

INDIVIDUAL INSURED ANNUITY



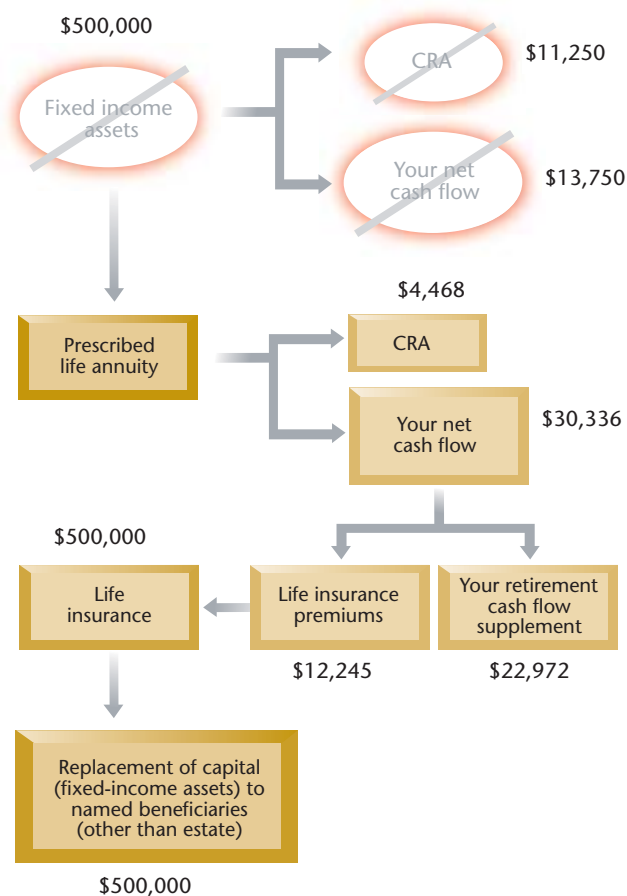
Jennifer Philanthropist case study



A division of London Life Insurance Company

A strategy for supplementing after-tax retirement cash flow and inter-generation wealth transfer.

The *Individual insured annuity* concept provides a greater after-tax cash flow than the GIC.



The *Individual insured annuity* concept offers:

- Guaranteed cash flow for life
- Preferential tax treatment of annuity income
- Inter-generation wealth transfer through life insurance proceeds paid tax-free to beneficiaries at death
- Permanent life insurance protection
- Flexibility to change policy beneficiary and coverage amount (subject to policy provisions and any underwriting requirements)
- Eliminates probate fees on death benefit with named beneficiary other than the estate (not applicable in Quebec)

Note: This example isn't complete without the illustration for the life insurance policy. Each page contains important information. Please read them carefully. *Individual insured annuity* values are based on annuity rates effective March 3, 2005. The values use *London Life universal life*, five per cent interest rate for a female age 65 non-smoker, standard rates. The retirement cash flow supplement incorporates the annual tax credit received (based on Ontario residency and 2004 personal tax rates as the life insurance policy is owned by the charitable organization of choice). A marginal tax rate of 45 per cent is assumed.



The client

Jennifer has just retired from teaching after 40 years. Teaching provided Jennifer with a very good pension plan. Additionally, she faithfully contributed to her registered retirement savings plan (RRSP) whenever she had RRSP room, maximizing her RRSP contributions throughout her working years. At age sixty-five, Jennifer has built a considerable portfolio of investments, including \$500,000 in guaranteed investment certificates (GICs) from her father's life insurance proceeds and other savings.

While Jennifer has many retirement income sources, she plans to use the interest on her GICs to support her goals of traveling extensively and continuing to support her favourite charities. Jennifer never married nor had children of her own. Instead, she dedicated herself to her students and would like to continue making a positive impact on the lives of children by leaving a lasting legacy of her passion and commitment to education and enrichment of youth. At her death, Jennifer would like to leave a large portion of her investments to a charitable organization that sponsors children for summer camps.

Are the GICs the most effective way to maximize her after-tax retirement cash flow? Will it ensure her goal to preserve \$500,000 for the children's camp is realized?

The facts

Using Jennifer's \$500,000 GIC portfolio and assuming an interest rate on the GIC of five per cent per annum, she would receive an annual before tax income of \$25,000. The entire income (100 per cent) will be taxable because the income from GICs is purely interest income. Based on her assumed marginal tax rate of 45 per cent, the tax payable on the income from the GIC is \$11,250, leaving \$13,750 after-tax.

The opportunity

Instead of renewing the GIC portfolio, Jennifer uses the \$500,000 to purchase a prescribed life annuity (prescribed under the federal Income Tax Act) which can guarantee a series of payments for her lifetime. The payments from the annuity will be a combination of principal plus interest. The taxable amount of the annuity payments is a level amount each year over the life of the annuity. Taxes are only payable on the prescribed interest amount and if everything is equal, Jennifer would receive a higher after-tax cash flow from the annuity than from the same amount invested in a GIC.

To replace the principal used to purchase the annuity, the extra cash flow from the annuity will be used to purchase a term 100 or minimum funded universal life permanent life insurance policy with a \$500,000 face amount. The death benefit will be paid to the named charity to ensure her legacy remains intact, as it was prior to purchasing the annuity. Jennifer is pleased the insurance will be there to assist her favourite charitable organization in such a significant way.

Discover the *Individual insured annuity* advantage

Based on rates effective March 3, 2005, \$500,000 deposited into an annuity would provide annual payment of \$34,803.66, guaranteed for life. The taxable portion is \$9,928.04. At the assumed marginal tax rate of 45 per cent, the tax payable on the annuity is \$4,467.62, leaving an after-tax cash flow of \$30,336.04.

