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## CANADIANS' ATTITUDES AND PERCEPTIONS ABOUT PLANNING FOR AND LIVING IN RETIREMENT

Fidelity Investments recently surveyed 1380 Canadians age 45 and over (median age 57), 47% of whom were retirees and 53% were pre-retirees. The survey, entitled "The Shift to Retirement Income – Beyond the Headlines", intended to find out Canadians' attitudes and perceptions about planning for and living in retirement.

The good news is that Fidelity's research shows that Canadian retirees and pre-retirees feel positive about retirement, considering it a time of "freedom", "enjoyment" and "fun". However, a sizeable proportion also associate retirement with financial stress.

On the positive side, many retirees have found the transition into retirement easier than expected. While 7% have seen their actual standard of living increase in retirement, 57% have maintained their standard of living and 40% have downsized.

The study showed that 50% of Canadians say they are on the right track when it comes to their investments, but 65% say they are concerned they may not reach their longer-term financial goals.

According to the Fidelity survey, "despite uneasy markets, the majority of Canadians who work with an advisor said they were confident in that advice – and



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"66% of pre-retirees expect to work in retirement." – Fidelity Investments Survey  
The Shift to Retirement Income – Beyond the Headlines

for retirees, the number has risen over the past three years.” Interestingly, the survey found that 66% of pre-retirees expect to work in retirement, while 51% think they would work as an employee and 28% thought that they may start a new business (some respondents indicated they would do both).

The top three reasons cited for working in retirement were: to stay mentally/physically active, financial reasons and to keep busy/help pass time.

The top three reasons cited for retiring were: health, job pressures and company being bought or getting packaged out.

While 51% of retirees said they retired earlier than planned, 42% said they retired about the time that they had planned to retire.

Given the fact that today many Canadians are retiring with a mortgage, it was interesting that 55% of the retirees said they are not likely to borrow against their home. However, 12% said that they have already sold their home or borrowed against it and 15% said that they are very or somewhat likely to use their home for future income.

While there is an assumption that people will sell their home to pay for their retirement, in fact many people end up staying in their homes or if they down size they end up buying a smaller property or condo that may be in the same price range as the home that they sold but located in a more expensive yet convenient location.

## Conclusions

The Fidelity survey suggests that Canadians should consider the following six points with regards to their retirement:

1. What do you want your retirement to look like? If you know what you want you're more likely to get it.
2. Make a written retirement plan. If you want to have control over how you live your later years, creating a written plan in advance will likely mean you have better options when you have to make choices about what you do and where you live.
3. Planning to work in retirement is not a retirement plan. Plan to work because it provides satisfaction, fulfillment and enjoyment – not because you need to.
4. Get good advice. Professional financial advice can improve your chances of having the retirement you want.
5. Don't assume your living expenses will be a lot lower in retirement. There may be things you spend more on, such as travel, entertainment, hobbies and health insurance.
6. A house is not a retirement savings account. Downsizing can be complicated and may not get you the financial results you want.

## BEAT ATTRIBUTION RULES WITH A TFSA

In an ideal world the spouse earning a high income should be able to give his earnings to the spouse with little or no income to invest so that the investment earnings could be taxed in the hands of the lower income spouse. Unfortunately current tax rules do not allow this. Attribution rules ensure that the earnings are attributed to the real income earner. Therefore, even if the money is invested by the lower income spouse, because it was earned by the higher income spouse it will be taxed as if it was earned by the higher income spouse.

While the pension income splitting rules that were recently introduced have created a reprieve for some retirees, the introduction of Tax Free Savings Accounts (TFSA) has offered another exception to the attribution rules.

An income earning spouse can now give the funds to a non-income earning spouse or relative to contribute to his/her TFSA, without needing to worry about the attribution rules.

Canadians over the age of 18 can contribute \$5000 per year to their TFSA. Since TFSAs were introduced in 2009, if you have not opened an account yet, you can contribute a maximum of \$20,000 in 2012.

The contribution room is indexed to the Consumer Price Index and is rounded out to the nearest \$500 increment so it is likely to increase to \$5,500 soon.

Since in a TFSA funds grow tax free and you can make tax free withdrawals as well, these types of accounts are not only useful for saving money for emergencies and short term needs but can be very useful for retirees as withdrawals will not affect any income tested government benefits they may be entitled to.

