Assante WEALTH MANAGEMENT

Retirement Planning Readiness Tips

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All Things Retirement (for Canada) by Shaun Humphries

About 7 million Canadians will retire in the next two decades. There are a lot of factors that go into developing a successful retirement plan. The strategies are not difficult, but it's important that you do your homework well in advance to make sure there are no surprises. A successful retirement, like a successful life, rarely happens by accident. It happens by design!

When it comes to building and maintaining an active retirement plan and strategy, the following, are some points to consider:

1. It's essential that you take care of your health and make fitness a priority – Your quality of life, especially in retirement, will be tied directly to how you feel and how much energy you have. You can do an excellent job around planning for retirement. However, if you lose your health, many of your retirement dreams will be compromised. Start now, to look after your health through regular exercise, proper nutrition, nurturing relationships and broad social networks, and become expert at de-stressing.

2. Pay off your debts while you're still working – With rising house prices and cost of living, this is proving to be a challenge for many. According to a CIBC poll, about 59% of retirees are in debt. This could turn into a black hole if a downward spiral pattern emerges. Layoff the credit cards unless you pay them off monthly and realize you may not have the same lifestyle as you did before retirement. For most people, as they transition into retirement they have far less flexibility in their cash flow, so strive to eliminate debt by your retirement date.

3. Start saving earlier and save more – although it's never too late to start. Ideally, you want to begin your plan as early as possible. In a TD Bank poll of retirees, 58% suggested that the start early idea is a meaningful way to defend against outliving capital. There's no doubt that age 60 is now the new age 40 and people are working longer and putting off retirement. If you have the flexibility to do this with your professional talents or work, it's something to consider. Work provides meaning, social interaction, and the possibility of not putting pressure on your savings so that investment capital lasts longer.

4. Travel while you can – Health issues and pre-existing conditions can put a real drag on your desire to travel. Insurance costs may become prohibitive, or you may be denied insurance altogether. Travel is number one on many bucket lists. For those of you who are traveling a lot already, and want to continue this lifestyle well into retirement years, you may want to consider purchasing travel health insurance that guarantees your future insurability. A few companies offer these products and are well worth investigating.

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5. Don't be afraid to retire – In that TD poll, 11% were very positive about retirement, and 48% were positive, and 37% were concerned about their futures as retirees. Often the anxiety that exists before retirement is reduced after the first two years retirement. Retirement is not a one-size-fits-all concept. Make of it what you want. It is a transition rather than an event, and it's up to you to make sure it's a successful transition.

6. Successful retirees were conscious of the importance of their social relationships. The happiest retirees, are active and have many positive relationships in their lives. Satisfaction in retirement is driven much more by attitudes and behavior that by the amount of money in the bank. Research continues to substantiate this philosophy. Many people tend to overestimate the impact of material possessions and underestimate the effect of social connections.

7. Recognize that wealth comes from choices and not from chances – Having said that having wealth is not the be-all and end-all of determining retirement happiness. However, there is an absolute reality that you need financial capital for retirement. Smart retirees didn't wait for luck to make them wealthy. It takes planning, consistency seeking the advice of professionals in getting the basics right. Be careful of an extravagant lifestyle that takes up too much of your cash flow, stay broadly diversified, and when you save, make your money work hard for you.

8. Make sure you have a written plan – People who are serious write down their retirement goals. Putting plans in writing lets you identify where you are, where you want to go and what you must do to get there. Your goal setting should include such areas as; where you'll live, income needs, travel goals, health goals, relationship goals, legacy goals, etc.

9. Learn to control your emotions – What works in the long term is often in direct contradiction to people's immediate emotional impulses. When it comes to sex, food, and money, emotions are our biggest enemy. We tend to start with great intentions and then get lured in the wrong direction through quick fixes, easy solutions and too good to be true ideas. There are few certainties when it comes to retirement investing. The key to success is to tilt the odds in your favor by making decisions based on probabilities rather than possibilities.

