STEPUP

Sales Tax Estate Planning Underwriting & Product Newsletter

6th in a series

We've spent a little time learning about guaranteed withdrawal benefit products. How is the guaranteed lifetime amount calculated? Does it stay level or can it go up if the investment portfolio performs well? What about estate and survivor benefits and creditor protection, particularly if I'm running my own business?

Calculating guaranteed retirement income

One question that arises is; "how is the guaranteed retirement income for these plans calculated?" The maximum amount available for withdrawals in a calendar year is sometimes referred to as the lifetime withdrawal amount. The lifetime withdrawal amount is equal to a percentage of the Income Base as noted earlier, which includes all deposits and locked-in growth less withdrawals. It may increase if the Income Base increases, but it will not decrease (provided withdrawals don't exceed the allowable annual limit).

All withdrawals from guaranteed minimum withdrawal benefit plans, except for fees, will reduce the Income Base, but withdrawals in excess of the allowable annual limit can reduce the future amount of guaranteed income.. Excess Withdrawal Alert is an optional feature available on some plans that warns advisors and investors that a partial withdrawal request would result in a downward adjustment to the Income Base, temporarily stopping the excess withdrawal. The issuing company requests authorization to turn the excess withdrawal alert feature off and to proceed with the withdrawal. There may be no fees or charges associated with Excess Withdrawal Alert. This can be an important benefit that protects the guaranteed income during the payout period when the impact of investor behaviour can be long forgotten.

If a retiree, receiving the lifetime withdrawal amount wants less money, the excess isn't normally carried over to the following year. The market value and Income Base will only decrease by the amount received.

Guaranteed withdrawal benefit plans also provide additional flexibility when they are set up as a registered retirement income fund (RRIF), life income fund (LIF), Life Retirement Income Fund (LRIF) or Preferred Retirement Income Fund (PRIF). Each year the investor must withdraw the legislated minimum, and if it is greater than the lifetime withdrawal amount, there is no penalty to withdraw up to that amount.

Peter A. Wouters,
Director, Tax Retirement & Estate Planning Services

Peter works with independent advisors and other professionals raising awareness on issues and concerns faced by affluent individuals, professionals and business owners. He supports efforts in researching and developing optimal solutions for clients aimed at improving their financial well-being and supporting their personal wishes and lifestyles. He has provided 1000s of workshops, seminars and technical support throughout the country on tax, retirement income and estate planning issues, concepts and strategies to both advisors and consumers. As an accredited Registered Financial Gerontologist, a good deal of his time is spent on building awareness and educating people of all professions who work with or specialize in the needs, expectations and issues of elders. Comprehensive lifestyle planning is an important element of these processes.

The Sales, Tax, Estate Planning, Underwriting & Product (STEPUP) team provides internal and broker support, including seminars, education, advanced concept illustrations & Client case technical consultations.

Peter can be reached at peter.wouters@empire.ca

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Whether the plan is in the accumulation phase or income phase, it offers downside protection particularly important in the retirement risk zone or when dealing with sequence of returns risk

A Guaranteed Minimum Withdrawal Benefit Plan may be a viable product solution which can be used as a registered retirement savings plan (RRSP), a registered retirement income fund (RRIF) or as a non-registered investment vehicle for the years leading to retirement. An investor can benefit from potential market growth while being insulated every year from market declines. If there is a market downturn, the investor may still receive the annual Income Base Bonus provided no withdrawals are made during that calendar year.. Normally, a sharp decline in the retirement risk zone would cause anxiety and potentially upset retirement plans. But with a Guaranteed Minimum Withdrawal Benefit plan, even though the market value drops considerably, the Income Base can continue to rise due to the Income Base Bonuses. And it's the Income Base that determines retirement income.

Estate and Survivor Benefits

The estate or survivors benefit guarantee amount is paid directly to the beneficiary when a beneficiary is named. The guarantee is generally 75% or 100% of gross deposits, increased by any market resets, and reduced proportionately by any withdrawals. The reset process locks in increases in the market value of the investment on policy anniversary dates. It keeps the guarantee relevant. The contract normally bypasses the probate and estate settlement process if there is a named beneficiary. Long delays are avoided as well as costly probate and estate fees. Also, beneficiaries receive proceeds in private.

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Furthermore, the contract can be set up so that the surviving spouse may continue to receive a guaranteed retirement income. In fact, anyone can be named as the successor annuitant in a non-registered contract. For an RRSP or RRIF, the successor annuitant can only be the spouse. When the successor annuitant takes over the contract a reset of the death benefit (if the successor annuitant is less than 80 years old), the income base, and the guaranteed income takes place. The guaranteed income available from the contract could increase or decrease as a result of these resets. And if the successor annuitant is below the minimum age to receive guaranteed income the lifetime withdrawal amount will be set to $0.

Whether the plan is in the accumulation phase or income phase, it offers downside protection particularly important in the retirement risk zone or when dealing with sequence of returns risk, when income is needed and markets are underperforming or when death occurs perhaps exacerbated when that happens at the same time.

Potential Creditor Protection

Creditor protection may be of interest to people carrying a lot of debt, co-signing loans or who own businesses and want to protect personal investable assets from creditors.

Guaranteed minimum withdrawal benefit policies are individual variable insurance contract and, under provincial insurance legislation, may be protected from creditors if:

- the beneficiary is the spouse or common-law partner, parent, child or grandchild of the annuitant in most of Canada except
- in Québec where the beneficiary is the spouse, parent, child or grandchild of the contract owner or
- the beneficiary is irrevocable.

Note that there are certain circumstances where protection from creditors will not exist. If the possible protection from creditors is an important consideration, advisors and investors should consult with a legal advisor before deciding to purchase the contract.

Peter Wouters

Related articles and resources

GWB Order to Disorder series 1 of 7: The Risk of Longevity

GWB Order to Disorder series 2 of 7: Rate of Return and Impact on Accumulation vs. Withdrawal periods

GWB Order to Disorder series 3 of 7: When did you get on the rate of return cycle

GWB Order to Disorder series 4 of 7: What is a Guaranteed Withdrawal Minimum Benefit (GMWB)?

GWB Order to Disorder series 5 of 7: Investor behaviour

GWB Order to Disorder series 7of 7: Many Protective Features, Benefits & Advantages

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