An annual premium of \$12,245 would be required to cover the level cost of insurance charges for a \$500,000 *London Life universal life* insurance policy (female age 65, non-smoker, standard risk). In keeping with Jennifer's wishes to supplement her after-tax retirement cash flow while preserving the capital for her favourite charitable organization, the ownership of the life insurance policy is transferred to the charity. At the time of transfer, Jennifer will be entitled to a donation tax credit for the value of her donation. From that point on, Jennifer will be entitled to an annual tax credit for the amount of the donation, which in this case are the premiums paid. This will further enhance her after-tax retirement cash flow.

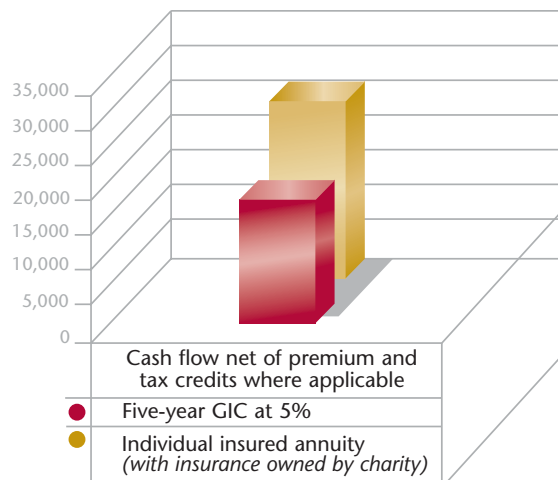
	<i>Individual insured annuity</i> (with the insurance owned by the charity)	<i>Individual insured annuity</i>	Five-year GIC at 5%
Gross payment	\$34,803.66	\$34,803.66	\$25,000.00
Taxable amount of payment	\$9,928.04	\$9,928.04	\$25,000.00
Tax payable at 45%	\$4,467.62	\$4,467.62	\$11,250.00
After-tax cash flow	\$30,336.04	\$30,336.04	\$13,750.00
Insurance premium	\$12,245.00	\$12,245.00	Not applicable
Annual tax credit	\$4,881.37	Not applicable	Not applicable
Cash flow net of premium	\$22,972.41	\$18,091.04	\$13,750.00

- The *Individual insured annuity* concept provides nearly 32 per cent more cash flow, on an after-tax basis, than the GIC
- Factoring in the tax credits for assigning the life insurance policy to the charity, the *Individual insured annuity* concept is even further enhanced – providing 67 per cent more after-tax cash flow than the GIC

Cash flow comparison:
\$500,000 principal remains intact

The cash flow produced by the *Individual insured annuity* is greater than that produced by the GIC based on all measures if Jennifer lived on the interest income from the GIC without ever touching the \$500,000 principal.

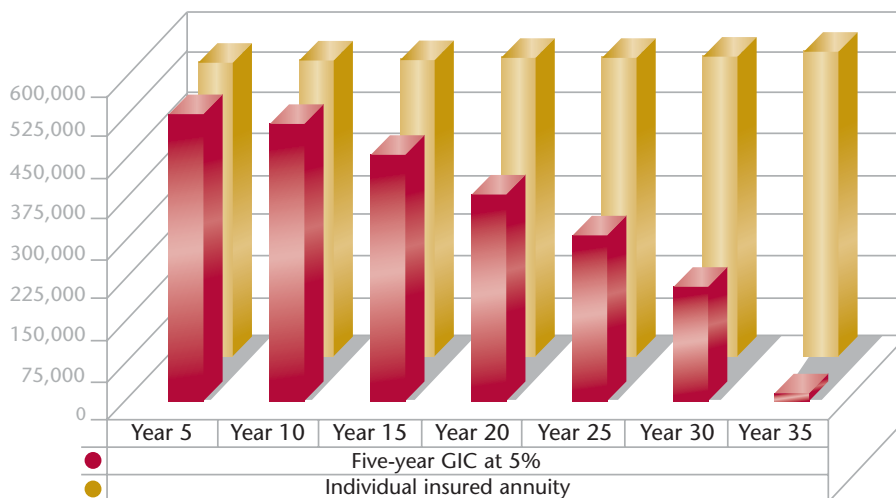
Individual insured annuity versus GIC at five per cent



Estate value comparison:
Jennifer's charitable gift

Over time, based on a five per cent rate of return, the GIC estate value (and potential charitable donation value) reduces considerably if Jennifer cashed in a portion of the principal annually to obtain the same cash flow as the *Individual insured annuity* (assuming annual after-tax cash flow is \$22,972).

Comparing the value of her charitable gift



Clearly, Jennifer and her favourite charity are both ahead by using the *Individual insured annuity* concept.

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Important considerations

The *Individual insured annuity concept* using a prescribed annuity structure can provide for higher after-tax cash flows than non-prescribed annuities. However, situations may exist where clients need more income in the future than the prescribed annuity contract provides. Because the prescribed annuity contract can't be surrendered and ownership can't be transferred, once purchased, clients will not be able to access the capital held within a prescribed annuity contract.

Clients will want to ensure they can obtain life insurance before purchasing the annuity.

For situations involving planned giving, the amount of the donation tax credit will be subject to the income tax legislation in place at the time of donation. Donation tax credits are calculated in accordance with federal and provincial legislation. For more information on planned giving using life insurance, please consult your financial security advisor.

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Information provided by London Life Insurance Company and is current as of March 2005

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