10. Understand your cash flow requirements – These days, it's rare indeed for people to track their cash flow. However, as you approach retirement, it's vital that you master your cash flow requirements. As a starting point, if you're a salaried employee, take a look at your after-tax deduction income that is flowing to your family bank accounts. Subtract from this income those expenses that you feel will no longer be around when you retire. Examples could include; mortgage payments, RRSP contributions, maybe certain costs for the kids. Once you have subtracted for these expenses, this is essentially the level of after-tax income that you're currently living on. It's been my experience that few retirees can afford to live on a lot less than this number. Rules of thumb abound. A common one is that retirees need 70% of their retirement income. In general, I believe that rules of thumb are irrelevant. What's important are what your actual expenses will be. Every family is unique, and your retirement plan needs to reflect that fact.

11. Understand cash flow requirements by tracking them for a period of time – Although I don't necessarily believe budgets are something that most people can adhere to consistently, I do think that monitoring cash flow from time to time provides essential information for families as they plan for retirement. Tracking expenses sensitizes people to not only where they spend their money, but also categories that tend to be more periodic. Most people have a pretty good idea what their typical monthly expense trends are. However, what they often forget about are the periodic expenses. These expenses can be for such things as; seasonal expenses (snow clearing or gardening), recreation hobbies, travel or some forms of

insurance payments. These periodic expenses can add up, and it's vital to be clear on these dollar amounts before you retire. Larger costs, over and above your regular monthly retirement income can put a real monkey wrench in your budgeting process unless you prepare in advance.

12. Understand the difference between discretionary and nondiscretionary expenses – When you retire; it's critically important that you are clear on what expenses you have some discretion over and which expenses are month-to-month and will always be there for you. Your nondiscretionary costs are not negotiable. Matched up against these expenses should be predictable income sources that are not subject to market volatility. On the other hand, discretionary expenses provide you with some room for margin. Examples would include; holidays, helping the grandkids, gifts, etc. Because there is discretion on when to incur these payments this flexibility can come in handy. One example of this would be times when capital markets decline in value. It is during these times when it would be nice to be able to hit the pause button and not draw down on assets that may be temporarily down in value. If these assets were helping to fund discretionary expenses, you could defer these expenses until the markets have improved. You don’t have the same, flexibility with nondiscretionary expenses.

13. Understand investment basics – I don't expect my clients to be investment experts. However, we make a significant effort to try to educate our clients on investment basics. We do this because over the years we have found that investors who have a basic level of knowledge act with far more discipline than those investors who have not spent some time wrestling with investment basics. Retirees, who have a basic level of understanding around investment planning, take advantage of the laws of probability more efficiently and can make better use of their financial advisors.

14. Rules of thumb for a retirees investment mix may not be relevant – One of the most challenging things for retirees in the current environment is the low-interest rates. At the time we are putting together this tips list, ten-year government bonds are paying 2.1%, and we’ve been at some of the lowest interest rates in several decades. This creates a problem for retirees. Historically, retirees have been encouraged to use a rule of thumb around how much equity or growth investments they should have in a portfolio. The rule of thumb was, "100 minus your age". This represents the amount of growth or equity investments to have in your portfolio. As a result, based on this formula, a 65-year-old should have no more than 35% of the portfolio in growth investments. Of course, here is the challenge. If fixed income investments are paying in the range of 2% to 2.5% on 65% of the portfolio, and inflation is averaging 2% to 2.5%, that's a great strategy for going broke safely. As a result, many retirees are running portfolios that are flipped in the opposite direction of these portfolio guidelines. Often, these portfolios are 40% income investments and 60% growth investments. Although this portfolio strategy is not in line with the rule of thumb, it's entirely in sync with the reality of the current economic environment. It's a great example of how retirement planning needs to be nuanced and customized to each retiree’s situation.

15. When retiring you may need two types of portfolios – This idea goes along with rule 14. As a result of the historically low-interest rates, today's retirees hold a much more significant percentage of their portfolio in growth investments than historically has been the case. This has led to an increased risk level for many of these portfolios. As a result, we have encouraged clients to have two portfolios when they retire. One portfolio is what we refer to as the engine of economic growth. This is a portfolio that we expect will give us the returns necessary to fund the retirement plan and will be the portfolio that we will harvest profits from to produce income. The second portfolio is what we refer to as an "income wedge" portfolio. This portion of the portfolio is structured to provide income to the retiree over the next 3 to 5 years. As a result, this portfolio is comprised of very conservative investment securities, such as; GICs, term deposits, government bonds, corporate debentures and conservative income funds. Over time, the retiree will draw down on this income wedge portfolio to fund income. On a regular basis, the client would harvest profits

from the growth portfolio to replace money drawn down from the income wedge. By putting this portfolio strategy in place, the retiree experiences peace of mind that their income investments will have very little fluctuation due to market corrections, and they will have a growth portfolio in place, that over the long term will provide sufficient returns to fund their retirement lifestyle.