You can set up a self-directed TFSA and depending on your risk tolerance and time horizon invest your savings in a variety of instruments from stocks, bonds and mutual funds to GICs and high interest savings.

## PERMANENT INSURANCE POLICIES ARE A BARGAIN NOW

The last time that the exempt rules for life insurance policies were updated by the Department of Finance was more than 30 years ago. However, the 2012 Federal Budget includes a proposal to update the exempt rules and this means that permanent insurance policies can become more expensive as early as 2014.

The changes proposed in the 2012 Federal Budget are meant to ensure that the rules reflect increased longevity, low interest rates, and product innovations and are also more consistent with plans available in other countries.

## What Are the Implications for Insurance Policies?

The proposed changes will standardize mortality and interest rate assumptions used in permanent policies and this will result in lower accumulation room than what is currently available. As a result, quick-pay policies will likely lose their exempt status.

Corporate-owned insurance policies will be adversely effected too, since the new rules will affect the calculation of Net Cost of Pure Insurance (NCPI) and the Adjusted Cost Basis (ACB) calculation for policies.

This could mean that smaller loans will be available on a tax-free basis and less money will be credited to the capital dividend account (CDA) of a corporation. It is also likely that the level of investment income tax (IIT) could increase.

All in all these changes are likely to result in an increase in the price of insurance and a reduction in the amount of money that could grow on a tax sheltered basis in exempt policies and could therefore reduce the appeal of these type of policies as a long term investment option.

The Department of finance has suggested that the proposed rules take effect in 2014, therefore you should review your insurance portfolio and if permanent exempt insurance makes sense as part of your strategy then you should seriously consider purchasing your policy before 2014 to take advantage of the current provisions. When rules change existing policies will generally get grandfathered and the new regulations will only apply to new policies issued after the rules take effect.

## TAX-EFFICIENT INCOME

Taxes play a big role in determining your investment returns and you should always take taxes into account when choosing investments.

There are three types of income for tax purposes. Interest income, dividend income and capital gains income.

### Interest Income

GICs and bonds generate interest income which is considered ordinary income and is taxable at your marginal tax rate. Furthermore, it is taxable as it accrues, even if the interest compounds and you do not receive the income until the maturity of your GIC or bond. Currently the top marginal tax rate for ordinary income in Ontario is 46.4%.

### Dividend Income

Dividend income is more favourably taxed than ordinary income. Dividends have to be "grossed up" first but then you can claim a dividend tax credit against a portion of the resulting taxes. As a result the dividend tax rate for the highest marginal tax bracket in Ontario is 28.2%.

## Capital Gains

Capital gains is the increase in the value of your investments and is subject to tax when you sell your investments. You have to report 50% of your capital gains as ordinary income and pay taxes on it. Therefore the capital gains tax rate for the highest marginal tax bracket in Ontario is 23.21%.

### Series T Shares

Deferring taxes to a future date is always a good strategy. When you are accumulating funds, by investing in equities that generate capital gains vs. ordinary income, you can defer paying taxes until such time that you sell your investments and then pay tax on only 50% of the capital gains.

When you need income from your investments by investing in mutual funds that offer series T shares, you can defer paying taxes on your income. Series T shares are designed to provide monthly income at a specific rate. This rate is generally 5%, 6% or 8% of the net asset value per share on the last day of the previous calendar year. This distribution rate should not be confused with the fund's rate of return.

These distributions will be treated as return of capital which is not taxable. However, this will reduce the adjusted cost base (ACB) of your mutual funds. This means that when you sell your units in the future you will realize a larger capital gain or smaller capital loss.

### ABOUT THE EDITOR

Tina Tehranchian MA, CFP, CLU, CHFC, is a branch manager and senior financial planner with Assante Capital Management Ltd. Assante Wealth Management is one of Canada's largest wealth management companies, offering integrated financial solutions to create wealth and prosperity for you and your family. Our 800 advisors in 300 offices across Canada take pride in the exceptional service they offer to clients through trusted face-to-face relationships and a level of service excellence second to none. Money Matters is published as a special service for clients of Tina Tehranchian.

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