

TAX ALERT



TAX ALERT is a commentary on topics of current interest – usually topics relating to recent changes in tax law, new CRA administrative practices or current interpretations arising from tax cases. Professional advice should be obtained before acting on any of this information.

RETIREMENT – NEW TIMES – NEW RULES

You have lived about two thirds of your life raising family and working. Now you can look back with some pride – the kids are doing well and no need to worry about them anymore. Work also went well and you think you have the bucks to retire soon. Life will be different then as you turn your attention to more leisure time, good health and prosperity. Are you ready for that and whatever else goes with it?

Lives are longer now than they once were so retirement funds need to be larger so you don't run out of money. If you have something left over when you die, where is the money going to go? Usually it goes to family of course but that involves some thought if children's marriages are rocky or if one of them is vulnerable and needs a different solution than an outright bequest. You might even want to look to grandchildren and their needs and how best you can help them. Should they be treated equally or should some get a bigger chunk of the pot than others so you can open opportunities for them they might not otherwise be able to afford - anywhere from more education to buying a first home.

As you can see, there are many financial issues to deal with in retirement and they are unique family to family – one size does not fit all. So, let's deal with a few specific ones.

PENSION OPTIONS

If you are fortunate enough to be a member of a pension plan there are two important things to consider before you retire.

The first one is whether you take a pension under the plan or do you transfer pension money to a self- directed retirement account so you can manage the funds yourself. With a pension plan you may lose money if you die after the guarantee period ends but before normal life expectancy. On the other hand, if your money is in a locked in retirement account your estate gets to keep what's left. For most, the pension plan offers better income security and is the better choice. Add pension income to CPP and OAS and things start looking pretty good.

A second consideration is what length of guarantee period should you select under the pension option. It will depend on your health and the expected longevity of your spouse if you are married. In any event, opting out of some guaranteed term in exchange for slightly higher pension payments is not a smart decision. Your spouse may insist on a minimum guarantee period depending on the laws in your province of residence.

INVESTING

Until you retire your emphasis is on growing your investments so you have the money to pay the bills in retirement. Whether you have a RRSP or investment portfolio maximizing your return gets a lot of attention before retirement and you have the flexibility to do that over a long term even with some speed bumps along the way.

In retirement, emphasis changes from growing your savings to preserving capital because it is now more difficult if not impossible to recover with the shorter period of time ahead of you. Therefore, investing should become more conservative in retirement so your rate of return will decline accordingly. When calculating how much your investments will earn after retirement don't count on more than about 5% because you just shouldn't take the risk.

THE COTTAGE

If you are lucky enough to own a cottage and it has been in the family for a long time, it is likely to be a significant part of your estate and some difficult issues are almost certain to arise.

What if one of your children wants it and the others don't or worse still what if all of them want it. How do you deal with either of those options? Do all of them have the resources to maintain it? How do you set up a structure with multiple owners all trying to get along? In financial planning, this is one of the big nuts to crack.

It may be better to make better tax wise to make your cottage your principal residence when you sell it or die rather than your home because the cottage gain is so high. Tax planning is tricky in order to maximize the benefits of the principal residence exemption.

SECOND MARRIAGES

In a second marriage or even in a first one, provincial family law has some rules that you must play by. There is more sensitivity in a second marriage. In Ontario, for example, the surviving spouse can take his or her entitlement under family law equalization rules rather than under the terms of your will. That being the case, it certainly is a good idea to discuss your will with your spouse and come to a solution that you both can live with.

If your planning is integrated in your wills so much the better. For example, as part of your agreement you might leave certain assets in a spousal trust and on the death of the second to die the remaining assets pass to the children of the first to die. That's just a sampling of things to sort out in all marriages but especially in second marriages. In wills where spouses each agree to integrate their wills (mutual wills) to get the desired outcome for their families of both spouses, it's very important that this agreement be reflected in a contract between the spouses.

DISABILITY

Unfortunately, it seems to be more common these days than it once was for children to have a disability such as autism, ADHD or similar syndromes all which are primarily intellectual disabilities. Consequently, disability may limit the child's ability to own property or make valid legal decisions. Use of a family trusts may become a necessary choice to resolve ownership and income issues

The disabled child may be on social assistance and provincial laws could also prevent your child from owning property or having significant income or else they forfeit their assistance benefits. You need to consult with family and find out the best way you can contribute funds in your will for the benefit of the disabled child so it fits in with the planning of others in the family. Two very common choices for funds to help fund the needs of a child with disabilities are a Henson trust and a Registered Disability Savings Plan.

And finally, does your will recommend a personal guardian if you have a child with a disability.

FAMILY LOANS

Too often parents do not spell out the expectations of cash advances to children. Are they gifts or are they loans and will they be forgiven on death or will the outstanding amount come out of the child's inheritance. Let's be mature about this and get the terms down on paper. Other siblings may justly be concerned about unfairness to some over others so best to sort it ahead of time. A family meeting to explain what you are doing and why is not a bad idea.

Family loans from the Mom and Dad bank to allow children to purchase a home are becoming far more common. It was recently reported that in British Columbia family financial assistance was provided in 42% of new home sales. These are big bucks so documentation is a must.

GRANDCHILDREN

When you are in retirement your grandchildren are probably still in school or some of them are possibly going to university, community college or travelling the world. All of this takes money - most of it which they do not have. If you have the resources, you may want to consider contributing to a RESP or paying tuition while you are retired. There isn't even anything particularly wrong with helping them to finance a trip around the world if that is what they want to do. Maybe a motorcycle crosses the line. You will get a lot of pleasure seeing the look on their faces if you do it now so think about it.

WILLS AND POWERS OF ATTORNEY

It would seem that having current wills and powers of attorney is a no brainer but it is. Some of my clients confess to the fact that these documents are out of date or might not even be valid after there has been a divorce and new marriage.

If you are in that boat, take some time to go see a lawyer and get this done. Make sure that beneficiary designations are consistent with your RRSP/RRIF plans and insurance policies. And make sure that you have considered that jointly owned property passes to the co-owner directly and not under the terms of your will. There are lots of traps so get some legal advice.

And think carefully about who should be your executors and attorneys under financial and health powers of attorney. Maybe some of your kids will be better at it than others and should have the casting ballot in case of disagreement.

SPENDING IN RETIREMENT

The many aspects of financial planning in retirement are as unique as faces in a crowd. Do some deep thinking and then work with advisors who know their stuff.

In most cases spending patterns are already set before retirement and will not change much after so don't count on a big decrease in cost of living. In most cases that does not happen and any decrease will be modest – studies indicate about 5% on average.

While your spending remains much the same the day before and the day after you retire, that will change as you move on in age at around age 80. At about that time costs are likely to go up and perhaps quite significantly because it's then that higher personal care costs begin. You may be faced with additional amounts for medications, attendant care and maybe even retirement home costs which can be very expensive. You can't determine how long you will live or when added costs will kick in as you age so take that into consideration and have a budget reserve.

I wrote an article called *Guaranteeing Retirement Income* and it is on our website, www.personalwealthstrategies.net under Financial Planning Alerts. Have a look because you

may find it helpful. And if you want some further advice in areas of retirement other than financial planning, have a look at Donna McCaw's book, *It's Your Time*. It not only covers off financial issues but it also discusses health and wellness, leisure, relationship and transitions. It is a helpful read.

Good luck with your retirement. Use some of these available hours to get your retirement planning in order because you will be in a new paradigm!

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