16. Harness the power of income splitting – For most people, during their working years, they could not income split with their spouse/partner – unless they were self-employed. However, when you retire, you're able to split income from defined benefit pension sources and starting at age 65, from income payments flowing from registered retirement income funds. In 2009, the federal government of the day introduced these new pension income splitting rules. Almost overnight, we saw clients dropping one full tax bracket. When conducting retirement income planning forecasts, it's critically important to model the effect of income splitting to generate the highest possible after-tax income through your retirement years. This is one area where it pays to get the advice of your financial planner. Your advisor can provide you with tax forecasts that allow you to maximize both income splitting and taking advantage of marginal tax rates that can shift over time.

17. It would seem that the pension income splitting rules have done away with the benefits attached to spousal RSP plans; however, that's not the case. Although it's correct that superannuation/defined-benefit pension plans can be split with the spouse as soon as the pension is received (for example at age 55), that's not the case with income flows from the registered retirement income fund (RRIF). In the case of a registered retirement income fund, the pension income splitting rules don't apply until age 65. As a result, spousal RSP's continue to play a vital income splitting role for anyone retiring between the age of 55 and 65 and has no defined benefit pension sources and desires to maximize income splitting opportunities with their spouse/partner.

18. Government benefits – Five years before retirement it's important you to get clear on your government benefits. For most people, they will receive the maximum benefit from old age security (OAS) payments. However, Canada Pension Plan benefits are different and are a function of your historical career earnings and contribution history. It's essential that you apply, before retirement, to obtain a quote for your forecasted CPP benefits when you retire. The earliest you can receive Canada pension plan benefits is age 60. However, you can defer taking Canada pension plan benefits until age 71. For every year you take Canada pension plan before the age of 65 you will be hit with a .6% per year penalty for each year you take the benefit early. So, if you began taking Canada pension plan at age 60, you would be slapped with a 36% reduction in your Canada pension plan. On the flip side, for every year you defer taking Canada pension plan after a 65, you will increase CPP benefits by .6% per year until age 71. At that point, you must take your benefits. The most significant take away is to make sure you confirm your projected benefits.

19. Investment management fees matter but not the way that you think – When it comes to retirement coaching, wealth planning or investment management services, fees are always an important consideration. However, when looking at fees, it's important to distinguish that there are two separate fee structures. First, there is the portion of the fee that goes directly to the investment products being used for the portfolio - mutual funds, ETF's (exchange-traded funds), and individual stock or bond purchases. Second, a portion of fees charged goes to the wealth advisor or financial planner. This fee is for such things as, financial planning, financial forecasting, tax planning, estate planning, retirement income planning, asset mix design, security recommendations, portfolio rebalancing, and behavioral coaching. Increasingly, study after study confirms the value of the second fee back to retirees and investors. One of the key benefits is the value attached to behavioral coaching. This will be discussed in more detail in the next point.

20. The value of behavioral coaching – You can't help but watch almost any sporting activity on TV without being assaulted by investment firms espousing the virtue of low-cost investment options for doing it yourself investors. What's ironic about this advertising is that even the largest manufacturer of passive and low-cost/do it yourself investments (Vanguard in the US) has concluded that their clients are better served when working with an advisor. Consistently, study after study confirms that its investment behavior that trashes or boosts performance more than any other factor. Temperamentally, the average investor does not act with discipline when it comes to capital markets, and they need a behavioral firewall between them and capital markets so they can experience the returns they are aspiring to. That firewall is a financial advisor. For example, in 2011, the investment funds Institute of Canada conducted a study that looked at the average stock fund return for Canadian investors from 1992 to 2011. The average stock fund return was 8.2% compounded annualized over that time. Over that same time, the average stock fund investor return was 3.5% per year. The difference was described as the investor behavioral penalty. In other words, investors were not acting with discipline to the fluctuation that took place through market cycles. They were selling when the markets were doing poorly and buying when the markets were doing well. This is a recipe for unsuccessful investing. In July 2010 Ipsos Reid conducted a study that looked at both advised and non-advised households. For those households that had an advisory relationship of 4 to 6 years, they had 2.81 times the investable assets when compared to non-advised households. For those families with advice relationships for 7 to 14 years it was 4.78 times the value, and for those households with advice for 15+ years, the value was 6.96 times the value of non-advised households. Behavioral coaching matters and is a critical component to not only investment success but long-term retirement income planning success.

