FINANCIAL FACELIFT

With their mortgage paid, how can Kent and Remy balance charitable gifts and retirement saving?

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Kent, 45, and Remy, 50, bring in a family income of $390,000 yearly, with Kent's salary making up more than $300,000.

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With their high family income and low housing costs, Kent and Remy have been giving generously to charity, donating about $50,000 a year over the past few years. Now that the mortgage is paid off on their $370,000 Alberta house, they aim to double their largesse.

Kent is 45 years old and Remy is 50. Their combined family income is $390,000 a year, with Kent's salary alone more than $300,000. When Kent retires in 15 years, he will be entitled to a generous defined-benefit pension – if he continues with the same employer and his salary rises as expected.

Their goal is to give $100,000 a year to charity starting this year, but they want to make the most of their giving. Because Kent is in the top tax bracket, they'll get back roughly half of what they give each year. They'd use the refund, plus another $50,000, to make the following year's donation, and so on.

Can Diego, 71, and Monique, 68, spend $130,000 a year in retirement and still give to charity?

"We are hoping one of your experts can help us figure out the right balance between donating each year and saving for retirement," Kent writes.

They plan to retire when Kent is 60 and Remy is 65 with a budget of $120,000 a year after tax, rising in line with inflation. Kent also asks about the best way to maximize the effect of their charitable donations.

We asked Jennifer Hughes, a certified financial planner with Modern Cents in Toronto, to look at Kent and Remy's situation. Modern Cents is an advice-only financial planning firm.

What the expert says

On the surface, Kent and Remy appear to be in excellent shape, Ms. Hughes says. "The main caveat is that much of their security depends on Kent continuing to accrue his generous defined-benefit pension and supplemental pension," the planner says. “If Kent were to leave or lose his job and his income fell, then making such large gifts could become challenging,” the planner says.

To illustrate, she tested a scenario where Kent’s pension accrual stops after this year. “They could still meet their retirement spending goal but they would end up with very little in liquid assets and no capacity for charitable giving.”

Kent and Remy have nearly maximized their registered accounts but hold little in non-registered savings, Ms. Hughes says. Their two children are in university with costs fully funded through a registered education savings plan.

The couple intend to help their children with down payments through First Home Savings Accounts up to the maximum of $40,000 each, or $80,000 in total. They have already contributed $16,000 to each account and plan to contribute another $8,000 for the next three years for each child.

Kent and Remy want the flexibility in retirement to relocate closer to their children, wherever they settle after they finish university. So the analysis assumes the purchase of a $1-million home in today’s dollars about the time they retire in 2040.

Now with $4-million, what’s the best way for Mike and Miriam to deal with their capital gains?

The planner looks at two scenarios: the first would see Kent and Remy continue their existing strategy to give $50,000 a year to charity up to the time they quit working. In retirement, Kent’s defined-benefit pensions, including the supplemental pension and their combined government benefits, are expected to cover their after-tax spending target, which will have risen to $164,000 a year in 15 years with inflation. The forecast assumes a 4.8-per-cent long-term rate of return on their investments and 2.1 per cent inflation. They’d leave an estate of about $6.8-million.

In the second scenario, they increase their giving to $100,000 a year starting this year. They would still leave a sizable estate, the planner says – about $4-million.

“Still, it is important to be mindful of potential ‘what-ifs’ – such as Kent’s taking a lower-paying job, his pension ceasing to accrue, or changes to his supplemental retirement plan," she says. "In these events, their retirement spending goals could still be met, but they would need to significantly reduce their charitable giving."

Worried about market turmoil, do Estelle, 62, and Blake, 54, need to work longer than planned?

To strengthen their retirement foundation, they should continue contributing the maximum to their registered accounts, including taking advantage of Remy's $31,000 of available tax-free savings account room, Ms. Hughes says. They should also begin building non-registered savings. "This could provide a buffer if circumstances change, while also creating additional tax-efficient options for giving."

Charitable contributions generate a non-refundable tax credit, which reduces taxes payable rather than lowering taxable income.

