NetWorth

Plan to retire one day? Make sure your financial plan measures up

Retirement is one of life's most important financial goals. While it's easy to envision what you want that lifestyle to look like, it takes a whole lot of planning and saving to turn the dream into reality.

One of the most successful ways to achieve an ideal retirement is to have a financial plan, yet a new report by the BMO Wealth Institute reveals some alarming news. In the past seven years, it seems, there's been a dramatic decline in the number of Canadians who have a written financial plan - from 58% in 2008 to just 38% in 2014. Their excuses? They don't need one, they haven't gotten around to it, they think it's too early to prepare, they don't have an advisor, or they just haven't given it much thought.

In 2014, one-third of all Canadian adults (33.8%) were not preparing financially for retirement, either on their own or through an employer pension plan. Furthermore, almost two-thirds (59.6%) did not know how much money they would need to save to maintain their desired standard of living during retirement. Additionally, nearly one-third of those surveyed (29.5%) were not very confident or not at all confident that their household income at the time of retirement would be enough for them to maintain their desired standard of living.

The retirement landscape is rapidly evolving post–financial crisis and how Canadians react and adapt to these changes will impact the waves of retires who are fast approaching their retirement years. The first wave of baby boomers reached this age in 2011, so we are now experiencing Canada's retirement boom.

While the early boomers (born between 1946 and 1955) will be trend setters and game changers in the retirement landscape, the late boomers (born between 1956 and 1965) and the gen-Xers (born between 1966 and 1979) should take note of their experiences.

To get a better understanding of the retirement landscape, and to take advantage of the experiences of current retirees, it helps to concentrate on the four P's of retirement planning:

People – a portrait of retired and nearly retired Canadians.

If you're going to be single in retirement, take action immediately – the ball is in your court. If you have a spouse or partner, an effective retirement plan requires that you both become personally involved in the planning process. When planning your retirement, first and foremost, expect the unexpected – and then prepare for it. Retirement came at an unexpected time for 40% of retirees. Breaking that number down, 29% had to expedite their retirement, while 11% had to delay it.

Let's connect

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Point of view - what's top of mind when it comes to retirement?

Retirees and near retirees have a unique set of concerns, many of which are the result of switching from earning a living to living on a fixed income. The most common of these concerns can be split into two key areas: health and money. The coveted goal of retirement planning is to build enough wealth to guarantee security and comfort in retirement.

Planning process - a financial plan is a powerful tool.

Financial planning takes into account all aspects of your personal and financial situation. A good financial plan can help you answer important questions: What will your retirement look like? What do you want to do in this next stage of life? And, most importantly, how are you going to pay for the retirement you envision for yourself? As such, each plan looks somewhat different. However, there are many similarities in the tools used to create those plans. It's all-encompassing to include investment and tax planning, retirement expenses projection and income needs analysis, life and health insurance needs, government and employer pension benefit review, long-term care needs assessment, and estate planning.

Preparedness - are you getting ready for retirement?

Almost two-thirds (61%) of Canadians believed they were ready to retire from a non-financial standpoint (mentally, physically, socially, and emotionally), and almost as many (58%) felt they were ready financially. However, the overall sense of not being prepared to retire, considering both financial and non-financial aspects, has increased somewhat since 2008 (from 32% to 41%). This loss of sense of preparation is most likely due to the lack of planning or preparation amongst more than half of those surveyed in areas such as consolidating debt (57%); creating a detailed retirement budget (65%); and converted retirement savings into income (75%).

Regardless of what age and stage you're at, a robust financial plan can help you achieve the lifestyle you want once you leave the workforce. And it's realistic, evolving as you do to reflect any changes in your life, expectations, financial situation, and goals.

