RETIREMENT
INCOME GUIDE

EQUITY
Associates Inc.

MING
& ASSOCIATES

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INTRODUCTION

We spend many of our working years allocating a portion of our earned income to one day fund our retirement. We go to work each day knowing that saving for retirement is an important progression of our lifetime, recognizing that we will not work forever. While most of us understand that saving for retirement is important, many of us have not figured out how we will turn our lifetime savings into an income stream when the day finally comes.

Whether you are currently living in retirement, entering your prime earning years, or just setting out in your profession; today remains the best time to put a plan in place for your future. As Financial Planners, we understand that this can be a stressful subject especially when you try to tackle it alone. A large number of Canadians are concerned about retirement expenses, leading to high levels of anxiety. It is our job to help guide people through this life process.

We have put this guide together to give insights on sources of retirement income, common risks to retirement, withdrawal strategies, accessing government pensions and more. We hope you find this information helpful, and we would be pleased to hear from you if you need assistance in creating an income solution that is right for you.

PLANNING YOUR RETIREMENT INCOME **WHY?**

We believe that those who plan also prosper. Smart people plan for retirement and put it in writing. Each of us can remember a time when we discussed great ideas but wished we had written them down.

At retirement, your whole financial life essentially collapses down to one question:

Will your money outlive you, or will you outlive your money?

Answering this question requires a long-term outlook since most people will likely enjoy a long retirement. For instance, take a non-smoking couple who retires at 62 years of age. Actuaries tell us they will have a joint life expectancy of nearly 30 years at retirement (which means the second person to die would pass on average at 92 years of age). If we assume an inflation rate of 2% (Bank of Canada's default target value and historically low, meaning it is quite possible the rate will be higher) the cost of living for the average couple will basically double in 30 years. That is to say what will cost about $2.00 in 30 years only costs $1.00 today.

If you haven't got a plan to increase your income as much as your living expenses go up in retirement, then you may be in effect **planning to run out of money.** (That is why the best pension plans are indexed to the cost of living)

A proper financial/life strategy achieves two purposes: it bridges the gap between where you are now and where you want to be; that is, it allows you to ACT rather than RE-ACT your way to success. Imagine how you will feel when you have an implementation plan that addresses all your key concerns and ensures that all of your resources are working in harmony towards your life goals.

Every person has a different vision of their retirement; some people want to be close to their family while others may wish to travel the world. Your retirement dream is unique to you, and so is the income you will need to generate that dream. In Canada there are four main sources of retirement income: Personal Savings (Investments and/or Business Assets), Government Pensions, Workplace Pensions and, for some, your Residence. This guide will touch on the fundamentals of each source and highlight the importance of having a comprehensive strategy in place to integrate all income sources, minimize taxes, and fund your (hopefully lengthy) retirement.

MOST COMMON SOURCES OF RETIREMENT INCOME

INVESTMENT PORTFOLIOS

REGISTERED ACCOUNTS

A registered account is an investment account that is given tax-deferred or tax-sheltered status by the Canadian Government. Everyone wants to (or should want to) pay less tax. For many, their largest asset in retirement is their Registered Retirement Savings Plan (RRSP) which when used alongside a Tax Free Savings Account (TFSA) can be managed throughout the years so that you pay the least amount of tax possible. You are permitted to hold a wide range of securities in your registered accounts, including Mutual Funds, Exchange Traded Funds (ETF), Guaranteed Investment Certificate (GIC), Stocks, Bonds and cash.*

i. Registered Retirement Savings (RRSP, RRIF, LIRA, LIF)

There is a good chance that you have been contributing to an RRSP for a significant portion of your working years with the understanding that RRSP contributions are tax deductible. Money invested in an RRSP is grown on a tax-sheltered basis and when you withdraw the funds, they are fully taxable as earned income in the year they are withdrawn. Your RRSP contribution room accumulates each year at a rate of 18% of your earned income that year (up to a limit of $30,780 per year in 2023), and you want to be careful not to over-contribute.

