Money Makeover: These two look set, but are they set enough?

Rhea and Andrew look ready for retirement, but there are still a few doubts.

By: Deanne Gage Special to the Star, Published on Wed Jul 08 2015

The People
Rhea, a 53-year-old health care worker, and Andrew, a 61-year-old civil servant, plan to retire late next year. They are debt-free and, having amassed $1.5 million in Registered Retirement Savings Plans, Tax-Free Savings Accounts and non-registered investments, they possess more than enough assets to fund their retirement. On top of their savings, they have defined-benefit pension plans.

The Problem
The couple's advisor has told them they are more than well prepared financially, but Rhea worries whether their retirement nest egg can last up to four decades, especially since her pension isn't fully indexed to inflation and she is statistically likely to outlive Andrew.

Rhea and Andrew also don't understand how much they are paying in fees for their investment accounts. All their assets are with the same financial institution but they question whether they are getting good value.

Rhea says they pay 1.35 per cent to have funds invested in a professionally managed money program, but they still pay management expense ratios (MERs) on various mutual funds and exchange-traded funds they hold. Should they invest in more low-cost investments?

They are also torn over whether they should purchase joint, last-to-die life insurance to offset income tax that their estate may owe when they are both deceased. Their advisor suggested they consider buying a $250,000 insurance policy to preserve their estate. They would value a second opinion.

The Particulars
Rhea's pension: $4,000 a month, gross. When she turns 65, it reduces to $3,360 a month. Her pension is indexed annually by half of the rate of inflation.

Andrew's pension: $6,450 a month, gross. When he turns 65, it reduces to $5,350 a month. His pension is indexed annually by the average rate of inflation from the two previous years.

Assets
House: $370,000
RRSPs: $155,500
LIRA: $22,500
Non-registered investments: $736,500
Rhea's inheritance: $466,000
TFSAs: $92,000

Liabilities
None

The Plan
Some couples' worries about age difference and inflation derailing retirement plans are legitimate, but not in this case. "The excellent savings that they have accumulated, even without including Rhea's inheritance, will be more than enough to offset these factors," says Bruce Thompson, a certified financial planner with Money Coaches Canada in Regina. He assumed a two per cent inflation rate and that their funds need to last until Rhea is 90 and Andrew age 98.

Their overall asset mix across all account types is 14 per cent in cash, 37 per cent in fixed income and 49 per cent equities, an appropriate asset mix for them, Thompson says, considering their ages and close proximity to retirement.

Rhea and Andrew's understanding of what is included in the fees they pay (1.35 per cent, plus MERs on the mutual funds and ETFs) is correct, he adds.

But when Thompson calculated all the funds' MERs, he determined that Rhea and Andrew were paying 2.06 per cent in annual fees. "On a $1.5 million portfolio, that's more than $30,000 a year," he notes. "This is excessive, especially considering the size of their portfolio." No question, the couple's portfolio should be eligible for lower investment fees.

A handful of Canadian companies offer mutual funds that have solid performance histories and MERs in the 1.2 to 1.4 per cent range. But, if the couple goes this route, they shouldn't expect comprehensive advice with regards to insurance, tax, estate planning, retirement cash flow, and so on.

"But the $10,000 — at least — that they would save in the first year in management fees would easily pay the $3,500 to $4,500 that a fee-for-service financial planner would charge them to prepare a comprehensive financial plan that would address all of these planning topics," Thompson says.

The best value for Rhea and Andrew is to work with an unbiased financial planner who can recommend an appropriate investment service for them today, and, equally important, keep them informed about the ever-changing investment landscape and recommend product and service changes when it is to the couple's advantage, Thompson suggests. Any investment service can quietly evolve into something that is more profitable to the company providing it, at the expense of the investor.

"A planner would also provide them with an annual review of their plan, tax-efficient draw-down of their retirement assets, reassurance that they are still on track, and estate planning advice," he says.

As for buying the life insurance policy for estate reasons, Thompson says that there is a common emotional argument made for purchasing life insurance to prevent Canada Revenue Agency from being "the biggest beneficiary of your estate." What the couple needs to ask themselves is whether they want to leave a specific amount of money to their two adult daughters (i.e. $750,000 each) or if they are content to leave them whatever is left once creditors (including CRA) are paid. Rhea and Andrew preferred the latter option, since they say their daughters are already expected to inherit a decent amount of money.

"Without buying any insurance, they can already achieve their goal of leaving whatever is left over in their estate to their daughters," he says. "They do not need to consider purchasing life insurance to preserve their estate."