Ontario's budget deficit *fell by* **11%** for the current fiscal year ending March 2011

ESTATEPLANNING

BY ANDRÉ L'ESPÉRANCE

Death, with fewer taxes

Increasing estate value for the affluent


L'ESPÉRANCE

Frequently incorporated in estate plans for affluent clients, an estate bond is a tax-efficient strategy that creates a large and immediate estate value. An estate-bond strategy is also an estate wealth accelerator that allows assets to pass on to heirs or shareholders, tax-free. Typical clients for this strategy are retirees who have more income or assets than they need to sustain their retirement lifestyle, and business owners with excess liquidities. The strategy provides both a tax-free death benefit and an investment component.

The benefits are many

An estate bond creates a large and immediate estate value that is far greater than what assets might earn in a taxable investment portfolio. Because the strategy uses permanent life insurance products, cash values are also tax-sheltered. If proper beneficiary designations are in place, the assets are nearly creditor-proof and the amounts invested are available if clients require liquidity during their lifetime.

Making it work

Setting up an estate bond is simple. Using a universal life or whole life insurance policy, clients begin to move their money from open savings accounts into an exempt life insurance contract. As shown in the chart "Estate bond power," a couple who transfers $50,000 per year for 10 years (a $500,000 investment) would create an immediate death benefit worth over $1,100,000.

Cash account growth in a universal life policy pushes the death benefit over $2,800,000 if the client lives until age 85. If the client lives until 95, the total death benefit nearly doubles.

For a corporate client, the death benefit could be paid into the company's capital dividend account, which tracks the tax-free amounts a company receives from various sources. These funds can in turn be paid out to shareholders tax-free.

The next step is to determine what investments to use inside of the permanent insurance policy. Universal life and whole life products go in and out of favour with clients, depending on market conditions and their willingness to accept and manage risk.

A lot of our clients like to have peace of mind with these products, especially when they are being used in a strategy like this one, so they will often choose conservative investments. Usually, they have a separate cash account with their investment advisor for buying stocks and implementing riskier investment strategies. In their insurance policy, they typically choose conservative investments, knowing that their death benefit will be paid out at some point.

The safest route is to invest in GICs inside of a universal life policy. Whole life policies tend to offer relatively fair yields through their dividend scale.

The estate bond strategy also offers creditor protection if certain conditions are met. Properly naming the beneficiaries is one of them. If the estate is the named beneficiary, the investment won't be creditor-proof.

To make an individual policy creditor-proof, the beneficiary must either be irrevocable or the client's legal spouse, children, grandchildren, parents or grandparents. Stepchildren are not considered in this vertical line.

Five-year test

The five-year test is another rough guideline that will be applied when considering the protected status of a policy in bankruptcy proceedings. If the policy is established within five years of the client declaring bankruptcy, the assets will likely not be protected. Similarly, the client's intentions will come under scrutiny. If it's shown the client intended to shelter money from creditors, courts will likely cancel that protection.

Finally, for clients concerned they may need asset liquidity, the cash values that build up in the policy create a cash surrender value. Depending on the product, they can either borrow money from the policy or they can pledge the policy and borrow money from the bank, using it as collateral.

In both cases, the client can pay the money back, simply pay the interest, or let both ride, arranging for the loan to come due when they die, at which time the loan will be paid and the balance of the policy's proceeds will be paid out to the named beneficiaries or the client's estate.

In conclusion, the estate bond can multiply your client's savings and help provide a larger tax-free legacy for those they care about most. AER

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ESTATE BOND POWER

YEAR	DEPOSIT	CASH ACCOUNT	CASH SURRENDER VALUE	TOTAL DEATH BENEFIT	ALTERNATIVE INVESTMENT
1	**$50,000**	**$43,944.00**	**$31,058.00**	**$1,143,944.00**	**$52,503.00**
2	$50,000	$90,086.00	$64,313.00	$1,190,086.00	$107,653.00
3	$50,000	$138,534.00	$112,761.00	$1,238,534.00	$165,604.00
4	$50,000	$189,406.00	$163,633.00	$1,289,406.00	$226,520.00
5	$50,000	$245,224.00	$228,042.00	$1,345,224.00	$290,574.00
6	$50,000	$304,405.00	$288,941.00	$1,411,805.00	$357,948.00
7	$50,000	$367,130.00	$353,385.00	$1,475,571.00	$428,838.00
8	$50,000	$433,629.00	$433,629.00	$1,575,366.00	$503,449.00
9	$50,000	$504,024.00	$504,024.00	$1,625,418.00	$582,001.00
10	$50,000	$578,024.00	$578,024.00	$1,678,718.00	$664,725.00
15		$732,764.00	$732,764.00	$1,832,764.00	$859,528.00
20		$945,956.00	$945,956.00	$2,045,956.00	$1,119,171.00
25		$1,270,444.00	$1,270,444.00	$2,370,444.00	$1,466,156.00
30		**$1,721,102.00**	**$1,721,102.00**	**$2,821,102.00**	**$1,931,065.00**
35		$2,346,987.00	$2,346,987.00	$3,446,987.00	$2,555,549.00
40		$3,216,233.00	$3,216,233.00	$4,316,233.00	$3,396,435.00

Source: Richardson GMP

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