

Reflections



Message from the Editor

Fall has arrived and the end of the year is fast approaching. In this edition, we bring you a topic that is very timely as we move towards a new year – TAXES. Malcolm Fletcher's article will provide you with great advice about how to save tax using RRSPs. It's all about when to contribute and when to withdraw.

We are also launching, in this edition, a special series that will run over the next six editions of Reflections. Based on extensive interviews, Jim Nininger, former CEO of the Conference Board of Canada, has identified six key lessons that emerged from his study of people who have experienced retirement. Here is an opportunity to learn from people who have already done it!

Nancy Conroy, Editor
(Nancy Conroy, President of The Conroy Group Inc. is creator of LifeScape, a web-based retirement planning tool.)

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The Experts Speak.....

RRSP Tax Strategies:

When to Contribute and
When to Withdraw

by Malcolm Fletcher

Registered Retirement Savings Plans (RRSPs) are a great way for most taxpayers to reduce the income tax payable during their lifetimes. But to maximize the tax benefits of RRSPs, be sure to consider the timing of your contributions and subsequent withdrawals from the plan.

To better appreciate how tax savings related to RRSPs can be maximized, recall that the Canadian income tax system is *progressive*. This means that those with higher incomes face higher tax rates than those in lower income brackets. Similarly, the tax savings that an RRSP contribution provides are bigger for a taxpayer in a higher income tax bracket. Therefore, it is important to think about your *marginal tax rate** when assessing the best year(s) to contribute or withdraw RRSP funds.

* *marginal tax rate: is the rate of tax that is paid on the next dollar of income (i.e. up until a higher tax bracket is reached)*

When federal and provincial income tax rates are combined, residents of most provinces face seven or more different tax brackets. For purposes of this discussion, consider the following tiers of income for residents of Ontario and Quebec:

1. Residents of both provinces pay no tax on the first \$8,000 of income earned;
2. From \$15,000 to \$28,000 of taxable income, an Ontario taxpayer faces a 22% *marginal tax rate* and a Quebec taxpayer a 29% rate.
3. From \$36,000 to \$56,000 of taxable income, the *marginal rates* are about 31% (ONT) and 38% (QC).
4. Rates increase again just before \$60,000, to 33% (ONT) and 42% (QC).

The Life of Joe

Joe is a student who earns \$8,000 as a lifeguard. When he files his income tax return, he will earn $18\% \times \$8,000 = \$1,440$ of space to contribute to an RRSP.

...continued on page 3



A New Series is Launched! Jim Nininger's Six Lessons

As the Editor of Reflections, I am very pleased to be launching this series of articles based on the research work of Jim Nininger, former CEO of the Conference Board of Canada. Beginning in this edition of Reflections and continuing for six more editions, we will be bringing to you the lessons that emerged from a unique Canadian study that explored the lessons real Canadians have learned about themselves as they think about, move into and through retirement. The author was motivated to undertake this study because of his own fears and concerns about moving into retirement. His exploration of the issue has resulted in a wealth of information and advice about modern retirement, a new career and lifestyle for Jim himself, and six invaluable lessons that we can all take advantage of in planning our own retirements.

Jim's Story

Jim's own retirement story begins in 2000. Jim had worked at the Conference Board of Canada for most of his career, first as a researcher and ultimately as the head of the organization. His own retirement was fast approaching and he was feeling apprehensive about it. In an interview with Jim, he said, "I really didn't know what I wanted to do" He found it difficult to picture what this next stage of his life would look like. He loved his job and really didn't want to retire. So.....he decided to ask a few other people about their feelings about retirement to see if he could gain a better understanding and put in place a sound plan. One person asked him "What are you passionate about?" and that question ultimately lead him to his study on retirement and a very keen interest in the whole issue of modern retirement.

Three years and many interviews later, Jim has produced several formal reports on the results of his

extensive interviews with more than 115 individuals from both the private and the public sector. These studies can be accessed online at http://www.myschool-monecole.gc.ca/executives_transition/index_e.html. It's interesting to note that Jim's six lessons emerged during a week's "holiday" that Jim took with his wife. With all the data from his extensive interviews in hand, he and his wife reviewed the stories and, after considerable debate, agreed that there were six key themes or lessons that cut across the experiences of the participants.

Lesson #1, *Retirement is a Journey, not a Destination*, represents one aspect of retirement that may have a big effect on how people adjust. According to Jim, if people "identify themselves with their work" or tend to "see retirement as a destination" they may have more difficulty than those who don't.

Furthermore, people who don't develop outside interests are more at risk. He knows about this first hand since he admits that he was a workaholic and didn't really have a lot of hobbies and interests outside of work. According to Jim, "if you aren't doing it now, you won't do it then". His Lesson #2 reflects this; it's *Get a Life while you are still working*. He knows about this one since he admits that he planned do a lot more reading when he retired but he still isn't because he is spending his time doing things he thinks are more important – volunteer work, sitting on two private sector boards, and travelling with his wife, to name a few.