Upon reaching the age of 71(or before), an RRSP is transferred to a Registered Retirement Income Fund (RRIF) as it is government mandated to start taking minimum withdrawals each year (and pay the associated income tax) at that time. The idea behind this structure is that for many, pre-retirement income is expected to be higher than retirement income, so there should be an overall benefit from a lower tax rate when using an RRSP by deferring tax to later (lower income) years. Putting in place a plan to effectively draw down your RRSP/RRIF alongside your other savings and government benefits can provide significant after-tax savings if done properly.

ii. Tax Free Savings Account (TFSA)

Tax Free Savings Accounts were introduced in 2009 and are becoming a larger piece of the retirement puzzle as each year passes. Every Canadian Resident over 18 receives predetermined contribution room each year ($6,500 for 2023 with a cumulative total of $88,000). A TFSA is a tax-exempt account as it is funded with after tax dollars. This means there is no tax deduction at time of contribution, however, withdrawals, and most importantly the growth, are not taxable.

*See Equity Associates Inc. disclaimer.

A TFSA could be considered the worst named product in the financial world. The word 'savings' suggests cash in a bank account earning minimal interest, where the true value of a TFSA is cultivated when used as a "Tax Free Investment Account" over many years. Money put into a TFSA can be invested in almost any type of investment (similar to RRSP's). The decision on how to invest TFSA money is a very important investment decision as the ability to capitalize on tax sheltered growth and compound returns over long periods of time can really add up.

Other than keeping an emergency fund (3-6 months living expenses) in your bank account, any extra money should be moved into a TFSA. It will save you tax dollars, however, you want to be very careful not to over-contribute.

It is always important to align your TFSA strategy with your long-term goals as withdrawals later in life have no effect on your taxable income, meaning any clawback of government benefits and your overall tax rate may be minimized if planned appropriately.

NON-REGISTERED ACCOUNTS (OPEN)

If you have maximized your contribution limits in your registered accounts, additional investments are held in 'Open' accounts. Contributions and withdrawals of principal are not subject to income tax. You will be taxed on any growth and income generated in the account. The three main types of investment growth are interest, dividends, and capital gains; which are all taxed differently. Figure 1 below shows how each are taxed at the top marginal rate in Ontario.

This illustrates the importance of selecting the most suitable investments to hold in your non-registered accounts, for instance;

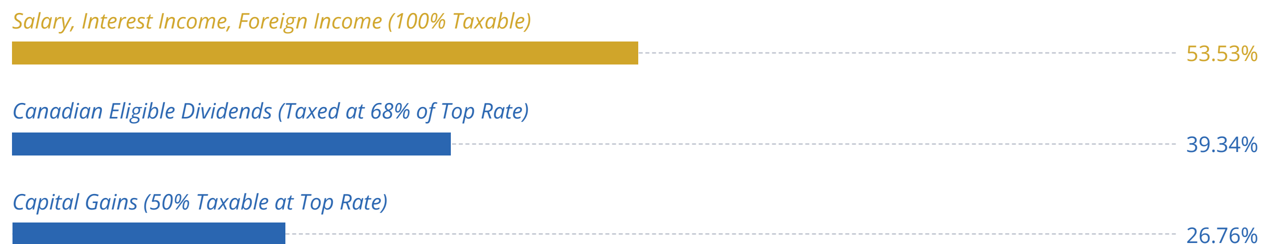

Figure 1: 2022 Top Marginal Tax Rates - Ontario

- **Interest income** is generated from Guaranteed Investment Certificates (GICs) Savings Accounts and Bonds. This income is fully taxable at your marginal tax rate similar to employment income.
- **Dividend income** is generated by stocks or corporations that pay a dividend. Dividends are taxed more favourable than interest and less favourable than capital gains;
- **Capital Gains** (or loss) results when you sell an investment such as stocks or real estate for a gain (or loss). Only 50% of the gains you realize are taxable as earned income and tax is not paid until the asset is sold (ie. the gain is realized).

BUSINESS ASSETS

Business Assets can consist of corporate savings and/or the value of the owners' business to be monetized as part of their retirement plan. There are numerous issues to ensure that any corporate investments and/or business transition or sale is integrated effectively with an overall plan. Issues range from optimizing the income on corporate investments- which are deemed to be passive income and therefore generally taxed at the highest marginal rate - to integrating any income or sale proceeds effectively. Issues such as maintaining the purity of a Canadian Controlled Private Corporation(CCPC) so that access to the lifetime capital gains exemption is maintained must be kept in mind when doing any corporate investment planning.*

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GOVERNMENT PENSIONS

CANADA PENSION PLAN (CPP)

CPP is a government administrated pension; however, it is funded by individuals and employers throughout your working years. Your CPP benefits will depend on how much you and your employer have contributed over the years. There are numerous options on how to access these benefits when the time comes.

