FINANCIAL FACELIFT

Can Judy, 62, afford to join Charles, 64, in retirement this summer?

DIANNE MALEY
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Short term, Judy and Charles want to pay off a $15,000 line of credit and travel extensively 'in the early years of retirement,' Judy says.

SARAH PALMER/THE GLOBE AND MAIL

Charles and Judy are in their mid-60s with three adult children, all financially independent.

Charles has retired from his $80,000-a-year sales job and will soon begin collecting his defined benefit pension. Judy plans to join him this summer, leaving behind her $68,500-a-year administrative job. She has a defined contribution pension plan.

They have a mortgage-free house in a Southern Ontario city valued at $850,000.

Short term, they want to pay off a $15,000 line of credit and travel extensively "in the early years of retirement," Judy writes in an e-mail.

"Can I retire now with enough funds to reach age 90?" she asks. They are willing to sell their house "in the later years" if necessary to cover health care expenses.

Judy will have to move her group retirement savings plans when she leaves work and wonders how to manage them. "I would appreciate recommendations as to how and where to invest these funds to maximize success."

Their retirement spending goal is $76,000 a year after tax.

We asked Vikki Brown, a certified financial planner at Modern Cents, an advice-only financial planning firm, to look at Charles and Judy's situation.

What the Expert Says

Charles retired in 2023 at age 64 and chose to defer his defined benefit pension until he reaches 65 this summer, Ms. Brown says. Judy is hoping to join Charles in retirement at the end of July. To meet their lifestyle needs, Charles has been withdrawing $3,200 per month from his registered retirement savings plan (RRSP), providing him with after-tax income of $2,250 a month to augment Judy's salary.

Charles and Judy's primary concern is whether they will be able to meet their retirement lifestyle spending goal of $76,000 after-tax each year until Judy reaches age 90.

"This spending goal is higher than what they are currently spending, providing them with some flexibility," the planner says. This will allow for additional travel in their earlier years and could be used later for potential medical needs.

They are working hard on getting the line of credit paid off by making payments of $1,000 per month. The LOC is projected to be paid off in April, 2025. At that point they plan to direct the $1,000 and any surplus cash flow toward their tax-free savings accounts (TFSAs). They plan to use their TFSAs to save toward a new car purchase in the next four years or so, Ms. Brown says.

Judy has $36,370 in unused TFSA contribution room and Charles has $41,030. Charles and Judy plan to start taking Canada Pension Plan and Old Age Security benefits at age 65.

"However, they may want to consider deferring these pensions until age 70," the planner says. This would give them a greater guaranteed monthly income throughout their retirement and provide some longevity protection, she says. Delaying CPP until 70 would boost their lifetime benefits by 42 per cent. Similarly, OAS can be delayed and attracts a deferral bonus of 36 per cent at age 70.

Assuming they defer their benefits to age 70, they will have before-tax combined annual pension income, including Charles's DB pension, of $87,870 in today's dollars. Assuming a 15-per-cent average tax rate, that would give them $74,690 a year after tax. Charles's pension is estimated to pay $2,105 a month with a 75-per-cent survivor benefit.

"With pensions covering more than 95 per cent of their lifestyle spending needs, they are comfortably able to meet their $76,000 a year spending goal until Judy's age 90," the planner says. That assumes a 2.1-per-cent inflation rate.

The current market value of their portfolio is $733,600, which is more than enough to subsidize Charles's defined benefit pension until they reach 70, Ms. Brown says. Assuming an annual rate of return of 4.42 per cent net of fees, they are projected to have about $608,000 remaining in portfolio assets by Judy's age 70.

"Judy mentioned they would be willing to downsize their home in their later years to maintain their lifestyle," Ms. Brown says. "This should not be necessary but could be an option if they needed in-home care or a long-term care facility." Charles has been withdrawing from his RRSP and has 30 per cent taxes withheld at source, which is greater than what his actual tax rate will be this year, the planner says. Converting his RRSP to a registered retirement income fund (RRIF) would allow Charles to choose his withholding tax amount. “This would give them more money in their pocket each month.”

Judy will likely want to convert her defined contribution pension plan to a life income fund (LIF) this year with regular withdrawals starting in 2025. Like a RRIF, the LIF has a minimum amount that must be withdrawn each year. But it also has a maximum, making the LIF less flexible. “Because of this, it is recommended that Judy start drawing down on this account first and at the maximum level,” Ms. Brown says.

Judy will also need to convert one of her RRSPs to a RRIF this year to create more income to meet their spending goal. “Starting to withdraw from the registered accounts this year will help them get more money out at lower tax rates, before CPP and OAS start and push them into a higher tax bracket,” the planner says.

The registered account conversions can be accomplished when Judy moves the group accounts from the employer-sponsored plans.

Their other assets are being managed by an investment adviser within RRSPs. “Judy has expressed concern about the returns they have received working with this adviser and would like to explore other options,” Ms. Brown says. The managed accounts are invested in high-income mutual funds providing a 3-per-cent to 5-per-cent yield, after fees, with a portion of it being reinvested monthly. “I recommend they stop the reinvestments within the RRSPs to start building up the cash reserves needed for upcoming withdrawals.”

They could consider moving the accounts to a new investment adviser or investing on a robo-advisory platform, the planner says. A robo-adviser or online portfolio manager is a low-cost alternative that can be used to invest their money in one of the platform’s exchange-traded fund portfolios, Ms. Brown says. The investments are made based on a risk tolerance assessment. Additionally, the robo-adviser will rebalance the accounts for them, making it a low-maintenance option. “However, the lack of personal touch may be daunting to some investors, particularly when entering the retirement phase,” the planner says.

The People: Judy, 62, and Charles, 64.

The Problem: Can Judy join Charles in retirement this summer and meet their lifestyle goals until age 90?

The Plan: Judy retires as planned and begins drawing early on her registered plans. She might want to consider a robo-advisory firm when transferring her work savings plans.

The Payoff: A comfortable retirement.

Client Situation

Monthly Net Income: $6,333.

Assets: Home $850,000; cash $15,300; employee stock purchase plan $7,843; combined TFSAs $128,278; RRSPs $190,631; spousal RRSP $184,724; Judy's defined contribution pension plan $219,190; estimated value of Charles's defined benefit pension plan $434,414. Total: $2-million.

Monthly Outlays: Property tax $380; water, sewer and gas $240; home insurance $96; electricity $90; maintenance and garden $210; car insurance and fuel $328; groceries $1,000; clothing $150; vacation, gifts and misc. $1,600; dining, alcohol and entertainment $645; life insurance $65; cellphone, cable and subscriptions $286; line of credit $1,000; employer stock purchase plan contributions $285; RRSP contribution $400. Total: $6,775.

Liabilities: $15,000 line of credit at prime rate.

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