Estate & Financial *Planning*

The Pros And Cons Of Investing In "Seg" Funds

(ILC)-Many people will be attracted this RRSP season to fund investments that are marketed with the promise of a "guarantee." What you should know before you buy one of these, is that you are not completely covered against losing your money.

In most cases these funds-called segregated, guaranteed or protected funds-will only give you back your original investment after 10 years or on your death. If you withdraw your money in less than 10 years, you stand to lose money and get back less than you invested.

The chances of losing money in these funds is highest if you need to withdraw your money after just a short while. The risk diminishes the longer you hold the investment. That's because these funds are invested in stocks or bonds that fluctuate in value, which in turn affect the value of your investment in the fund.

What Are The Costs Of These Funds?

Most of these funds are really just mutual funds with insurance policies attached.

As with mutual funds, there are ongoing costs you pay to the fund manager, including a fee to manage your money. These costs are known as the Management Expense Ratio (MER). The MER on many seg funds is typically higher than for ordinary mutual funds. This reflects the extra cost for the insurance.

The insurance premium may add as much as 1 percent or more to the MER on an equity seg fund issued by a mutual fund company. Seg funds offered directly by insurance companies are typically less expensive and compare favourably with traditional mutual funds. However, a more variable cost are the sales commissions or "loads" insurance company seg funds charge. These have historically been higher than for regular mutual funds, and some seg funds still levy both a sales charge when you buy and a sales charge when you sell even though this practice has been abandoned by most of the fund industry.

Given the higher MERs and sales commissions for many seg funds, the question to ask yourself is do you need the insurance guarantee, and if you do, what price are you prepared to pay?

Since stock markets have historically risen over the long term, the likelihood of actually needing the guarantee to get your original capital back after 10 years would be small. Consultants William M. Mercer found there's a 2 percent likelihood of losing money in the stock market over 10 years. Of course, this is no guarantee that history will repeat itself.

Some companies selling segregated funds offer a "freeze" option. If your fund's value rises, you have the ability to lock in that new, higher value as the guaranteed amount. The guarantee date would then be reset to a new date 10 years down the road. So you would have to wait another 10 years to actually get that new guaranteed amount, although your beneficiary, of course, would collect sooner if you died.

Beware that the guarantee, depending on the policy, may be reduced to 80 percent or some other percentage once you reach age 90, for example. You can't buy some of these policies after you turn 80.

When the 10 years is up, you can leave your money in the seg fund, get your money out or convert it into an annuity.

The name "segregated fund" came about because the assets in the fund are held separately from the insurance company's other assets. Segregated funds are also referred to as "individual variable annuity contracts" or "variable insurance contracts."

What Are The Unique Features Of A Seg Fund?

If you die, the segregated fund, unlike other investments, goes directly to your beneficiary without your province charging probate fees.

Segregated funds can give you protection from creditors, if the policy names an immediate family member as beneficiary. This may be particularly useful if you are self-employed. This protection may be lost if a court found you had set up the seg fund to avoid your debts.

Remember that while they offer benefits, insured funds are not a solution to volatile markets.

Seg funds might meet your needs if:

- You are retired, or close to retirement, and worried about risk.
- You want some equities in your portfolio, but you know volatile stock markets will keep you up at night.
- You want to provide for someone after your death.
- Protection from creditors is important to you.

Seg funds might not suit you if:

- You are young and have many years for your savings to grow.
- You don't believe the equity markets will drop for a 10 year period.
- Estate planning is not a concern.

[More details on investment basics are available from the not-for-profit Investor Learning Centre of Canada (ILC) in their plain-language Bottom Line Guide To Investing. You can order it for $9.95 by credit card by phoning 1-888-452-5566, or by visiting the ILC Web site at www.investorlearning.ca.]

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Lou Mulligan CFP, RHU

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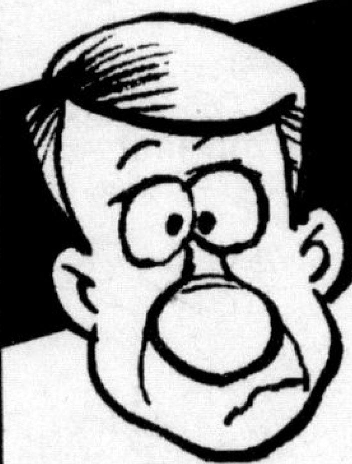

Linda Myronyk

Get the straight facts about RRSP's

- Make your RRSP grow faster
- Are "self-directed" RRSP's for you?
- How RRSP's work as a tax shelter
- RRSP contribution limits
- Increase foreign content with clone funds
- Spousal RRSP's and income splitting

TIME	PLACE	DATES
7:30 - 8:30 p.m.	MONEY CONCEPTS MILTON 420 Main St. East (Above Harvey's)	February 8, Tuesday February 15, Tuesday

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ADMISSION IS FREE

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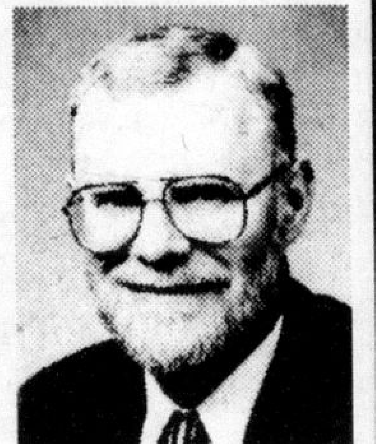
INVESTING FOR THE MILLENNIUM



Bob Reid, CFP

Recent market trends suggest that 2000 will continue to be volatile for equity and bond markets. Is your RRSP, or other investments for that matter, equipped to deal with these fluctuations (up and down) and assure you of the capital required to fund your retirement?

THIS IS NOT ABOUT RRSP'S

There are several strategies that can be employed to reduce volatility. One way is to establish a monthly contribution plan and invest a fixed number of dollars each month. Even if you have sufficient funds to make a lump-sum purchase now, this can be effective strategy. Essentially this approach takes the worry out of whether the markets will go up or down after your initial purchase and you wind up at the end of the year with a cast base that is the average price of all the monthly purchases. By choosing to create a retirement plan and to follow a disciplined approach to investing your savings, you enhance your chances to enjoy a successful and enjoyable retirement.

IT'S ABOUT YOUR RETIREMENT PLAN!

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