Many people take a hurried approach when accessing their Canada Pension Plan. For some, CPP is something they want to access as soon as possible since they have been contributing their entire life and cannot wait to "get something back from the government" as soon as possible. Another common approach we see is the random, uninformed CPP decision. The government mails you an application prior to your 65th birthday, you complete the application and begin your pension. It is probable that you have been contributing to CPP on every paycheck as long as you can remember. Inevitably, this has become an asset of substantial lifetime value and deserves some thought as to how to maximize its value to you.

Many factors go in to the amount of CPP payment you could receive, including how much you've contributed through your working years. CPP payments are fully taxable income to you and although CPP's base value is calculated at age 65 the government provides alternative options beginning at age 60:

- **Early Withdrawal Option:** You can elect to take your CPP any time after turning 60. If you elect for the early withdrawal option, your CPP payment will be reduced by 0.6% per month (7.2% per year) before 65. This could result in your CPP payments being reduced by up to 36%.
- **Late Withdrawal Option:** You can elect to defer beginning your CPP payments to a later date (up to age 70). Your CPP payment will be increased by 0.7% per month (8.4% per year) after age 65. This could result in CPP payments being increased by up to 42%.

We encourage clients to think of their CPP as an additional income source that should be integrated into their total income stream in the most effective way. While we recognize it can be unpleasant to plan what would happen if you or your spouse passed away, it is something that should be considered when discussing CPP and retirement. The CPP Survivor pension amount depends on the surviving spouses age;

Survivor's Age	Survivor's Pension
Age 65 or Greater	60% of the contributor's retirement pension up to the maximum payable
Under Age 65	A flat rate plus 37.5% of the contributor's pension if the surviving spouse is not receiving other CPP benefits

CPP Survivor Pension

By planning for later stages of life, you may be eliminating some agonizing decisions for your spouse while you are still here to support them with the process. There are many factors that go into determining CPP amounts and withdrawal decisions such as tax rates and how they might vary through your retirement years as well as your anticipated health condition. In our view these benefits should be carefully analyzed since they are both guaranteed and indexed to the cost of living by the government over your lifetime.

OLD AGE SECURITY (OAS)

The second form of government pension for retirees is Old Age Security(OAS). This is a universal retirement pension available to all Canadians. Similarly to CPP, OAS income is fully taxable. Where CPP benefits are derived by the amount you've contributed in your working years, the OAS benefit is determined by years of residency in Canada. The requirements of OAS are as follows:

- You are age 65 or older
- You are a Canadian citizen or legal resident
- You have lived in Canada a minimum number of years since Age 18 (10 years for partial benefits, 40 years for full benefit).

While there is no early withdrawal option for OAS, it may be delayed similar to CPP. For each month past age 65 that you delay your OAS payments benefits will increase by 0.6% up to a maximum of 36% at age 70. However, OAS payments are clawed back for each dollar of taxable income over $86,912 in 2023. Like CPP, OAS payments are indexed to the cost of inflation and together can form a solid base to many retirement plans if integrated effectively.

WORKPLACE PENSIONS

DEFINED BENEFIT

As a retiree, if you are fortunate enough to have a defined benefit company pension plan, this will ease the process of achieving a successful retirement income. Having a fixed amount payout (defined benefit) throughout retirement will allow you to focus your efforts on other important factors which include family and health. You will generally be given your payout as a formula(percentage) of your income earning years and almost all of these types of plans are indexed to inflation. Defined Benefit pension calculations are unique to each plan. There are three main types; career average earnings, final average earnings, and flat benefit amount. Each has many variations to them as shown in the Table below.

