Manulife Financial

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CONCEPTually speaking

from the Advanced Sales Unit of
Manulife's Tax & Estate Planning Group

Insured Annuities and Government Benefits

The Insured Annuity is a popular financial planning concept designed to increase cash flow to your clients when they are alive while making sure they maintain funds to leave a legacy when they die.

One of the lesser talked about benefits of implementing an Insured Annuity is that it may have a positive impact on your clients eligibility to receive and retain certain government benefits.

Here's the issue.

When your clients reach age 65 many will begin receiving Old Age Security (OAS) benefits. Some of your more wealthy clients will continue to have higher levels of taxable income that could impact their ability to receive and retain OAS benefits. Typically referred to as the OAS clawback, clients will start losing a portion of the OAS benefit when there taxable income exceeds $69,562. A total clawback of the benefit applies when your client has net income of $112,772.

In certain situations the Insured Annuity concept may not only increase your client's net cash flow while living but also have a positive impact on their ability to retain their OAS benefits.

Consider the following situation. Mary is age 70 and a non-smoker. Her net income is approximately $90,000. As a result of having this level of net income she is experiencing a clawback of the majority of her OAS benefit. Mary has a sizeable investment portfolio that is generating interest income that she is spending each year to meet her lifestyle needs. Mary has earmarked certain investments to go to her heirs when she dies.

Let's see how the Insured Annuity concept might improve upon Mary's financial situation.

Mary has a $1,000,000 GIC earning 3%. It is generating interest income of $30,000 ($18,000 after tax - assuming a 40% personal tax rate). If she implemented the Insured Annuity concept her net cash flow would increase to approximately $34,000 after tax, an increase of $16,000.

Interest earned from the GIC is reported as income by Mary, but if she replaced the GIC with an Insured Annuity, Mary would only have to report the $8,585 taxable portion of the annuity as income.

Under this scenario Mary’s net income as reported for tax purposes is reduced by over $21,000 even though the Insured Annuity strategy has significantly increased her annual net cash flow. As a result of this reduction in net income Mary is now eligible to receive the full OAS pension without incurring any clawback that would have applied under the GIC scenario. This additional benefit is another reason why the Insured Annuity concept can be such a powerful planning strategy for seniors.

Note: The clawback information provided is based on taxable income amounts effective January 2012 and subject to change.

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