21. Know your pension plan options – Over the years I've been surprised by the lack of understanding many people have had around their pension plan options. On the one hand, they take great encouragement from the fact that they have an employer-sponsored pension plan but often are somewhat cavalier and lack understanding around the mechanics of how the plan operates. When it comes to employer-sponsored pension plans, there are two main types of programs that are offered. These plans are referred to as defined benefit plans and defined contribution plans. Before you retire, it's critical that you understand what kind of employer-sponsored pension plan you're involved in (if you have one) and the mechanics of how your pension plan works.

22. Is your defined-benefit pension plan inflation-adjusted? – If you have an employer-sponsored pension plan that is of the defined-benefit variety, it's vital that you are clear on the cost of living adjustments on the pension. Over the years, I've found that pension plans sponsored by government agencies, crown corporations, municipal governments and large union organizations will typically have some form of cost-of-living adjustments on the pension. The formula attached to the cost of living adjustments can vary and it's important that you talk to your benefits administrators to understand how these cost-of-living adjustments are calculated. The assumptions behind the adjustment can then be worked into your retirement income plan.

23. If you are part of a defined contribution pension plan it's very important that you do your homework – A defined contribution pension plan is structured so that both the employee and the employer put a percentage of income into the pension plan. A common percentage is 5% of payroll contributed by the employee and matched by another 5% from the employer. These amounts go into the pension account and then need to be invested. Some plans hire independent investment managers to manage the accounts on behalf of the employee group, and no ongoing decisions need to be made by the employee. Increasingly, organizations are moving toward self-managed investment options. In other words, the employee is the one that takes responsibility for making investment choices. Not handled well, this can lead to disastrous results. In previous sections discussed in this tip sheet, we reviewed the role that investor psychology plays in successful investing. If your employer is not providing educational opportunities around how you should be

investing your money, it's vitally important that you take it upon yourself to improve your education in the area as well as working with a financial advisor that can provide you with assistance.

24. Before you retire, make sure your estate plan is updated – When we refer to the estate plan, it's about the following documents; an up-to-date will, powers of attorney for property and a living Will. Depending on your family circumstances, the will may also contain testamentary trusts. Although your estate plan is not directly related to the retirement income plan, it's an important peace of mind document to have in place when you retire. Often, when families begin planning their retirement, their attention is turned to questions about legacy planning. This will usually be the intersection point between the retirement income plan and the estate plan. As well, your will can provide an essential vehicle for protecting the hard-earned financial assets that you built up over a lifetime. Trusts can protect assets if your children go through marital separation or business insolvency. As well, trusts can be established to provide ongoing legacy payments and income support for grandchildren as well as charitable aspirations.

25. Your power of attorney document provides a voice for you when you can no longer act on your behalf – It's not a fun topic to think about, but incapacity can strike at a moment's notice due to stroke or car accidents, etc. That's why it's so important to have a power of attorney document in place. This document allows you to appoint a personal representative to make financial decisions on your behalf. Many people think that a spouse will automatically have powers of attorney on financial assets. That indeed is the case with jointly registered accounts and property assets. However, that does not apply to accounts that are simply registered in the individual's name. For example, if you have a tax-free savings account or a registered retirement income fund and have lost capacity, your spouse or partner does not automatically have the authority to make investment decisions on your account. They can only provide direction if you have given authorization through your power of attorney. The importance of the power of attorney document is even more pronounced when no surviving partner is around, and you are now relying on children, or family to make these decisions on your behalf. This is a relatively inexpensive legal document, so there's no excuse to not having it in place. Not having the document, can lead to long delays and expensive court costs to get the necessary powers for your family to act on your behalf.