If a person claims more than $200 in charitable donations, the portion above $200 normally qualifies for a 29-per-cent federal tax credit. For people with high incomes, though, there's an added benefit: the portion of their donations that matches the amount of taxable income above the top federal tax bracket qualifies for a higher 33-per-cent credit instead, the planner says.

Alberta has a special 60-per-cent rate for donations of up to $200, so both spouses should claim the $200 credit. Kent should claim the remaining amount in his name alone.

"Looking ahead, he should monitor how much of their giving qualifies for the enhanced 33 per cent tax credit because both his income and the federal tax thresholds will change over time," the planner says.

Can Romesh, 54, and Gayle, 52, retire in a decade if they spend $125,000 on a basement renovation?

Currently, their donations come directly from cash flow; they do not have any sizeable non-registered savings for contingencies, the planner notes.

One option would be to donate up to the threshold that qualifies for the 33-per-cent federal credit, directing additional cash surpluses into a non-registered portfolio earmarked for future giving, Ms. Hughes says. This portfolio should focus on generating capital gains rather than income or dividends. The idea is to have stocks, mutual funds or exchange-traded funds that have risen in value since purchase.

"Under current rules, donating these securities directly to a registered charity eliminates the capital gains tax that would otherwise apply while still providing a donation receipt for the full market value," Ms. Hughes says. This would also give Kent and Remy extra retirement security and flexibility if they needed additional funds because of higher retirement expenses or a career change that could affect Kent's pension entitlements.

With $4.4-million, how should Omar and Tanya withdraw funds in retirement to pay less tax?

Another option is a donor-advised fund, or DAF, a charitable investment account that allows donors to contribute cash, securities, or other eligible assets and receive an immediate tax receipt, the planner says. The funds can then be invested tax-free and distributed to registered charities over time, allowing donors to plan their giving strategically.

"It is important to note that once funds are contributed to a donor-advised fund, they cannot be accessed for personal needs," Ms. Hughes says. A DAF would be particularly useful as Kent and Remy approach retirement, when some of the 'what-if' scenarios become clearer. "It would provide a reliable tool to plan, fund, and time charitable gifts throughout their retirement."

Client situation

The people: Kent, 45, Remy, 50, and their children, 18 and 20.

The problem: How much can they donate to charity without jeopardizing their standard of living?

The plan: Take full advantage of tax breaks on registered plans, including Remy's TFSA. Build up their non-registered savings for more flexibility in retirement. Consider opening a donor-advised fund.

The payoff: An outline of how to proceed in the most tax-efficient manner.

Monthly after-tax income: $21,510.

Assets: Bank $19,700; Kent's RRSP and locked-in retirement account $184,950; Kent's TFSA $158,200; Remy's RRSP $221,700; Remy's TFSA $126,000; registered education savings plan $36,700; house $368,500. Total: $1,115,750

Estimated present value of Kent's DB pension: $1.65-million and supplemental retirement plan: $580,000. That's based on a discount rate of 4.8 per cent and is what someone with no pension would have to save to generate the same income.

Monthly outlays: Property tax $300; water, sewer, garbage $150; home insurance $145; electricity $100; heating $300; maintenance $485; garden $60; transportation $500; groceries $940; clothing $275; gifts $470; charity $4,165; vacation, travel $2,170; dining, entertainment $1,125; personal care $355; club memberships $165; subscriptions $120; life insurance $22; health care insurance $465; phones, TV, internet $165; RRSPs $1,000; TFSAs $1,165; Kent's pension plan and SRP contributions $3,130. Total: $17,775. Surplus of $3,736 goes to saving.

Liabilities: None.

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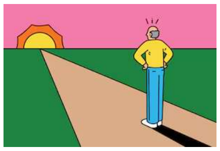

‘We’re in our mid-50s. Do we have enough money to retire comfortably in a decade?’

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How much can Halle and Hank, both 50, pay for their kids’ postgrad studies without risking their retirement?