Here are some tips to help you design a financial plan that's right for you:

- Seek help - Professional advice is paramount when calculating financial projections and researching investment information. And it's critical when dealing with complex tax and estate issues. Financial professionals also act as a sounding board for your questions and concerns, ensuring you're comfortable with your decisions (especially during times of heightened market volatility) and keeping you on track with your financial plan.
- Prepare - Put pen to paper by detailing your living expenses and spending habits to project your retirement needs based on your current spending .Set up a continuous savings plan using whatever savings vehicle that is appropriate for your situation, whether it's a Registered Retirement Savings Plan (RRSP) or a Spousal RRSP. And make the most of a Tax-Free Savings Account (TFSA) to save and invest tax-free.
- Think young - With the life expectancy of Canadians increasing, your retirement might not only start earlier than expected but it might also last longer. Start early and keep saving until you have a significant pool of assets that will generate the income you need to live a comfortable retirement, regardless of when that day arrives.
- Be flexible - Your financial plan is not set in stone. Meet with your financial professional at least once a year to review your retirement readiness, as well as any time there are significant changes to your personal or financial situation.

We believe proactive planning and professional advice go hand in hand. Let's discuss if you would like a copy of the BMO Wealth Institute report titled Retirement Planning: How do your retirement plans measure up?

Income Tax Assessments – What to do with your refund

As the weather gets warmer, you may have already received or will soon receive an assessment from the Canada Revenue Agency (CRA) of your 2014 personal income tax return or from Revenu Quebec (RQ) if you also file taxes in Quebec.

If you are receiving a tax refund, it may be worthwhile meeting with your BMO Nesbitt Burns Investment Advisor to discuss your plans for these funds, such as repaying non-deductible debt, or catching up on your contributions to your RRSP, TFSA or RESP.

Generally the CRA and RQ process paper returns in four to six weeks, but electronically filed returns can be processed by the CRA in as little as eight business days (or by RQ within 14 working days). However, both the CRA and RQ advise to wait at least four weeks after filing your return before contacting them about the status of your refund (longer if you file a paper return with the CRA after April 15). Last year, according to the CRA, the average individual tax refund received was $1,655.

A recent study undertaken by BMO Nesbitt Burns revealed that 40 per cent of Canadians who expect to receive a refund this year will use it to cover household bills and/or reduce their overall debt load. Canadians also plan to use their tax refunds (or a portion of them) to:

- Save or invest (25 per cent)
- Travel and/or purchase leisure items (14 per cent)
- Do home renovations or pay down their mortgage (9 per cent)
- Donate to charitable causes (1 per cent).

The remaining respondents were either unsure or did not indicate a specific use for their refund.

Income Tax Assessments

From a tax perspective, ensure that you take the time to review your Notice of Assessment with your tax advisors to determine if the CRA (or RQ) has made any adjustments to your filed tax returns. It is important to review the assessment now and understand any changes since there are specific time limits to object to disputed assessments.

Finally, if you have a significant tax refund or alternatively were assessed interest and penalties for late or deficient tax instalments, be sure to consult your tax advisor to determine the appropriate level of future quarterly instalments. In particular, investors with larger portfolios should consider reviewing and planning for potential instalment requirements with their tax advisor - with assistance from your BMO financial professional. For more information, please ask for a copy of our publication "Tax Tips for Investors".

New Tax Rules Affecting Your Estate Plan

Late last year, several key income tax proposals affecting estate planning, which originated from the 2014 Federal Budget, were formally enacted into law.

These provisions, which will be effective beginning in 2016, will have significant implications for existing and future testamentary trusts, as well as spousal, 'alter-ego' and 'joint-partner' trusts. Additionally, these changes in the law will affect planning for testamentary charitable gifts. The following is a brief summary of the forthcoming changes; please consult your tax and estate professionals for specific guidance on how these amendments may affect you or your family.

Testamentary Trusts

A common estate planning strategy involves the use of a "testamentary trust" created at death (typically in the deceased's Will) to achieve income splitting tax benefits. Currently, this type of trust is able to access the graduated marginal tax rates available to an individual, allowing tax savings to be achieved on income that is retained in the testamentary trust. In contrast, a trust created during lifetime (an "inter-vivos" trust) pays tax on undistributed income at the top marginal rates for individuals.