	Overview	Example	
Career Average Earnings	Based on average earnings during the entire period you were a member of the plan.	Benefit percentage: Average salary: Years of plan membership: Formula calculation: **Annual pension:**	2% $40,000 25 $40,000 x 2% x 25 **$20,000**
Final Average Earnings	Based on average earnings in years leading up to retirement (last 5 years for example)	Benefit percentage: Best 5 Yrs: Years of plan membership: Formula calculation: **Annual pension:**	2% $70,000 25 $70,000 x 2% x 25 **$35,000**
Flat Benefit Amount	Monthly pension benefit based on a fixed dollar amount for each year you were a member of the plan.	Benefit amount: Years of plan membership: Formula calculation: **Annual pension:**	$65 25 $65 x 25 x 12 **$19,500**

Determining a Defined Benefit Pension

DEFINED CONTRIBUTION

Becoming more popular with companies recently this type of plan transfers the long-term risk of the plan to the employee rather than the employer. Employee and employer contribute a defined amount of money (often a certain % of your income) over the course of employment to create a lump sum of money to be accessed at retirement. Depending on how generous the plan is and how long the employee worked, investments within defined contribution plans can grow to be quite a substantial part of an overall retirement income plan.

Leaving your plan before retirement?
Most Defined Contribution (DC) plans require you to transfer investments out of the plan when you leave your employer. You will typically have 3 options to choose from;

- Transfer to an individual locked-in retirement account (LIRA), which can be invested in a range of securities
- Transfer to another pension plan, if they will accept transfer
- Transfer to an insurance company to buy a deferred annuity

A defined contribution plan does not pay out a fixed income or 'pay cheque' once you retire. Upon retirement or leaving a plan, Plan members typically have two options;

- Transfer to a LIRA, or a Life Income Fund (LIF) which is similar to a RRIF but with some restrictions on accessing the money in the account
- Purchase an annuity from an insurance company which will guarantee an income for life

Since there are many implications to all of the decisions surrounding accessing defined contribution plan benefits, some of which are irreversible, it is wise to have a long-term plan and consult a professional before making any benefit decision.

PRINCIPLE RESIDENCE

UTILIZING EXISTING EQUITY

For some, their principle residence can become a large unused source of retirement income. Many retirees have saved over the course of their life through mortgage payments to a creditor/bank and now have a giant asset that can be used to generate income. Depending on house values and mortgage rates it is important to view your house as an asset, that for some can be turned into income in later years. There are a few ways you can access your home equity which may include taking out a reverse mortgage or using a home equity line of credit. Both of these options need to be well planned and thought out before proceeding with, as each brings with it a certain level of risk to your plan, and may not be suitable for every individual.

DOWNSIZING REAL ESTATE

As you get older and your lifestyle changes, it might make sense to downsize your existing home or other real estate holdings. Using proceeds of sale to create or add to an existing retirement income portfolio is a great cushion for unexpected events and longevity of life. Sometimes it isn't about downsizing, but simply changing locations or suburbs and saving on certain expenses. Also, being a homeowner can be a hassle for some later in life. It takes a lot of work and time to maintain a larger home.

RISKS TO YOUR
RETIREMENT

There will be a number of factors that will affect your ability to generate a steady retirement pay cheque over the course of 20-30 years. As you enter the later stages of your working years, planning for your future income becomes increasingly important. By entering retirement without an income plan in place, you may be exposing yourself to considerable risks that you had not considered. There are three hurdles that must be addressed on every retiree's road map to financial security.

LONGEVITY & RISING EXPENSES

As life expectancy continues to increase, longevity risk remains a big piece of the retirement puzzle. When you refer to life expectancy tables, remember that statistically half of retirees live longer than they are expected ….and also that those who plan and have money will in general live longer than "average". Living longer also means that you are increasing your exposure to other risks such as rising medical costs and health care expenses. Many retirees underestimate their life span, which leads to them outliving their assets or having to curtail their lifestyle and this can put them (and their families) in a difficult situation during the later stages of life.

INFLATION & ASSET ALLOCATION

Inflation is the long-term tendency of money to lose purchasing power. We referred to this earlier, with the example that what costs $1.00 today will cost $2.00 in 30 years. In terms of retirement income, we need to think of the impact this will have on your assets. A significant part of any retirement income plan is ensuring that you hold investments with the potential to beat or at least keep up with inflation after tax. The following graph shows the impact inflation could have on $50,000 over 25 years. Remember, money isn't just money; more importantly money is purchasing power (what it will buy) and this will change over time.

