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Ellen Roseman

In my Sunday series on retirement income that started April 4, I've been looking at ways to make your money last as long as you do.

A column about life annuities (May 16) set off a flurry of questions from readers. I'll try to answer some today.

Q: For an elderly couple, both 77, how much capital would it take to buy a life annuity that would pay $1,000 a month until both died? And what if they wanted to have the monthly income indexed to inflation?

A: I asked Martin Kosterman, annuity specialist and senior financial adviser at IPC Fiscal Agents, to provide a quotation.

He said this couple would need capital of $140,903.50 to get a $1,000 monthly income for life. This would be for a joint and last survivor annuity guaranteed for four years, so the income would go to the estate if both partners died during the guarantee period.

They would need capital of $170,570.85 to get the same monthly income at the start, plus 3 per cent annual growth to keep up with inflation.

Q: What happens to the monthly annuity payments if the life insurance company goes out of business?

A: A non-profit company, Assuris, protects policyholders if member firms go under. All Canadian companies licensed to sell life insurance must belong to it.

If your life insurance company fails, your annuity policy will be transferred to a solvent company. Assuris guarantees you will get up to $2,000 a month or 85 per cent of the promised monthly income benefit, whichever is higher.

For example, if your monthly annuity income was $1,500, you'd get the same payments. But if your income was $3,000 a month, you'd get 85 per cent of that amount (or $2,550 a month).

Since 1990, when it was set up, Assuris has handled three liquidations – Les Cooperants in 1992, Sovereign Life in 1993 and Confederation Life in 1994. (Confederation's 266,000 individual policyholders had a full recovery, it says.)

Q: After my spouse and I die, can we pass along annuity funds to our children?

A: A joint and last survivor annuity for a couple is payable as long as you or your spouse is alive. You can buy single-life annuities with income guarantees, so the payments continue to your estate even if you die. But still, the capital is gone forever.

You can protect the capital if you buy a life annuity from an insurance company and a term to 100 life insurance policy from a different insurance company (with yourself as the insured person). This is often called an insured annuity.

Once you buy the annuity, you no longer have direct access to the cash within it, says financial planner Rona Birenbaum. Instead, the annuity's payments are used to pay the life insurance premium and the tax on the annuity income.

The remaining amount, which is often significantly more than that generated by GICs, is used to supplement your income.

Meanwhile, the designated beneficiary of your life insurance policy will receive the proceeds tax-free when you die.

Q: How are annuities taxed? Does it make a difference if I use money from my RRSP or non-registered money?

A: If you buy an annuity with RRSP funds, the income is fully taxable. So, you should use only money that comes from your non-registered investments.

Annuity payments yield about two percentage points more after tax than interest income from a GIC (for non-registered money). That's because some of the annuity income is the return of your own capital and not taxed.

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