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Are Dylan and Darlene ready to take it easy and retire from the work force?

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With a house in the Toronto area and substantial savings, Dylan and Darlene are eager to retire from the work force.

"We're both turning 57 later this year and are thankfully in good health," Dylan writes in an e-mail. "I work full time in marketing (earning $184,000 a year) and my wife enjoys working part-time in the health and wellness industry ($5,000 to $10,000 a year)." Neither has a company pension.

They have two children in their 20s, the younger of whom is going back to university for a second degree. Their target budget in retirement is $105,000 a year after tax.

"I enjoy my work overall, but after 30-plus years, I'm ready to step back," Dylan writes. "I'd be happy to work part-time after retiring but would ideally do this as a paying hobby rather than as a financial necessity," he adds. Darlene plans to resume her work once pandemic restrictions have been completely lifted.

They want to stay in their home for the rest of their lives without touching the equity. The value of the house would be left to their children "and/or be an insurance policy in case we need money down the road," Dylan adds. They want to develop an investment plan – including revisions to the current asset mix – "to facilitate tax-efficient decumulation of

funds during retirement." They also wonder when to start collecting government benefits.

We asked Ian Calvert, a certified financial planner at HighView Financial Group in Toronto, to look at Dylan and Darlene's situation.

WHAT THE EXPERT SAYS

In the first stage of their retirement plan, Dylan and Darlene should try to keep their taxable income at about $50,000 each, Mr. Calvert says. "This would keep them both in a favourable tax bracket of 24.15 per cent, federal and provincial," he says. To achieve this, they could make $40,000 of taxable withdrawals each from their registered retirement savings plans. They could convert all or part of their RRSPs to registered retirement income funds.

Early RRIF conversions are not considered eligible pension income for the pension tax credit before the age of 65. So the main reason for the pre-65 RRIF conversion is the more withdrawal-friendly nature, particularly if they want monthly payments, Mr. Calvert says. "Many financial institutions charge an RRSP de-registration fee of $50 per withdrawal," the planner says. "Charged monthly for two individuals, this would be quite an unnecessary and avoidable cost." Once the RRSP is converted to a RRIF, it's important to remember there will be minimum withdrawals required each year, he notes.

In addition to the $80,000 in combined RRSP withdrawals, they will need to draw $38,000 from their non-registered portfolio, Mr. Calvert says. Their cash flow would then be $118,000,

with $80,000 taxable and $38,000 non-registered, less $13,000 in combined income taxes, for after-tax spending power of $105,000.

Once they begin collecting Canada Pension Plan and Old Age Security benefits, they could lower their RRSP/RRIF withdrawals back to the minimum amounts – a reduction of about $20,000 each – to maintain the same marginal tax bracket, the planner says. "Their highest RRSP/RRIF withdrawals should be in the years before they start CPP and OAS," he says.

Based on an assumed lifespan of 95, this forecast leaves them short of their goal of never having to tap their home equity. "At this rate of withdrawal, their total investment portfolio is expected to last until age 86," Mr. Calvert says. "To achieve their longevity goal, or if there are unforeseen costs in their retirement, it's likely they would have to unlock some of their home equity in the last phase of their retirement plan if they choose not to sell their primary residence." Alternatively, they could sell their home and downsize or rent.

Dylan and Darlene wonder whether to take CPP at 65 or defer it. "This is an important point for every retirement plan," he says. If they wait to the age of 70 to take CPP, their benefit would be 42 per cent higher than at 65. While this would be a considerable increase of a guaranteed income that will rise with inflation annually, it may not be the right move for Dylan and Darlene, the planner says.

"The decision of when to take CPP should be based on the personal cash flow and needs of each individual," Mr. Calvert says. Although Dylan and Darlene have assets to draw on in their early retirement years, "the withdrawal requirement from their portfolio between ages 57 and 70 would be too high for too long," the planner says. If they depleted their non-registered or tax-free savings account assets too early, they would be left with only taxable income from their RRIFs, leaving them with much less flexibility, he says. For example, the ability to make larger withdrawals would be challenging because every dollar would be taxable. Retaining a portion of assets that allow for a tax-free withdrawal later in life will protect them against unexpected financial events, he says. So for them, taking CPP and OAS at 65 would result in a slower up-front decrease in their assets, thereby enhancing their sustainability, the planner says.

Finally, Mr. Calvert looks at the couple's investments, which consist of individual stocks and exchange-traded funds. "Three blue-chip Canadian stocks represent about 15 per cent of the portfolio," he says. While their dividend yields are attractive, "the concentration risk is too high," the planner says. The same stocks turn up in one of the ETFs they hold – "their largest position, further concentrating their portfolio."

Mr. Calvert suggests they diversify into more non-Canadian stocks to gain exposure to a wider variety of industries. As well, he suggests they "clean up" the portfolio by selling some of their small, speculative positions "to ensure all securities are working to fund their retirement cash flow needs." Drawing up an investment policy statement would help keep their portfolio well organized and diversified.

CLIENT SITUATION

The people: Dylan and Darlene, both 56, and their two adult children

The problem: Can Dylan afford to retire soon and still leave the value of their home for their children? When should they take government benefits?

The plan: Go ahead and retire. Draw funds from their RRSPs in the early years, supplemented by money from their non-registered investments. Take CPP (and OAS) at 65.

The payoff: Awareness that they may have to tap the equity in their home in their later years.

Monthly net income: $12,335 (including tax refund)

Assets: Cash and short-term investments $147,000; his stocks $223,000; her stocks $114,000; his TFSA $94,000; her TFSA $109,000; his RRSP $600,000; her RRSP

$553,000; RESP $49,000; residence $1.6-million. Total: $3.5-million

Monthly outlays: Property tax $625; home insurance $170; utilities $475; maintenance, garden $350; car lease $1,000; other transportation $545; groceries $1,200; clothing $150; gifts $120; charity $400; vacation, travel $1,600; dining, drinks, entertainment $925; personal care $100; sports, hobbies $150; subscriptions $60; doctors, dentists $300; drugstore $100; health, dental insurance $200; life insurance $200; disability $500; communications $385; RRSPs $1,875; TFSAs $1,000. Total: $12,430

Liabilities: None

Ian Calvert is a Vice President & Principal at HighView Financial Group.