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With many 'little cash pots,' how should Arden, 65, and Trent, 59, set up for retirement in a few years?

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Arden and Trent moved to Canada from the United States in 2008. She is 65 years old, and he is 59.

"It took several years before we found our feet and I found regular, well-paid work with a good pension," Arden writes in an e-mail. Trent works part time as an instructor.

Arden works for the federal government, earning $95,000 a year. She'll be entitled to a defined benefit pension indexed to inflation. Trent earns about $39,000 a year in education.

They live in Quebec, where they rent an apartment. They have relatively modest savings except for an inheritance.

They are busy saving for Arden to retire a few years from now, followed by Trent in a decade, and would "love for someone to look at their agglomeration of little cash pots," Arden adds.

"But my main issue is that I received an inherited individual retirement account (IRA) from my father that I will need to wind up by 2031," Arden writes. "What I would like to do is repatriate this fund to Canada and would prefer to do it as soon as possible," Arden adds. The IRA has a value of about $306,000, but that's before accounting for the income tax.

Arden says she has contacted numerous cross-border wealth management firms to try to get some fee-for-service advice "but the big money boys are very uninterested."

Their retirement spending goal is $60,000 a year.

We asked Ian Calvert, a certified financial planner and portfolio manager, at HighView Financial Group in Oakville, Ont., to look at Arden and Trent's situation.

WHAT THE EXPERT SAYS

Trent and Arden are preparing for retirement, Arden in 2028 and Trent in 2035, Mr. Calvert says. They would like to travel and spend time with their family who live in the United States.

"They need a retirement cash flow plan that focuses on the tax-efficient withdrawal of funds, and most importantly, the longevity of their assets." Because Trent plans to keep working for several more years, "they have different timelines for how much more they can accumulate before retirement," the planner says.

With Trent's taxable income being $39,000, he is in the lowest combined marginal tax rate, Mr. Calvert says. "On his path to retirement, which is still 10 years away, he should focus on adding to his retirement savings," the planner says. "Even small amounts over time will be beneficial."

Given he is already in the lowest tax rate, contributions to his RRSP would be useful for accumulating retirement savings, but less valuable from a tax perspective," the planner says. "A better approach would be to focus on his TFSA, where he has lots of room available," he says. "Building up this account will provide tax-free capital to be used in retirement."

Arden has a defined benefit pension of about $25,000 a year, which is a critical component of their retirement plan, Mr. Calvert says. This, plus their government benefits and U.S. social security, will provide consistent and reliable cash flow in their retirement years.

But without any real estate, they need to ensure their retirement portfolio is properly managed to provide steady cash flow and longevity, the planner adds. "Without a future sale or house downsizing event, there isn't a tremendous amount of flexibility if either their expenses or investments are mismanaged."

They have retirement funds sitting in an inherited U.S. retirement savings plan, or IRA. They wonder if, and how, they should transfer this plan to Canada. "There are benefits to consolidation in Canada and having your retirement assets in one location," Mr. Calvert says.

However, the fact that it is an inherited IRA adds additional complexities and hurdles to moving it to Canada in a tax-efficient manner, the planner says. "This is a complex endeavour that needs to be executed very carefully to avoid adverse tax implications in both countries," Mr. Calvert says. "Working with a tax specialist who deals with cross-border transfer issues is a must."

Arden could start by working with an accounting firm that has expertise in this area. The person they deal with should be a chartered professional accountant (CPA) licensed in the United States as well as Canada who has experience with this very issue.

"Spending the time and money to get proper advice will prove to be a good return on investment," the planner says. "There are many things to consider; for example, specific rules for inheritance IRAs, Canada-U.S. Tax Treaty guidelines, taxation in both countries and rules governing distributions and withdrawals. Essentially, they need to review the cost and benefits of a lump- sum withdrawal compared with leaving the funds in the IRA and taking the distributions over time."

Managing this transfer appropriately should be their top priority as this account represents a substantial portion of their assets.

In their first phase of retirement, the years of 2028-2035, their cash flow should remain positive; however, there isn't much room for miscalculations, the planner says.

"For this retirement plan to function, it all comes down to their expenses and keeping them within the target range," Mr. Calvert says. If they can live off $5,000 per month after tax, their plan would remain workable. If their expenses turn out to be much higher, they would have to "encroach on their capital."

In 2029, they would have the following family income: Trent's estimated income of $42,000 a year; Arden's Canada Pension Plan benefit of $8,700 a year; Arden's Old Age Security of $5,800; Arden's U.S. Social Security of $12,000 and pension income of $25,200. This would be a total family income of about $94,000 a year, less $15,000 in taxes for after-tax cash flow of about $79,000 a year.

In 2035, when Trent retires, he will no longer have employment income, resulting in negative cash flow. When Trent starts his CPP, OAS, and Social Security, his combined income will be about $18,000 a year.

This plus Arden's combined income – projected to be $57,000 a year – gives them a total family income of $75,000 a year, less $13,000 for taxes. There is a cash-flow gap of about $6,000 if their goal is to be spending $68,000 a year. To fund this gap, they should withdraw from their RRSP/RRIF. As such withdrawals will be taxable income, they will need to take out between $9,000 and $10,000 to pay the additional tax and cover the $6,000 shortfall for after-tax spending.

"This would be a very manageable withdrawal from their savings, which should be funded by their RRSPs," Mr. Calvert says. "It's a healthy withdrawal rate from their assets, but they shouldn't take too many chances with the underlying portfolio holdings," he says.

"A balanced portfolio that can generate steady income in the form of dividends, interest and distributions would be a great place to start."

Aiming for a portfolio yield of 3 per cent to 4 per cent "would provide a lot of certainty and take some risk off the table." At this combined income level, "OAS clawback would likely never be a concern."

If they can achieve on average a 5 per cent rate of return, they should expect a stable and even growing portfolio even after withdrawals, the planner says.

CLIENT SITUATION

The person: Arden, 65, and Trent, 59.

The problem: How to move an inherited U.S. retirement account to Canada with the fewest tax consequences.

The plan: Consult an accounting firm with expertise in cross-border taxation and transfers.

The payoff: A clear view of the assets and income they will have to draw on after they are no longer working.

Monthly net income: $6,800.

Assets: Cash $2,500; inheritance (before tax) $305,950; other $500; her TFSA $16,000; his TFSA $2,000; her RRSP $67,200; his RRSP $11,100; her employer pension plan (group RRSP) $25,175; market value of his defined contribution pension $23,000. Total: $453,425.

Commuted value of her DB pension (provided by applicant) $519,000. This is what someone with no pension would have to save to generate the same income.

Monthly outlays: Rent $930; home insurance $35; electricity $90; garden $50; transportation $460; groceries $700; clothing $20; gifts, charity $260; vacation, travel $460; other discretionary $100; dining, drinks, entertainment $130; sports, hobbies, subscriptions $15; other personal $50; health care $50; life insurance $80; phones, TV, internet $230; RRSPs $1,000; TFSAs $780; her pension plan contributions $510. Total $5,950.

Liabilities: None.

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