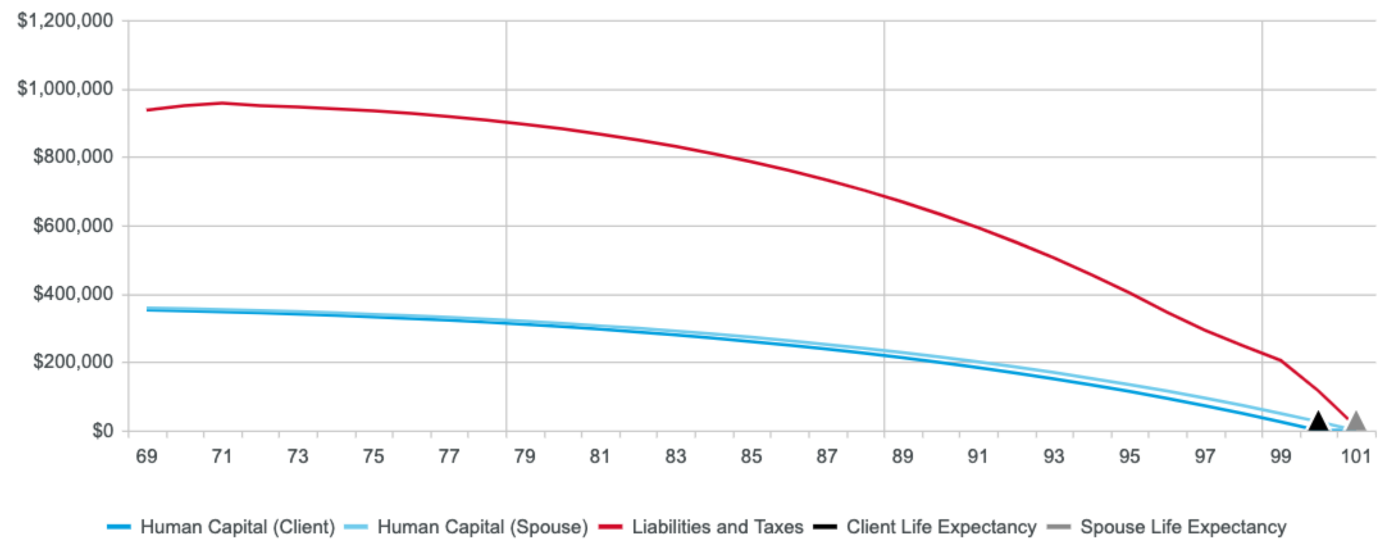
Jim & Barbe should be able to generate about $129,400/yr (after-tax -- or $10,783/mth). The RRSP's which will continue to reduce over-time as withdrawals are made (see light blue bars below). As you can see, the RRSP/RRIF will erode to $0 by her age 101 (using an after-tax goal of $129,400/yr):

Financial Assets ⓘ



However, from an estate planning perspective, at death, the entire balance of the RRSP's is added to the final tax return on the second death. Again, since the RRSPs are reducing, so does the tax bill. See the red line below:

Risk Management ⓘ

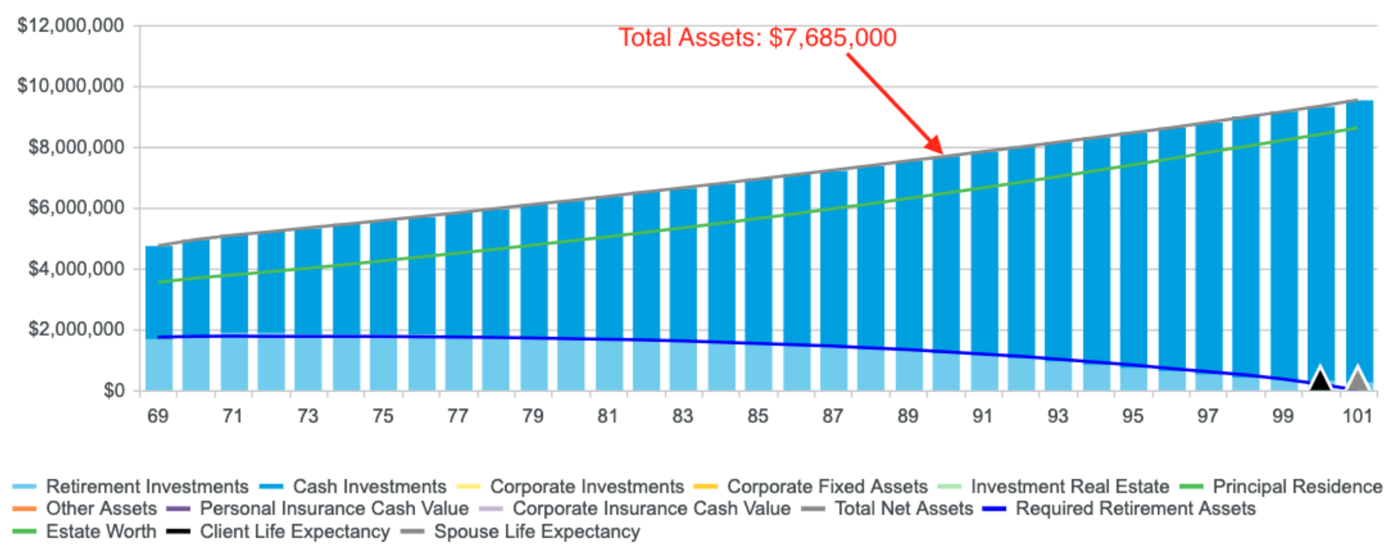


My point? The RRSPs and pension should provide more than enough income for their entire lives without ever including the open account.

Step #2 - Include All Assets (ie. Step #1 plus the $3,000,000 open account)

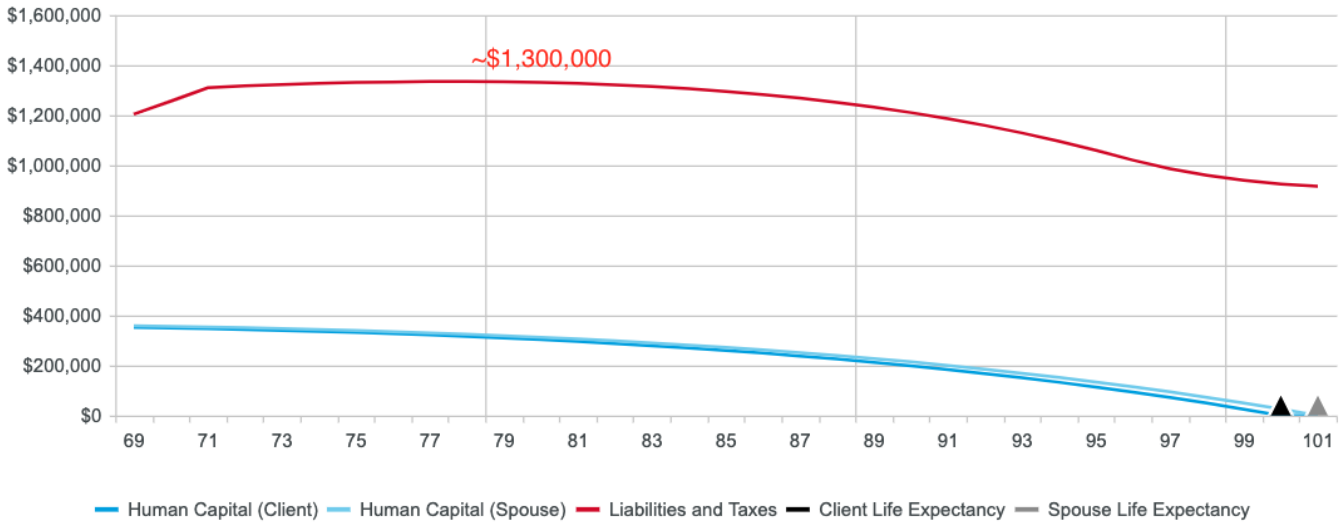
I'll assume the open account is a balanced portfolio with an ACB of $2,000,000 (5% rate of return). As you can see in the image below, the total estate continues to grow over time. At age 90, total assets are ~$7.7M. See below:

Financial Assets ⓘ



The estate tax liability doesn't dip below $1,000,000 until age 96. See below:

Risk Management ⑦



3. Why Life Insurance?

There are some key benefits that typical investments do not have:

- Investments inside a life insurance policy grow tax-free
- There are guarantees on the investment balance within an insurance policy
- The proceeds of life insurance are paid tax-free and bypass the estate and get paid directly from the insurance company to beneficiaries. This will likely be VERY helpful given their child lives in the US. Life insurance proceeds are paid within 10 business days (much better than having to settle an estate)
- If money is moved from the open account to life insurance, the estate tax liability will reduce

There are several different product options to choose from.