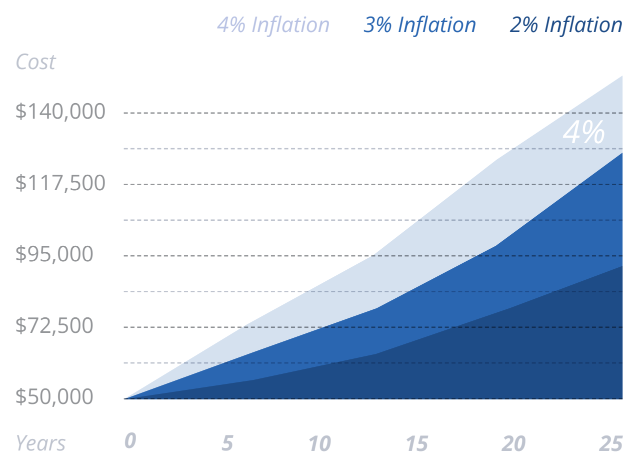
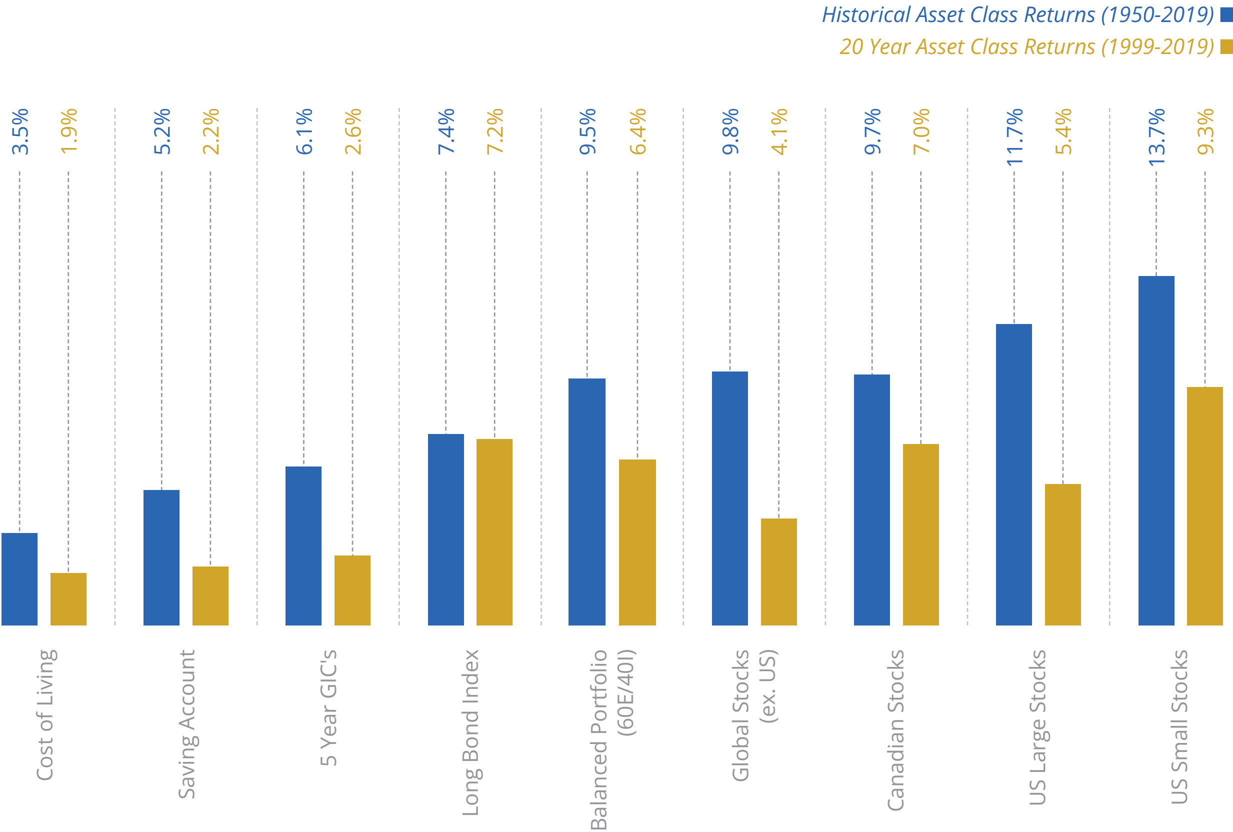


Figure 2: Hypothetical illustration showing the Effect of Inflation on $50,000 today. A $50,000 retirement income today may need over $100,000 per year in 25 years to keep up with inflation. It is crucial to plan for this.

