The Stan Clark Financial Team's

PERSPECTIVES

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Financial and estate planning

How you can use life insurance as an investment

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When you think of investing, the first thing that comes to mind isn't usually life insurance. Normally you think of life insurance for something like protection for a young family. While it plays a very important role in this area, it's beneficial in others, as well.

Many people are not aware that permanent life insurance policies – Universal Life and Whole Life – provide insurance protection that includes a savings component. This savings component allows assets to accumulate in a tax-sheltered environment. The tax-free growth is similar to that of RRSPs. In addition to tax sheltering, the insurance pays out the death benefit on a tax-free basis.

Let's consider the following example. John and Susan are both 60 years old. They have children and grandchildren. They've worked hard and done well. They've accumulated a sizable portfolio, paid off their debts and maximized their RRSPs. John and Susan have more than enough money to cover their living needs.

From an estate planning perspective, one of their main goals is to maximize the legacy they will leave and be remembered by. One of the best ways to do this, if they qualify medically, is to invest in life insurance.

Let's assume John and Susan purchased a $1 million, minimum-funded Universal Life insurance policy on a Joint Life, last-to-die basis. Based on today's rates, this would cost them $13,795 per year, and that cost would be set for life.

Let's look at this from an investment perspective. The investment is the annual premium of $13,795. The return is the $1 million, tax-free benefit that their estate will receive. The profit and rate of return this gives depends on how long they live.

Let's say they both pass in year one. Now, that's a remote chance, but you never know. If they do, the profit would be $986,205, more than 70 times their investment.

Now let's say they live for 10 years. In this case, they would have paid a total of $137,950 into the policy, and would receive the $1 million benefit. That's a profit of $862,050, which equals an equivalent pre-tax rate of return of 61.65 percent, per year, compounded. That's pretty good compared to 10-year bond rates of less than three percent.

How about if they live 30 years to age 90? Here, they would have made 30 payments totalling $423,850. In return, they get the $1 million benefit for a profit of $586,150. That equals an equivalent pre-tax rate of return of 9.26 percent per year compounded, nearly three times as much as government 30-year bonds.

This strategy is also commonly used for businesses. Canadian-controlled private corporations pay very low tax rates. They often accumulate surpluses that are trapped, and attract taxes when paid out – or when the shareholders die. A company can pay the life insurance premiums using these trapped surpluses; most or all of the proceeds from the insurance benefit flow out of the company tax-free. This results in rates of return even better than those used on a personal basis.

Permanent life insurance is not for everybody. But in the right circumstances, it can be a very effective wealth management and transfer tool. The Stan Clark Financial Team has designed a spreadsheet that shows exactly what this strategy can mean to you and your estate. If you would like to talk to us about it, please don't hesitate to get in touch.

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To learn more about CIBC Wood Gundy, The Stan Clark Financial Team and the many ways we can help manage your wealth, please contact us by phone or by email as listed below.

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