4. Product Option #1
Use a joint last-to-die policy with guaranteed costs and a guaranteed rate of return (1.5%). Maximize the death benefit. The illustration below is 100% guaranteed. Compare the Net Estate Values to an open portfolio:

Personal Asset Transfer Plan (Comparison with an Alternative Investment)

Life Insured: Client 1_1, 70, Male, Non-smoker
Life Insured: Client 1_2, 69, Female, Non-smoker

Policy Details		**Alternative Investment**	
Owner: Owner		Interest	50%
		Dividends	30%
Policy Type:	Joint last to die	Deferred capital gain	10%
Face Amount:	$3,566,000	Realized capital gain	10%
Death Benefit Type:	Sum Insured plus Fund Value		
Cost of Insurance:	Guaranteed Level Rates	Tax Rate:	42.00%
First Year Annual Deposit:	$250,000.00	A.I. Rate:	Illustration Rate plus 0.00%
Initial Illustration Rate:	1.50%		

Personal Asset Transfer Plan for Owner Tax Free **Alternative Investment Values**

Age	Total Annual Premium	Total Charges	Fund Value	Cash Value	Net Estate Value	Year	After-tax Estate Value	Net Estate Value at Death
71/70	250000.00	$80,985	$167,033	$43,067	$3,733,033	1	$252,378	$252,378
72/71	250000.00	$80,985	$336,572	$212,606	$3,902,572	2	$507,156	$507,156
73/72	250000.00	$80,985	$508,654	$384,688	$4,074,654	3	$764,359	$764,359
74/73	250000.00	$80,985	$683,317	$600,673	$4,249,317	4	$1,024,010	$1,024,010
75/74	250000.00	$80,985	$862,826	$821,504	$4,428,826	5	$1,286,133	$1,286,133
76/75	250000.00	$80,985	$1,045,480	$1,045,480	$4,611,480	6	$1,550,753	$1,550,753
77/76	250000.00	$80,985	$1,231,334	$1,231,334	$4,797,334	7	$1,817,894	$1,817,894
78/77	250000.00	$80,985	$1,420,443	$1,420,443	$4,986,443	8	$2,087,581	$2,087,581
79/78	250000.00	$80,985	$1,612,865	$1,612,865	$5,178,865	9	$2,359,839	$2,359,839
80/79	250000.00	$80,985	$1,808,658	$1,808,658	$5,374,658	10	$2,634,694	$2,634,694
81/80	$0.00	$80,985	$1,758,588	$1,758,588	$5,324,588	11	$2,659,792	$2,659,792
82/81	$0.00	$80,985	$1,707,642	$1,707,642	$5,273,642	12	$2,685,137	$2,685,137
83/82	$0.00	$80,985	$1,655,803	$1,655,803	$5,221,803	13	$2,710,731	$2,710,731
84/83	$0.00	$80,985	$1,603,056	$1,603,056	$5,169,056	14	$2,736,576	$2,736,576
85/84	$0.00	$80,985	$1,549,385	$1,549,385	$5,115,385	15	$2,762,676	$2,762,676
86/85	$0.00	$80,985	$1,494,774	$1,494,774	$5,060,774	16	$2,789,031	$2,789,031
87/86	$0.00	$80,985	$1,439,206	$1,439,206	$5,005,206	17	$2,815,646	$2,815,646
88/87	$0.00	$80,985	$1,382,665	$1,382,665	$4,948,665	18	$2,842,522	$2,842,522
89/88	$0.00	$80,985	$1,325,133	$1,325,133	$4,891,133	19	$2,869,663	$2,869,663
90/89	$0.00	$80,985	$1,266,594	$1,266,594	$4,832,594	20	$2,897,070	$2,897,070
95/94	$0.00	$80,985	$958,152	$958,152	$4,524,152	25	$3,038,197	$3,038,197

Remember, the option above is 100% guaranteed (vs. market risk).

