

Insurance

Insurance: a secure, regulated and protected investment option

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The extreme market volatility and the meltdown of the American financial industry in recent weeks have been weighing heavily on the minds of investors with exposure to the stock market. Of late, though, some of that concern has spread to insurance industry, and how the struggles of such giants as American International Group (AIG) could affect policyholders in Canada.

The Canadian insurance industry is highly regulated, with industry funded / government endorsed policyholder protection in place. Like never before, insurance solutions are proving to be sound, long term investments, many of which offer guarantees and higher yields.

Regulation of Insurance Companies in Canada

The life insurance industry in Canada is a highly regulated environment. The Insurance Companies Act of Canada (the Act) is the primary legislation governing all federally incorporated or registered insurance companies in Canada, and each province and territory then has its own provincial insurance regulations. The Act specifies that “a company... shall, in relation to its operations, maintain adequate capital and adequate and appropriate forms of liquidity”. As a result, all life insurance companies operating in Canada must adhere to the guidelines imposed by the Office of the Superintendent of Financial Institutions (OSFI) regarding capital reserve requirements to ensure their solvency. OSFI regulates and supervises close to 350 insurers in Canada, including life insurance companies, property and casualty insurance companies, and fraternal benefit societies.

If, despite OSFI’s best efforts, a Canadian insurer does file for bankruptcy, other insurers would likely purchase the bankrupt company’s assets and take over administration of their contracts. This would mean that the only difference to policyholders should be the company they are dealing with – their benefits would likely stay intact.

Protection for Canadian Life Insurance Policyholders

In addition to the security provided investors by OSFI’s requirements, another organization exists to provide additional protection. Assuris is a not-for-profit corporation funded by the life insurance industry itself that protects Canadian policyholders against the loss of benefits due to the financial failure of a member company. Federal, provincial, and territorial regulators require that all life insurance companies authorized to sell insurance policies in Canada be members of Assuris. It is an industry organization similar to the Canadian Deposit Insurance Corporation (CDIC), which protects GIC clients in the event of issuer default, whose mission is to mitigate the impact on Canadian policyholders of the financial failure of a life insurance company. Working in partnership with regulators on any necessary interventions, Assuris seeks to both minimize long-term costs and preserve consumer perceptions of industry strength. If necessary, Assuris ultimately seeks to coordinate the orderly transfer of policies from a bankrupt insurer to a solvent one in order to maintain policyholder benefits.

It is not necessary for policyholders to apply for protection with Assuris. Policyholders would be informed by the liquidator on how the respective benefits are protected should a Canadian life insurance company fail. If an insurance company merges with or is purchased by another insurance company the policy benefits that are protected by Assuris at the time of the merger or transfer continue to be protected after the merger or transfer.

Assuris guarantees that Canadian citizens and residents with policies from Assuris member companies will retain at least 85% of the promised benefits under a variety of products and also provides 100% protection when benefits are below certain dollar values. Complete information on the products covered, member companies, and how Assuris protects policyholders can be found on Assuris’ web site at www.assuris.ca.

Diversify with Insurance Solutions

With the knowledge that the insurance industry in Canada is well regulated and that protection is in place for policyholders, insurance solutions make more sense than ever in a time when investors are more risk adverse and are looking to diversify their portfolios and minimize their exposure to the market.

Higher yielding fixed income

Traditional investment vehicles, such as GICs, are often popular choices to satisfy fixed income investment needs. However, the interest earned with a GIC is fully taxable and the after-tax rate of return may not provide enough to meet your goals and needs. The tax treatment of the payments from an Insured Annuity is much more favorable than that of a GIC, thus creating an even higher equivalent annual yield for non-registered funds – currently anywhere from 4.73% to 9.56%* (40% tax rate), for clients age 60 to 80, depending on the individual investor's scenario. An added benefit of this strategy is that it also pays your originally invested capital at death to your beneficiaries directly, without the usual estate-related hassles and costs.

Investing with guarantees

Segregated funds may be an interesting option for investors looking to continue to participate in equity markets and benefit from potentially higher gains, but are wary of the current market climate and are looking for an investment that carries less risk. Segregated funds are insurance contracts that operate very similarly to mutual funds, however they come with guarantees designed to protect your investments from market volatility. Typically, between 75% and 100% of the original capital is guaranteed after a predetermined time period and at time of death. Some products also come with “reset” features allowing you to capture market growth and increase your guarantee. In addition, assets can be distributed directly to named beneficiaries upon death, thereby avoiding probate fees and delays.

Generate guaranteed income

Guaranteed Minimum Withdrawal Benefit (GMWB) products are essentially segregated funds that provide a guaranteed income stream based on 5% of your original deposit. The income stream has the potential to increase, but it is guaranteed to be no less than 5% of your deposit. These products also allow the future guaranteed income to increase if you make no withdrawals in the specified bonusing period, making this an ideal solution for those with 10 to 15 years until retirement.**

Continue to build your estate

By shifting a portion of your assets from fully taxable investment vehicles (such as GICs, bonds, or cash) into a tax-exempt insurance policy, you can significantly enhance your estate plan. The investments you make in a life insurance policy grow on a tax-deferred basis during your life, and at death are paid to your beneficiaries tax-free. You can invest your capital very conservatively inside these policies or create exposure to equity growth with contractual guarantees and stability. Your family benefits from continual insurance protection, a reduction in your ongoing tax liabilities, and typically a much larger estate for your heirs.

**As at October 10, 2008.*

***Subject to any applicable death and maturity guarantee, any part of the premium or other amount that is allocated to a segregated fund is invested at the risk of the contract holder and may increase or decrease in value according to fluctuations in the market value of the assets of the segregated fund. A description of the key features of the individual variable insurance contract is contained in the information folder. This information folder can be obtained from your ScotiaMcLeod Financial Services Representative. Please read the folder carefully before investing.*

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