Jim is convinced that it is very important for people to *Be Prepared for Leaving*, Lesson #3. His study, *Leaving Work: Managing One of Life's Pivotal Transitions*, undertaken his last year at the Conference

...continued on page 4

RRSP Tax Strategies ...cont'd from page 1

However, if he claims a deduction for an RRSP contribution when he has no tax payable, he will save no tax! Later in life when he withdraws funds, the amount he withdraws will be taxed as regular income, and assuming he has other income that exceeds \$8,000, he will end up paying tax on an amount he never saved tax on. This is terrible tax planning! If Joe still wants to contribute to an RRSP, he can do so, but simply carry the contribution forward to a future year for deduction purposes.

Let's assume that Joe gets a full time job in a few years and begins to earn \$25,000, so he is now in a 22% tax bracket. If he went ahead and contributed to his RRSP back when he was a student lifeguard, and didn't claim a deduction in that low-income year, he can claim the amount now and, since he's in a 22% tax bracket, save tax of 22 cents for each dollar that he deducts.

However, if he expects to earn \$40,000 in only a few years, he may be better to continue accumulating any RRSP contributions until he's in the higher tax bracket. In this way, he can look forward to saving tax of 31 cents per dollar of RRSP contribution deducted. It may not seem like a big difference, but it's 41% more than the 22 cents per dollar of tax saved when his earnings were \$25,000!

Fast forward to Joe's retirement income situation at age 65. If his base income is \$60,000 or more, each extra dollar of income he receives from an RRSP or RRIF will attract 33% to 42% of tax (depending on whether he lives in Ontario or Quebec). But it will also attract a 15% repayment of Old Age Security (this is known as the «OAS claw back»). To avoid this situation, it may be better for him to de-register his RRSPs before age 65, voluntarily pre-paying income tax that he could otherwise defer, but doing so willingly because he'd like to avoid the 15% surtax.

What about Me?

Like Joe, it is important for you to take into account your tax bracket when you are contributing to, seeking a deduction for, and withdrawing RRSPs or RRIFs. If you are not sure of the tax implications affecting your RRSP decisions, it can be useful to get professional help to ensure that you make the best choice.

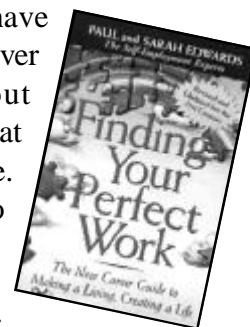
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Resources Reviewed

Finding Your Perfect Work: The New Career Guide to Making a Living, Creating a Life. 2003. Paul and Sarah Edwards.

Many individuals have worked for a living over many years without necessarily working at something they love. Perhaps you need to work in retirement to supplement pension income or perhaps you just want to continue to work when you retire. This book will provide you with tons of ideas about what the perfect work for you might be. The authors are experts in self-employment; if you are toying with the idea of working for yourself when you retire, then this is the book for you.



http://www.voyage.gc.ca/main/pubs/retirement_abroad-en.asp

Thinking of living abroad in retirement or perhaps you just plan to travel to foreign countries. This bilingual web site has excellent information on just about every country you can think of. It also has an excellent pdf document on retiring abroad.



Jim's Story ...cont'd from page 2

Board, served as his own transition to retirement from a fulltime career. This made his transition considerably easier than it might have been. Jim believes that it is important for individuals to take charge of their own retirement and for organizations to provide employees with the tools and information they need to manage the end of their career and the transition into retirement. Retirement planning courses, phased retirement, and sabbaticals during a career can be helpful benefits for employers to offer to employees.

Based on the study, Jim is a big proponent of people *Cutting Themselves Some Slack*, Lesson #4. Although in Year 1 he didn't really do this enough himself, many people he interviewed believed that taking a break upon retirement was very important to a smooth transition. It's a time to get more sleep, get healthy, and to discover all the opportunities presented by a more flexible schedule.

In shifting his priorities in retirement, Jim has been

influenced by Lesson #5, *Renew and Rediscover Relationships*. He sets aside a half day each week to spend with his grandchildren. Jim says that when he was working fulltime, he simply wouldn't have been able to do this. He and his wife have also agreed that they will take a number of trips each year at very specific times, like January. If Jim is approached to do any work during these periods, he just says no.

Retirement presents a wonderful opportunity for individuals to pursue their passions, to shift their priorities, and to devote more time to important relationships. Jim's last lesson, #6, is *Make the Most of This Phase*. Jim has passionately adopted this philosophy in living this phase of his own life and is living proof that living the lessons actually works!

Over the next six editions, we will be covering the six lessons. Stay tuned for Lesson 1 – Retirement is a Journey, not a Destination – in the February edition of Reflections!



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Upcoming Seminars

Upcoming Three Day English Seminars

2004: Oct 20-22 Nov 24-26 Dec 1-3
2005: Jan 12-14 Feb 16-18 Mar 16-18

Upcoming Two Day English Seminars for Executives

2004: Nov 8-9 (full) **Nov 22-23 (NEW)**
2005: **Jan 17-18 (NEW)** Feb 14-15

Contact the Retirement Planning Institute for more information on its pre-retirement planning seminars.