ADVISORS ASSET MANAGEMENT

Understanding the Estate Feature

Structuring Wealth for the Next Generation in a Rising Interest Rate Environment

Investors looking to maximize their investment returns, but have concerns about extending maturity beyond their lifespan, may find fixed income investments with an embedded estate feature beneficial.

An estate feature can help investors balance their long-term income needs with short-term pricing, redemption fees, and liquidity risks should they pass away.

Also referred to as a **survivor's option** or **death put,** an **estate feature** is an option that can be added to a fixed income instrument that gives the holder's estate the right, not the obligation, to sell the investment back to the issuer at face value (or par) in the event of death or, in some circumstances, the legal declaration of incompetence.

This feature serves as a **valuable tool in estate planning** because it allows for the full redemption of principal and accrued interest due, before the security's maturity date, even if the market value of the investment has fallen.

There are two general requirements which must be met before an estate feature option can be exercised. First, the investor must have passed away. Second, the investment must be put back to the issuer while the securities are still in the account of the deceased holder. Once the investments have been transferred to another account, the death put is usually no longer valid. Estate features often include a variety of other requirements and restrictions and investors should consult the offering documents for and investment for more details.

A survivor's option can help address interest rate risk at the time of death.

Fixed Income investments with an estate feature can be especially **attractive in a rising interest rate environment.** Interest rates and fixed income investments have an inverse relationship, so when interest rates rise, bond prices generally fall. This means that if interest rates rise, the beneficiary of an estate may be left with an investment that is selling at a discount to its face value. Having a survivor's option can help preserve wealth by giving the beneficiary the option to sell the fixed income instrument back to the issuer at par.

Conversely, should the current value of the fixed income investment be greater than its par value, as is commonly the case in a falling interest rate environment, the beneficiary can waive the survivor's option, choosing instead to sell the security in the open market at a premium.

Generally, all **brokered CDs** carry a death put feature. **Market-Linked CDs (MLCDs)** and **Corporate Notes** can also be structured with a survivor's option. It is important that investors verify the estate feature provisions of each investment and the individual terms outlined in the offering documents before making an investment decision.

Investors should be aware that in exchange for the estate feature option, they may receive a lower yield as compared to the same investment without a death put. Also, added features, such as a survivor's option, may limit buyers in the secondary market, should the original investor want to sell the investment.

There may be special terms and restrictions associated with an estate feature that an investor should be aware of.

Issuers may require a **minimum holding period,** which would require the estate's beneficiary to hold the security for a specified period of time before exercising the survivor's option, generally 6 months to 1 year. Some companies may also stipulate a minimum holding period after the bond is issued. For instance, if an investor passes away 3 months after purchasing a survivor's option security with a 6-month holding period, the estate would need to hold the investment for 3 more months before the death put becomes available. After those 3 months, the estate can put the bonds back to the issuer at par and transfer the proceeds to the next generation.

Issuers may also **limit the amount that can be redeemed** at any one time, either by the total amount they are willing to redeem in a year or by how much an estate can redeem. For example, if an individual estate feature limit exists of $200,000 per year per estate, and a beneficiary wants to redeem $250,000 of bonds, they would be able to tender $200,000 worth of bonds in year one and then wait to redeem the remaining $50,000 the following year.

Additionally, issuers may **only make payments on specific dates,** such as semiannually (on June 15 and December 15) or on the next coupon date.

Investors can help combat these restrictions by working with their financial professional to understand the terms of the estate feature and maintaining a diversified portfolio allocation strategy.

Lastly, the specific terms and conditions under which a survivor's option can be exercised may vary depending on the type of account. For **Individual Accounts,** the requirements are more straight-forward in that the beneficiary may tenor the bonds following the death of the bondholder, pending any restrictions previously discussed. For **Joint Tenancy, Tenants in Common,** and **Trust** accounts, the requirements can differ, and investors should consult their financial professional and/or tax professional prior to investing, as well as review the individual offering prospectus.

An estate feature allows investors to preserve their wealth for the next generation. It offers beneficiaries the option to follow a different investment strategy and take advantage of current market conditions without diminishing the initial value of the investment.

For more information on the estate feature, contact your financial professional.

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