5. Product Option #2 - Use Whole Life Insurance as an asset class
This is the more common solution because the contract has large cash values which are invested (the current rate is 6.25% -- I'm showing 5.25% below). The cash values and death benefit grow significantly over time. Notice the death benefit will grow to be similar to product option #1 (above), but there is significant cash/investment value.

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Participating Whole Life Insurance

ILLUSTRATION PREPARED FOR:
Client 1, M, 70, NS
Client 2, F, 69, NS
Joint Age: 61

Illustration Date: November 26, 2019

Policy Values*

		Guaranteed Values			Non-Guaranteed Values		
					Current Dividend Scale less 1.0%		
Year	Joint age	Guaranteed Annual Premium ($)	Guaranteed Cash Value ($)	Guaranteed Death Benefit ($)	Total Annual Premium ($)	Total Cash Value ($)	Total Death Benefit ($)
1	62	153,299	73,562	2,610,000	250,110	173,056	2,831,110
2	63	153,299	199,008	2,610,000	250,110	406,518	3,055,568
3	64	153,299	302,788	2,610,000	250,110	629,443	3,287,737
4	65	153,299	426,737	2,610,000	250,110	881,581	3,521,989
5	66	153,299	554,045	2,610,000	250,110	1,149,689	3,764,377
6	67	153,299	684,701	2,610,000	250,110	1,431,643	4,009,545
7	68	153,299	818,682	2,610,000	250,110	1,734,066	4,268,712
8	69	153,299	955,961	2,610,000	250,110	2,051,825	4,531,076
9	70	153,299	1,096,510	2,610,000	250,110	2,391,966	4,807,884
10	71	153,299	1,240,307	2,610,000	250,110	2,748,964	5,088,329
11	72	153,299	1,387,345	2,610,000	0	2,875,168	4,977,623
12	73	153,299	1,537,641	2,610,000	0	3,007,338	4,876,712
13	74	153,299	1,690,757	2,610,000	0	3,150,820	4,793,555
14	75	153,299	1,846,079	2,610,000	0	3,299,713	4,719,587
15	76	153,299	1,913,122	2,610,000	0	3,368,208	4,661,390
16	77	153,299	1,951,211	2,610,000	0	3,408,549	4,608,433
17	78	153,299	1,989,239	2,610,000	0	3,452,907	4,565,322
18	79	153,299	2,027,310	2,610,000	0	3,497,351	4,526,209
19	80	153,299	2,065,587	2,610,000	0	3,545,879	4,496,110
20	81	153,299	2,104,299	2,610,000	0	3,594,288	4,469,277
21	82	0	2,143,765	2,610,000	0	3,801,176	4,639,679
22	83	0	2,184,426	2,610,000	0	4,013,013	4,812,396
23	84	0	2,226,882	2,610,000	0	4,222,809	4,979,773
24	85	0	2,271,960	2,610,000	0	4,437,879	5,149,722
25	86	0	2,317,451	2,610,000	0	4,656,755	5,322,382
26	87	0	2,335,196	2,610,000	0	4,846,843	5,493,025
27	88	0	2,351,215	2,610,000	0	5,027,830	5,654,925
28	89	0	2,365,780	2,610,000	0	5,205,949	5,815,092
29	90	0	2,379,153	2,610,000	0	5,381,578	5,973,610
30	91	0	2,391,580	2,610,000	0	5,555,175	6,130,560

6. Final Thoughts

Ultimately, we should be meeting with this client to go through estate planning scenarios together. Most of the meeting is putting the software on a big screen and showing them how much money they will have and how much tax is projected. Once they completely understand, that's when I show where insurance 'fits'. The numbers above are only examples and by no means a recommendation.

My suggestion to you is to avoid using the word insurance. Immediately they will push-back ("I don't need insurance"). Explain that based on the projections (from above) we expect a $1.3M tax bill. Let's meet to talk about how we can plan/manage that bill.

Make sense?