Retirement planning — after you retire

The plan doesn't stop when you stop working. How to get it right

by Jonathan Chevreau, MoneySense, June 30th, 2017

While similar, retirement and what I like to call financial independence are not necessarily the same thing. The latter arrives when you have sufficient sources of passive income and assets accumulated that you can meet all your daily lifestyle expenses without having to continue to work. When that day arrives, you can create a life from which you have no desire to retire—at least not retire in a traditional sense.

Financial independence can come at any age. There are some frugal types who achieve this "findependence" in their 30s or 40s, although few of them stop working. Henceforth, they may wish to continue to work – but they will be doing so because they *want* to, not because they feel they *have* to, financially speaking. For most of us, that moment will come a few decades later.

These two concepts fit hand in glove, like the Chinese yin and yang. The yin is all the decades of work and wealth accumulation. The yang is the day you become "findependent" and create your new phase of life based on different priorities. This phase can extend as long as you're motivated and able to do so, both physically and mentally. Everyone is unique and you can't count on off-the-shelf financial advice to get the right plan in place.

Think of creative artists who are so engaged by their art that they view it as part of their daily life, not just a means of making a living. Do you think Mick Jagger of the Rolling Stones is still rocking in his 70s because he needs the money? Or consider Grandma Moses, who famously didn't even begin to start painting seriously until she was 78. Other late-bloomer artists include impressionist painter Paul Cézanne, whose career didn't take off until his 60s.

The big difference before and after your "Findependence Day" is that now that passive sources of income predominate over earned income, you have moved from the mode of wealth accumulation to that of wealth decumulation.

Depending on the financial plan you have worked out with an advisor, you will likely have to juggle multiple sources of income. In the good old days, someone who worked a lifetime in a single job offering a defined benefit pension may have "retired" full stop at or around age 65, and received one giant monthly stream of income from their former employer for life, plus the usual government benefits.

But the rest of us, including Millennials, there are a lot of things to consider in planning your finances in retirement. In a sense, it's easier to save for retirement when the major challenge is just sock away the money. Taking the money out later is actually more complicated and there is not one best way to tackle this challenge. Here are some things to think about.

Multiple income sources

Some retirees are more likely looking at multiple streams of income, large and small, possibly including earned income from a part-time job. Perhaps you have a couple of smaller DB pensions because you changed jobs a few times; you may have taken the "commuted value" of those pensions to turn them into locked-in retirement accounts (LIRAs) that could one day be annuitized.

Most will have Canada Pension Plan (CPP) as early as 60 and Old Age Security (OAS) as early as 65, though both can pay out more if you can wait till 70. For those with lower incomes, there is also the tax-free Guaranteed Income Supplement (GIS). Everyone's situation varies, which is another reason to get a custom retirement plan in place.

Some won't have any employer pension but with any luck will have a large RRSP instead. Those with generous employer pensions don't have much RRSP room because of the Pension Adjustment (PA) but to provide pension parity, Ottawa gives those without employer pensions much more RRSP contribution room.

Income taxes keep coming

One of the surprises retirees discover is if you have a tidy nest egg you will also take a hit on income tax and tax on investment income. All those years of maxing out RRSPs to generate a tax deduction on your earned income come back to bite you after 71, because you'll have to convert your RRSP into a Registered Retirement Income Fund (the other options are turning the holdings into an annuity or cashing out, but the tax consequences of the latter are horrendous).

Most will choose a RRIF, which means at the end of the year you turn age 71, Ottawa will require you to make annual withdrawals that are fully taxable, just like earned income. The percentage starts modestly enough –5.4% at age 72, but rises steadily to 20% after age 95.

One way to slow down the forced percentage is to base your withdrawal on your spouse's age, if he or she is younger than you, says Matthew Ardrey, wealth manager and vice president of Toronto-based TriDelta Financial.

Spousal strategies & your TFSA

If you are still earning income and have a spouse younger than 72, you can also make spousal RRSP contributions to his or her RRSP. While you can no longer contribute to RRSPs after 71, you *can* continue to contribute to a Tax-free Savings Account (TFSA) for as long as you live.

If forced to withdraw more from your RRIF than you need to live on, you can pay tax on withdrawals, then move some of the excess funds into your TFSA. There your investments can grow cheerfully tax free until you pass away and leave it to your spouse or heirs.

Similarly, if you have a large non-registered portfolio of tax-efficient Canadian dividend-paying stocks, you can convert some of these holdings to the TFSA (first paying tax on any triggered gains). The beauty of the TFSA in old age is it won't trigger clawbacks of OAS or GIS benefits. That's one reason Ottawa introduced it back in 2009.

Some retirees worry that if they don't abide by the 4% rule (which states that's the maximum you can withdraw from your nest egg without outliving your money in retirement) their RRIFs will dwindle to zero as they age.

The underlying fear is that minimum withdrawal rates will rise and investment returns are declining, but gradually converting RRIF funds to TFSAs and non-registered holdings should take the sting out of this scenario.

Are annuities right for you?

Annuities, which involve buying a guaranteed future payout, are another thing you can consider, especially if you think you're set for a long life and face a higher threat of outliving your money. Annuities haven't been ideal vehicles in the era of low interest rates but you can partly annuitize now and continue to do so periodically over the years, as rates start to rise to higher levels.

Ardrey says retirees might consider delaying annuitizing till later in life. "You can always convert the remainder of your RRIF to an annuity at any time." Delaying gives you more flexibility when young and, based on mortality tables, a higher annuity payout per dollar converted once you're older.

Allocating your assets

Finally, there's the issue of asset allocation. One traditional rule of thumb is that your fixed-income allocation should equal your age. If you're 70, you want 70% in fixed income and 30% in equities. But don't be ultra-conservative, warns Adrian Mastracci, portfolio manager at Vancouver-based Lycos Asset Management. If you live a long time, you'll still want some inflation-fighting dividend-paying stocks, particularly those with proven long-term records of raising their payouts.

Ideally, Canadian dividends are held non-registered to benefit from the Dividend Tax Credit. Fixed income and US dividends go in your RRIF, and your TFSA should hold more fixed income, non-dividend-paying foreign stocks, and domestic stocks (with or without dividends). Also consider alternative investments in your registered accounts, Ardrey suggests.

The fact they pay interest income means they're less tax-efficient, but they can supplement today's historically low interest rates while being sheltered in registered accounts.

Your financial advisor can help you on the asset mix and on how to withdraw funds to live as tax-efficiently as possible. When crafting your asset allocation, remember to consider pensions and annuities as another form of fixed income. So if you have a huge DB pension, consider that to be fixed income (as is CPP/OAS), and err on the side of putting more of your remaining investments in equities.

Pensions and annuities will pay out as long as you live but essentially they die with you. Check with an estate planner if you want to leave a legacy for the kids. Your starting point will be your remaining investments, life insurance, the family home and any business assets.

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