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Investor's Digest of Canada

July 6, 2018 Vol. 50, No. 13

Funding your retirement decades

When you go on vacation, you always lock your doors and buy trip cancellation insurance, common-sense strategies that protect your property and well-deserved holidays. But what about your retirement savings? Don't they deserve protection too?


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Annual RRSP ritual: Most readers have probably made their annual registered retirement savings plan (RRSP) contributions and filed away the papers. They won't even think about those savings until contribution crunch time next year or when they're ready to access those funds.

Back in the "good old days", many people worked at the same job until they were 65, when they received a defined benefit pension and the fabled gold watch. Today, fewer than four in 10 Canadian employees are members of a private pension plan, adding more strain on the need for a strong RRSP.

Living longer while unemployed: The need to stash away money for retirement is even more important when you look at rising life expectancy figures.

People used to retire and live just a few more years after that. For the total Canadian population, average life expectancy is now projected at 79 years for men and 83 years for women.

The lucky ones with "good genes" may end up in the growing cohort of people over 100, the fastest-growing age group in Canada, last estimated to have jumped by more than 40 per cent from 2011 to 2016. Retirement can now last several decades – that's a long time to be "unemployed".

Not everyone realizes the importance of an RRSP. Statistics Canada reports that between 2000 and 2013, the number of Canadians using RRSPs dropped by 16 per cent to 4.2 million and the total value of annual contributions dropped by 26 per cent to $22.5 billion.

The reason: fewer 25-to-54-year-olds were making contributions. Some Canadians are even withdrawing funds from their RRSPs before retirement, often to help buy a house, but cutting down on the amount of funds that can work to grow their retirement.

RRSP tax bite: RRSPs still represent the best way for many people to save for retirement, who often receive a tax refund along the way as an incentive to save. The RRSP funds grow over the years, temporarily free of income tax. When you start to withdraw the funds (at retirement), you pay the income tax, presumably at a lower tax bracket than when you made the original purchase.

While RRSP savings pass tax-free to a surviving spouse, if you are divorced, single, or widowed, the Canada Revenue Agency reduces your savings with a 54 per cent tax bite (in Ontario).

It's a painful lesson I had to share with a 70-year-old single client not too long ago. He had accumulated $2.8 million in a registered retirement income fund (RRIF). He was aghast to learn the government would collect $1.3 million in taxes on his death.

As we all know, life happens – and not always in a positive way.

Aside from your ultimate tax liability, achieving your retirement goals can be very difficult if unfortunate life events develop along the way, so taking responsibility for your retirement needs should be addressed sooner, not later.

Living benefits: You should consider a Critical Illness insurance policy that pays up to $2 million following the diagnosis of any one of more than two dozen conditions, including heart attack, stroke, cancer and bypass surgery.

A healthy person now contributing $500 a month to their RRSP can reduce that to $400 a month and use the other $100 for critical illness coverage. The difference won't appreciably affect the final RRSP, but it will definitely make a welcome difference in helping the person if he or she falls ill.

Arranging Long-Term Care (LTC) insurance is another defensive strategy. With the cost of long-term care in a nursing home now ranging from $4,000 to more than $10,000 a month, hard-earned retirement savings can deplete quickly. Around-the-clock home care is even more expensive.

Despite the growing need for the product as baby boomers cross the 65-plus threshold, fewer than 25 per cent of all insurance advisors have ever sold a long-term care policy, and many tier-one insurance companies have left the market.

However, a large cheque provided by a critical illness policy can be a lifeline for someone who becomes ill. In addition, taking an optional Return of Premium rider allows the return of all premiums paid if no claim is made. Imagine calling your auto or home insurer to get back all your premiums because you didn't make a claim.

High-limit disability insurance is now available with coverage of up to $150,000 a month or $2 million a year, all of it non-taxable.

Life insurance: One of the best ways to protect your retirement savings is to buy a life insurance policy. It is truly the most tax-effective and cost-effective financial instrument available today and enjoys unique treatment under the Income Tax Act. Not only does life insurance flow to your beneficiaries completely tax-free, it also bypasses wills and probate fees.

Its biggest benefit, by far, is that it provides financial security for your family and covers your tax liabilities. If you are in business, it can underpin your shareholders' agreement and guarantee payment to your family for your shares in a co-owned company when you die.

Married couples should consider inexpensive joint-and-last-to-die insurance to fund the ultimate tax liability that will occur on the second death.

Charitable giving: An RRSP also allows you to name beneficiaries. If you have planned for your non-registered assets or insurance to go to your children, you might want to think about naming a charity as the beneficiary of your RRSP/RRIF.

Charitable donations at death can help to protect the value of your RRSPs because the charitable receipts issued will help reduce or eliminate estate taxes. You may also consider buying a life insurance policy that designates a charity as the owner and beneficiary of the policy.

So, someone could take out an additional $50,000 a year from their RRSP/RRIF and make a charitable donation with that money. This will eliminate the taxes due on the withdrawal and at the same time reduce the amount of taxes that would be going to the government on the donor's death.

Maybe you would prefer taking that $50,000 a year and buying a life insurance policy valued at $1 million (assuming age 70). That money would be used to pay for the premiums and that would be considered a charitable donation. That donation will then eliminate the taxes on the RRIF withdrawals.

PPP is for (creditor) protection: The obvious way to optimize your retirement savings is by putting away as much as you can, but RRSPs have fairly low contribution limits ($26,230 for 2018).

Business owners and incorporated professionals should consider getting a personal pension plan (PPP) instead.

It allows you to save far more than allowed under current RRSP rules while at the same time saving taxes and enjoying an expanded level of creditor protection.

A PPP acts as a true pension plan, providing security in that you know how much you will receive every year under its defined benefit component. But it also gives you the option of taking the defined contribution plan route, which refers to the "defined" amount you contribute to the plan every year.

According to Canada Revenue Agency rules, you can switch every year between the two kinds of components depending on the cash flow needs of your business.

One of the big benefits of an PPP is that you can also deposit much more into it than you would in a traditional RRSP – as much as 65 per cent more, depending on your T4 income and years of service.

A recent case: Sheila, age 55, owned a distribution company incorporated 10 years ago. She has already saved $285,714 in RRSPs and plans to continue making the maximum contributions each year until she turns 65.

If she stays in a regular RRSP, she will accumulate $1,570,905 by age 65. But if she chooses the PPP strategy with its substantially higher annual contributions, she will accumulate $2,272,000 at 65 – that's 45 per cent more than if she had used RRSPs to save for retirement for the same level of risk.

Not a DIY project: Don't do it alone. Regardless of how you save for your retirement, get help now from experienced professionals to deal with tax matters, insurance issues and legal issues. With proper planning in place, your lifestyle can be maintained, your ultimate tax liability minimized, and unfortunate bumps along the way won't derail your plans.

Our team of experienced advisors is available across Canada. Call us for a consultation, we'd love to help.

Mark Halpern is one of Canada's top life insurance advisors, a Certified Financial Planner (CFP), Trust and Estate Practitioner (TEP) and CEO of WEALTHinsurance.com®. He guides successful business owners, who are already challenged for time, through the complex process of ensuring the people and organizations they care about are taken care of. Mark collaborates with your professional advisory team to achieve your desired outcomes. His approach is simple. He gets you organized, provides a big picture view of your financial affairs, determines your strategy and helps you take action. He can be reached at 416-364-2929, toll-free at 1-866-566-2001 or by email at Mark@WEALTHinsurance.com. Visit WEALTHinsurance.com/toolkits.html for your FREE Estate Planning Toolkit.