Nearing retirement, couple wonder how to make the most of post-work income

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With their working years tapering to a close, Melanie and Marcus have a clear goal.

"We want to maximize income so that we can live frugally but still be able to enjoy Toronto arts and culture," Melanie writes in an e-mail. She is 65 and working part-time in the health-care field while also collecting defined-benefit pension benefits. Marcus is 59 and self-employed. Together, they bring in about $108,550.

Melanie hopes to fully retire by next spring, while Marcus wants to keep working for another five years. They have a retirement spending target of $60,000 a year after tax.

Melanie wonders when she should begin drawing Canada Pension Plan benefits. Should she start now or defer taking CPP as long as possible so the benefit will be higher?

Should she continue to contribute to her registered retirement savings plan past the age of 65 if she is still working? She also wonders whether she should hang onto her mutual funds.

We asked Leslie Gardner, a financial planner at Money Coaches Canada, to look at Melanie and Marcus's situation.

What the expert says

Marcus's gross income averages $55,000 a year, while Melanie gets pension income of $16,915 and employment income of $33,952, Ms. Gardner notes. They own their condo outright and have some savings.

The planner recommends Melanie begin taking her CPP benefits now rather than waiting. Deferring the benefit until she retires next spring would not provide much of an increase. While Melanie has taken full advantage of her tax-free savings account, she has about $33,000 in unused RRSP contribution room. She wonders if she should continue to contribute to her RRSP.

"Based on her retirement spending needs, she does not need to continue to save," the planner says. When Melanie retires fully next spring, she will be in the same marginal tax bracket as she is now.

Marcus is a sole proprietor and does not have a pension plan now, Ms. Gardner notes. He has a defined contribution pension plan (a locked-in retirement account) from a previous employer. As well, he is contributing $400 a month to his RRSP, which will help offset some of his income tax. He could use any surplus money to begin contributing to a TFSA.

Based on her calculations, Ms. Gardner says Melanie and Marcus will achieve their retirement spending goal of $60,000 a year, adjusted for inflation, to the age of 95.

After they have both retired, they will get Melanie's pension of $16,915, plus their estimated combined CPP of $23,000 and combined Old Age Security of $14,040, for a total of $53,955 a year before taxes. The shortfall would come first from their non-registered savings and their TFSAs.

Shortly after Marcus retires, Melanie will have to convert her RRSP to a RRIF (registered retirement income fund) at the end of the year she turns 71. She would begin making mandatory minimum withdrawals, currently 5.4 per cent, the following year. She could choose to base the mandatory withdrawals on Marcus's age instead, lowering the withdrawal rate to 4 per cent.

Melanie has a bank savings account that is earning low interest, plus some mutual funds in her non-registered account. "These funds are not needed to fund their lifestyle until Marcus is completely retired in five years," Ms. Gardner says. "From a tax perspective, the savings account interest is 100 per cent taxable and therefore is earning less than the inflation rate," she adds.

She recommends the couple sit down with a professional and review their investments. "Based on their risk tolerance and investment knowledge, they may want to invest their savings account funds in a product that provides the potential for capital gains, which are taxed at a lower rate than interest," the planner says.

As for the mutual funds, Melanie can check her annual CRM2 statement (phase two of the client relationship model) to determine her money-weighted or "personal" rate of return. The money-weighted return includes the effects of deposits and withdrawals during the year, and so measures the actual return an investor receives. She can weigh this return against the fees she has paid. "This will help her to determine if she is getting good value for her investment," the planner says.

As well, Melanie should revisit her mix of stocks, bonds and term deposits to see whether they are suitable for a person who is about to retire, the planner says. She recommends the couple review their asset allocation annually and have a drawdown strategy in place, including pension income splitting when they both fully retire.

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The People: Melanie, 65, and Marcus, 59

The Problem: How to get the most out of their retirement income.

The Plan: Melanie takes CPP now. Review their investments. After they have both retired, they can supplement Melanie's pension and their government benefits with their savings.

The Payoff: Enough to maintain their lifestyle and enjoy what the city has to offer.

Monthly net income: $5,900

Assets: Her savings account $35,000; his savings account $16,000; her income fund $8,500; her TFSA $55,325; her RRSP $200,000 (mutual funds); his RRSP $176,000; his LIRA $102,310; estimated present value of her pension plan $570,770; residence $500,000. Total: $1,663,905.

Monthly outlays: Condo fee $412; property tax $200; property insurance $100; electricity $180; heating $85; maintenance, garden $220; car insurance $200; fuel $200; other transportation $145; groceries $350; child support $440; clothing $120; gifts $375; charity $40; vacation, travel $250; books, CDs $60; dining, drinks, entertainment $250; personal care $60; pets $60; subscriptions $50; health care $120; telecom, TV, Internet $170; RRSPs $600; TFSA $200. Total: $4,887.

Liabilities: None.