It is impossible to overemphasize that many retirees and investors ultimately fail to understand the concept of risk. Risk in the media is commonly associated with the value of equities (stocks) that are subject to market volatility and therefore rise and fall in price each day. While the financial media tend to focus on this short-term price movement, the real risk to retirees is the answer to the question we previously asked;

"Will you outlive your money or will your money outlive you"?

Therefore, any proper retirement income plan needs to balance the effects of any short-term market volatility with the need to make sure you don't run out of money in the long-term. For most, that means the fear of losing your retirement nest egg, and choosing ultra conservative investment options such as a savings account or GIC, needs to be weighed against not keeping up with inflation and providing for an extended retirement timeframe. The chart below illustrates historical returns across asset.



Historical Asset Class Returns obtained from Morningstar's 2019 Andex Chart. Past performance is no guarantee of future results.
Individual performance may vary. Speak to an advisor about balancing risk and possible return.

This decision of what mix of assets to hold is the most important one most investors will make, and deserves to be fully understood.

MAXIMIZING SOURCES OF RETIREMENT INCOME – AND MINIMIZING TAXES!

In order to coordinate your decisions and develop a plan that integrates your assets, it is important to understand how each asset is taxed. Without putting a detailed plan in place to withdraw your assets in a tax-friendly manner, you may find yourself paying a significant portion of your retirement savings back to the government!

The first step in your retirement income plan is to determine your desired annual income. Once you know how much you will need (after-taxes), you need to identify the appropriate income sources to keep you in the lowest tax bracket possible each year. While a brief overview was provided earlier, Table 2 below provides a summary of each:

Account/Asset	Tax Considerations
Registered Retirement Savings Plan (RRSP/RRIF)	Taxable Income
Tax Free Savings Account (TFSA)	Tax Free Income
Non-Registered (Open) Account	Investment Income and Capital Gains are Taxed
Pension Plan Payments	Taxable Income
Government Benefits (CPP, OAS)	Taxable Income

Table 2:Tax Considerations

As you approach 60, you should have a good understanding of the assets in your investment portfolio, and you should also have a good idea on what your workplace pension (if any) may look like the day you retire. However, the decision on when to access your government benefits still looms. Below we outline a few strategies that can reduce taxes and improve your cash flow throughout retirement:

- Begin drawing down your RRSP/RRIF early, and delay taking government CPP until 70. This will help you lower the required RRIF minimum you have to take beginning at 72 (giving you more tax-planning flexibility) while increasing CPP payments by 42% for the remainder of your lifetime and insure you have a higher guaranteed life income.
- Average RRSP/RRIF withdrawals over time to remain in the lowest possible tax bracket (to avoid taxes and OAS clawback) and top up your income with your TFSA or non registered investments.
- Making early and averaged withdrawals to your RRSP/RRIF doesn't mean you have to spend the money, it just means you take the money out of the plan and pay the tax. You could then ensure your TFSA is topped up which for some can be the best way to maximize your estate.
- You can split RRIF (after age 65) and/or Pension income with your spouse.

THE MILLION DOLLAR QUESTION
WHEN AND WHERE (TO TAKE YOUR INCOME)?

It is a question that couples often spend many nights contemplating and the answer is... there is no 'one size fits all' answer. Everyone has unique circumstances. For instance, some of us are fortunate enough to be in great physical health and can expect to live a long life, while others may not be so lucky. We are also certain that each family has different portions of their savings scattered between the retirement income options outlined previously. This creates a level of complexity and adds a certain uniqueness to every retiree's plan. Change is also constant, and plans need to be reviewed periodically to ensure that you are keeping up to date.

With all of the variables involved most retirees find they can use help creating a comprehensive plan and staying on track. This is where working with a trusted advisor can help. At Ming & Associates we work with retirees to create a retirement income plan tailored to their vision of retirement, identifying effective strategies and minimizing taxes. We back this up with a trusted process, personalized service, and a committed team so you can be confident your entire financial roadmap will remain on track to meet your goals and dreams.

If you have any questions for us or if there is any way we can help,
we would love to have a conversation to learn more about you.

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