Your Retirement Plan

Maximizing Retirement Income

After years of saving, you're ready to use your accumulated wealth to finance your retirement. Income can come from a variety of sources: a part-time job, employer pension plans, government pensions, RRIFs and annuities. If you don't have an employer pension plan you may rely solely on your savings and government pensions to provide the income you need. Maximizing retirement income involves maximizing your entitlement to income from government sources and managing withdrawals from RRIFs and locked-in funds, while minimizing income tax.

Government pensions

Canada Pension Plan/Quebec Pension Plan (CPP/QPP) and Old Age Security (OAS)—both of which one must apply for—form the basis of the Canadian retirement income plan and for 2008 together they provide a maximum payment of just under $17,000 per year.

To maximize government benefits:

- Apply to receive CPP/QPP as early as age 60 (five years before qualifying for OAS). Collecting the Canadian pension early will reduce your monthly entitlement, but you will receive payments over a longer period of time. Furthermore, the lower CPP payment may result in a lower annual income and minimize the risk of OAS payment reduction.
- Consider splitting CPP entitlements with your spouse if he/she is in a lower tax bracket. Splitting benefits between two people who are in different tax brackets will reduce the total tax paid by the family and may also help to preserve some of the OAS benefits, which may be reduced based on the level of income.
- Apply for OAS in the year you are turning 65. If you are over 65 and not currently receiving OAS, you should apply to determine if you qualify for a full or partial pension.
- Spread the receipt of income evenly during retirement years. OAS may be clawed back if retirement income is above a certain threshold. It is important to structure income from an investment and RRIF portfolio to minimize the loss of OAS.

Employer pensions

Roughly one-third of working Canadians belong to an employer sponsored pension plan, and for those who participate in a Defined Benefit plan, they are often unclear about their pension benefit entitlement at retirement.

To understand your entitlement under a Defined Benefit Pension Plan:

- Ask your employer to confirm your monthly entitlement and when you can start receiving pension benefits. Does the entitlement increase if you begin receiving it later or, conversely, is it reduced if you start drawing benefits early? Is the employer pension plan tied to CPP

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benefits? If so, your pension entitlement may decline at age 65.

- Confirm how much of your pension plan your survivors are entitled to receive (i.e., if you pass away, what is your surviving spouse entitled to get? Is it a monthly benefit or lump sum?).
- Ask about inflation protection. Annual inflation as low as three per cent can significantly erode the value of your pension income over a 20-to 30-year period.

RRSP income options

Your RRSP, the registered vehicle in which you accumulated savings, is used to provide retirement income. It's wise to learn about all of the RRSP maturity options at your disposal. You have important choices to make as you approach retirement, and at the very latest, by the end of the year you turn age 71—the latest point to which you can now have an RRSP as a result of recent changes. Keep in mind that all with drawals or income from RRSP funds will be taxed as ordinary income. Consider these retirement income options:

- Roll your RRSP into a Registered Retirement Income Fund (RRIF). A RRIF is like a reverse RRSP; instead of making contributions to the plan, you make taxable withdrawals but the balance in the RRIF will continue to grow in a tax-deferred plan.
- Buy a life annuity to guarantee income for life and spread the tax burden over multiple years.
- Make a lump-sum cash withdrawal of the entire amount in your RRSP – this option will result in tax payable on the balance in your RRSP all at once. This may be beneficial in a year where you have only minimal income from other sources, however, you would also relinquish the opportunity to continue to invest the funds in a tax-deferred account.

The good news is that you are not limited to one maturity option; You can select a combination of some or all of the above to meet your needs.

LIRA income options

A LIRA is a locked-in RRSP. Funds in a LIRA originate from pension money and are more restrictive in terms of maturity options and permitted withdrawals. In some cases, the restrictions could hinder you from maintaining your desired lifestyle. As with an RRSP, you must "mature" the LIRA by the end of the year you turn 71 and select one or more of the following options:

- Purchase a guaranteed life annuity. Your payment will be influenced by factors such as your age, current interest rates, the period you want your payments guaranteed in the event of your death, and whether all or a portion of the payment will continue for as long as your spouse lives.
- Roll the funds in to a LIF, LRIF or prescribed RRIF, depending on the provincial legislation regulating the original pension plan (not all jurisdictions have the same maturity options). In certain provinces, a transfer to a LIF may allow for unlocking of a portion of the LIRA.
- Take advantage of the ability to "unlock" small balances in locked-in plans—some jurisdictions allow you to close your small accounts.

Pension income splitting

Recent amendments to tax legislation allow for a transfer of up to 50 per cent of eligible pension income (see definition below) to a spouse, beginning in 2007. This change provides couples with a significant opportunity to split retirement income. The allocation

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of this income is done by electing annually in each spouse's tax return. For income tax purposes, the amount allocated will be deducted from the income of the person who actually received the eligible pension income and this amount will be reported by the other (lower-income) spouse.

From the perspective of the recipient spouse, eligible pension income will include:

Canadians who are 65 and over and receive:

1) registered pension plan payments;

2) RRIF payments (includes LIF and LRIF payments);

3) lifetime annuity payments from registered plans; or

4) prescribed and non-prescribed annuity payments (interest component only)

Canadians who are 65 and under and receive:

1) registered pension plan payments; or

2) amounts (2) to (4) above only if received as a result of the death of a spouse

Asset re-positioning

Many of the assets you've earmarked for retirement are now needed to provide income for retirement. Asset re-positioning is one of the most important issues a retiree faces. For example, investments may be increasingly relied upon to provide cash flow or may be liquidated to supplement retirement income.

Reverse mortgages

In some cases, our home is our largest or only asset; however, the family home does not provide annual cash flow to supplement income during retirement. In fact, it could be a significant income draw due to maintenance, property tax and other costs. And yet, many of us are not willing to part with the many happy memories associated with our homes. In those instances where selling is not an option, a reverse mortgage may be a suitable alternative. It allows one to continue living in the family home, while providing access to the equity that can be used to fund retirement income.

What's next?

Your BMO Nesbitt Burns Investment Advisor is familiar with your financial circumstances and will help you identify how much income you will need during retirement and how to supplement your government and employer pension with income from your registered and non-registered portfolios.

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