26. Will you need life insurance when you retire – For most people, their need for life insurance, as it relates to providing income replacement for dependents, declines as they get closer to the retirement date. The general expectation is that by the time they reach retirement their increased financial assets, pensions, and reduced debt load means that the requirement for life insurance as a supplement is no longer needed. In general, I think this is true for most people. However, increasingly we are seeing retirees reaching retirement dates continuing to carry debt and fairly expensive lifestyle costs. As a result, there may, in fact, be a need to continue caring life insurance for the first several years retirement. This kind of question can be confirmed well in advance of the retirement date to make sure that you have the necessary coverage in place before retirement. If you delay this planning, life insurance can become cost prohibitive, or the individual may lose their insurability. The most common reason that people continue to carry life insurance into their retirement years is to create Legacy. The most common form of legacy insurance is Joint Last to Die Term to 100 coverage. This is a cost-effective way of providing a tax-free death benefit to the estate as a way of creating a legacy or additional liquidity that can look after tax costs that would be triggered in a last to die situation. Ideally, this kind of insurance coverage should be explored at least five years before retirement.

27. Know the difference between your investment risk temperament and the required returns to fund your retirement – As part of the investment planning process, it's common for your investment consultant to walk you through an exercise that helps to clarify your risk temperament when it comes to investing. In other words, how much year-by-year fluctuation are you willing to live with to obtain the desired return. It's a

truism that higher return portfolios expose investors to portfolios that have greater fluctuation. And of course, low return portfolios expose the investor to far less risk. You should never go through the exercise of confirming your risk temperament without addressing this question in the context of your overall retirement income plan and what your retirement goals are. For example, you may be of very conservative investor from a risk temperament standpoint. At a practical level, given the current level of interest rates, this would imply a portfolio strategy that barely beats the rate of inflation. Not a great strategy over the long term. When going through a retirement income planning forecast with your retirement coach, they may confirm that the required return is 2 to 3% above inflation. You now have a problem. Your comfort level is a portfolio that only provides returns at the rate of inflation, but your required portfolio returns are far above that. What do you do? Well, you have a range of options. If you don't want to take any additional risk and maintain a conservative portfolio position you may need to; backup your retirement date, save more money or reduce your expenditure goals. On the other hand, you could explore the idea of adding a little more short term risk to your portfolio to obtain the desired long term returns. Through a combination of financial education and ongoing coaching from your financial advisor, this may, in fact, be a very appropriate option to pursue. The main take away is you need to link your portfolio strategy and risk temperament directly to the retirement income plan. Once you do that, you will then be in a position to start making important trade-off decisions in the development of your plan.

28. Know the difference between retirement planning and retirement income planning – when you say the words "retirement planning", all kinds of topic areas come under this broad category. Such areas as; lifestyle, health, and longevity, cash flow planning, saving for retirement, investment vehicles and strategies, how much do I need to save each year, etc. Retirement income planning is a subset of the broad topic of retirement planning. Income planning deals specifically with such things as, the sustainable level of income, how to generate income, how the portfolio needs to be structured to produce income, the tax consequences of your income decisions, and the impact on your net worth based on spending trends, etc. Retirement income planning is critically important because it provides direction on a host of topics; return requirement, tax strategies, legacy strategies, sustainable cash flow, etc. Retirement Income Planning is a process that provides peace of mind, confidence and actionable strategies to put the retirement game plan in place. It takes the topic of retirement planning from the general to the very specific.

We hope that you have found this retirement tip sheet helpful. Have you ever considered a retirement coach? There are hundreds of strategies and numerous products and services that can potentially impact your retirement plan. Through experience and training, a retirement coach can quickly assess which strategies are relevant to your circumstances and enhance the probability that you will achieve your retirement goals. The coaching process is intended to help you clarify your goals and aspirations and to assess gaps or opportunities in your current planning. From opportunities, the coach will provide specific recommendations and strategies that will put you on the path to achieving your goals. The coach will then assist you with the implementation process, and on an ongoing basis, make sure that the plan is reviewed and updated. The updates take into account changes to your circumstances, changes to your goals and changes to legislation, products or economic environments that could impact the plan.

If you'd like to start a conversation on how our retirement income planning process could help you, don't hesitate to reach out to our office.

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