BMO NESBITT BURNS

Protecting Your Lifestyle

Survivor Income Needs

THIS PUBLICATION IS PART OF A SERIES THAT FOCUSES ON THE UNIQUE NEEDS OF INDIVIDUALS NEARING OR IN RETIREMENT

You and your spouse have likely considered the income needs of the surviving partner. There are a number of factors that could impact the surviving spouse's financial well being.

For example, payments from Canada/Quebec Pension Plans or an employer pension plan may be subject to reduction upon the death of a spouse; however, many expenses for the surviving partner remain fixed.

In addition, if the investment decision-maker for your family should pass on first, the surviving spouse may run into difficulties managing the finances. Furthermore, he or she may be elevated to a higher tax bracket (which could result in higher taxes) once the family assets become individual assets.

Finally, if multiple family members are involved, such as in a second relationship, proper planning is required to ensure ongoing income for the surviving spouse, while maintaining an inheritance for the other beneficiaries. Spousal income could be jeopardized by pressure from, or lump-sum gifts to, other family members. Establish a plan of action early to alleviate anxiety for you, your surviving partner and other affected family members.

Take steps to minimize tax and estate settlement fees

A number of strategies – some of them very simple and cost-effective – such as naming a beneficiary for your RRSP/RRIF and insurance plans, may be appropriate to reduce the value of your estate subject to probate taxes. You can defer payment of capital gains tax by taking advantage of the spousal rollover available for distribution to your spouse or to a Spousal Trust. You may also want to consider strategies to reduce taxation for your beneficiaries after your death, including the use of a Trust in your Will to split investment income on the inheritance.

Establish a trust to protect your survivors and increase after tax income

Do you want to ensure that your wealth remains within your family if your spouse remarries? If no Trust is imposed, surviving spouses are entitled to dispose of their inheritance as they wish. This may cause concern in the event the surviving spouse remarries or where there are children from an earlier marriage. A Trust allows you to control who will receive the residual inheritance upon the death of the surviving spouse and may protect your spouse from a family law claim in the event of remarriage. A Trust for a surviving spouse also provides an opportunity to reduce income tax on the inheritance. By creating a spousal Trust in your Will, you may be able to increase your spouse's after-tax income after you pass away. The income from the assets of the Trust can be taxed at lower rates in the Trust than in the beneficiary's hand – even where the income is paid to the beneficiary – because a Trust created in a Will has its own graduated marginal tax rates. The income tax benefits of a Trust in a Will are often, in themselves, sufficient reason to create spousal Trusts as part of an estate plan. A number of tax and legal

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details must be addressed in the course of setting up Trusts for a surviving spouse.

Ensure fixed expenses are covered

Many expenses, such as property tax, will remain fixed for a surviving spouse. In order to ensure there will always be money available to pay these expenses, you may wish to consider including a direction in your Will to allocate a portion of your estate to the purchase of a life annuity to generate a guaranteed lifetime income for your surviving spouse.

Use life insurance to generate survivor income

Sometimes an estate is simply not sufficient to maintain a survivor's standard of living. Life insurance is used to create or increase an estate because it can be a very affordable method of generating a tax-free lump sum of money for survivors. The death benefit is commonly used for income replacement, debt elimination, tax payment and estate equalization.

Guarantee lifetime income and preserve the capital for your heirs

Security of capital can be of prime concern in retirement and a very strong motivator for conservative investing. Using the insured annuity strategy, you can increase the amount of your after-tax income by lowering the taxable portion, yet potentially still receive a higher net return and preserve the capital for your heirs.The income you would receive from the annuity is a combination of interest income and return of capital, generally resulting in a higher after-tax income. Because only the interest portion of the income is taxed, you can keep more of what you earn. And there is no need to worry about outliving your money; you are guaranteed to receive the income, unchanged, for the rest of your life. In addition, with the insured annuity strategy you don't need to be concerned about depleting your estate. As part of the strategy you would purchase a life insurance policy that provides a death benefit at least equal to the amount of your capital, allowing you to use your capital for income without affecting the value of your estate. And even after adjusting for the cost of the life insurance, you may still have a higher after-tax income with this strategy than you would with a GIC. Insured annuities can be used for individuals or for couples. In the case of a joint-life policy, the annuity payments continue after the death of the first spouse and death benefits are paid out when the second spouse passes. In addition, the insurance proceeds would be tax free and could potentially bypass probate.

Charitable gift planning opportunities

When people seek to re-align their asset allocation to produce more income and diversify their portfolios, they may face substantial tax on their gains. This allows an opportunity to be creative in converting paper gains to cash flow, saving taxes and turning non-deductible items into those that attract tax credits, while addressing charitable objectives. A cost-effective way to achieve this goal is through a Charitable Gift Annuity, which allows an individual or a couple to make a significant donation and then receive a predictable stream of income and payments are guaranteed for life. Married couples can purchase a joint-and-survivorship annuity, which will continue to provide guaranteed income as long as either spouse lives. Given changes in the tax regulations for prescribed gift annuities, a larger donation receipt may be granted than in the recent past. For older annuitants, a sizable portion of the regular payments may be received tax free.

What's next?

Your BMO Nesbitt Burns Investment Advisor is familiar with your financial circumstances and will help you identify the need for estate planning services. When working with one of our Estate and Insurance Advisors, he or she can help you maximize future income for your surviving spouse and children and that your assets are organized in the most effective manner to minimize tax, preserve your wealth and ensure that your assets are distributed as you have planned. In addition, your Investment Advisor can introduce you to an estate planning or tax professional to provide advice and help implement your plan.

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