However, because the government has become concerned with the growth in the tax-motivated use of testamentary trusts, it announced its intention in the 2013 Federal Budget to review and consult on possible measures aimed at eliminating the special tax benefits that arise from taxing the income of testamentary trusts at the marginal tax rates. Following a consultation period, the 2014 Federal Budget reaffirmed the government's intention to proceed with these measures, which include the application of the flat top tax rate to income taxed within a testamentary trust effective for 2016 and subsequent taxation years.

Two exceptions to the imposition of the flat top tax rate will apply. Firstly, the first 36 months of a deceased individual's estate following the individual's date of death may be eligible for the graduated tax rates, provided the executor does not distribute the estate assets during this period (if so permitted under the terms of the Will). Secondly, graduated marginal tax rates will continue to apply for certain testamentary trusts (defined as "Qualified Disability Trusts") whose beneficiaries are eligible for the federal Disability Tax Credit.

The new rules for testamentary trusts will also eliminate some of the other special tax treatments accorded to testamentary trusts. For example, beginning in 2016, testamentary trusts will be required to make income tax instalments and must have a December 31 taxation year-end, similar to inter-vivos trusts.

Although these forthcoming changes in 2016 will eliminate access to the graduated tax rates on income retained and taxed within all existing and future testamentary trusts, trusts created in your Will (such as a trust for each child's family) may still provide income splitting opportunities since they can be used to distribute or "sprinkle" income on a discretionary basis to family member beneficiaries in the lower tax brackets. In addition, testamentary trusts offer many other benefits (including control and protection of assets), such that they will continue to be an important consideration in tax and estate planning.

Spousal, Alter-Ego and Joint-Partner Trusts

Another unexpected, though important, related legislative change introduced with these measures will deem capital gains arising in spousal trusts (or 'alter-ego' trust and 'joint-partner' trusts) on the death of the beneficiary individual after 2015 to be payable (and taxable) to that individual, rather than the trust as is the case under the existing rules. This change to the incidence of tax can dramatically impact an existing estate plan particularly in situations (such as a second marriage or 'blended family') where the beneficiaries of the deceased individual's estate are not the same as the ultimate beneficiaries of the trust. Also, charitable donation strategies involving these types of trusts may be adversely affected.

Because of the significance of these forthcoming changes, it will be important to consult with your external tax and legal advisors to determine any impact to your current Wills and estate plan, as well as any existing testamentary, spousal, 'alter-ego' or 'joint partner' trusts established by you or your family members.

Estate Donations

The charitable donation tax credit is generally subject to an annual limit of 75% of net income. However, for donations made in the year of death the credit limitation is increased to 100% of the deceased's net income and any donations that cannot be claimed in the year of death can be claimed in the deceased's prior year tax return, also up to 100% of net income in that year. There is also a special provision within the current tax legislation that allows specific donations made pursuant to a Will to be deemed to have been made by the individual immediately prior to his or her death, even though the actual transfer may occur during the estate administration. This treatment can be beneficial in allowing a donation tax credit to reduce taxes otherwise payable at death in the individual's terminal tax return (or in the year preceding death). Similar provisions apply where an individual designates a qualified donee as a beneficiary under an RRSP, RRIF, TFSA or life insurance policy.

Conversely, under the current legislation, donations made by an individual's estate (which were not pursuant to specific terms of the Will or beneficiary designation) do not qualify for this treatment and can only be applied against the estate's income tax otherwise payable, which in some cases, may not be sufficient to allow the full benefit of the donation tax credit to be realized. However, new legislation originating from the 2014 Federal Budget will allow more flexibility in the tax treatment of charitable donations in the context of a death occurring after 2015. Specifically, a donation made by Will (and designated donations) will no longer be deemed to have been made immediately before death. Instead, these donations will be deemed to have been made by the estate at the time the specific property is donated to the qualifying donee. As a result, further planning opportunities will exist after 2015 for qualifying estates as the estate trustees will have additional flexibility to apply the donation tax credit (from a donation made within 36 months of death) to:

i. the taxation year of the estate in which the donation is made;
ii. an earlier taxation year of the estate; or
iii. the last two taxation years of the deceased individual.

In light of these changes forthcoming in 2016, you should consult with your tax and estate professionals to fully review the possible tax implications and benefits of any charitable bequest strategy within your existing estate plan.

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