Don’t Wait For Pension Reform – Build Your Own!

Imagine having guaranteed income which lasts as long as you do. It never runs out. You can’t outlive it. You don’t have to worry about the markets or interest rates. Once the monthly payments start, they never stop – month after month after month.

Most Canadians enjoy this when they start receiving their Old Age Security payments at age 65 - a maximum of 524.23 per month.

Some Canadians will also receive monthly payments from the Canada Pension plan – a maximum of 960.00 per month.

Fewer Canadians will receive monthly payments from a Defined Benefit pension plan which are based on their average income and the length of time they have contributed to the pension plan.

Still fewer Canadians receive payments from annuities- monthly payments from an insurance company purchased with a lump sum of tax-paid or registered funds.

What all of these income streams have in common is worry free, secure payments for life.

Let’s examine the most uncommon life-time payment plan – the annuity. It once was a very popular choice for setting up retirement income. In fact, when the Registered Retirement Savings Plan (RRSP) was established, it was the only income option available. Later, the Registered Retirement Income Fund (RRIF) was offered and soon became the preferred option. Similarly, pension plans have changed from Defined Benefit to Defined Contribution. In both instances, the net effect has been a transfer of control and risk to the individual receiving the income. This transfer also represented a shift from interest – based to market-based investments.

Annuities are beginning to make a come-back because market-based investments have been less than stellar in the last decade and the baby boomers are worried about the risk of outliving their income as they start their retirement .There isn’t much sizzle in a plain annuity so a complicated hybrid model was introduced five years ago called Guaranteed Minimum Withdrawal Benefit plan which offered lifetime payments along with a market-based component, annual bonuses, triennial resets etc. Complicated or not, Canadians jumped all over this product by investing almost 20 billion dollars in the last 5 years.

However, a case can be made for using a basic annuity for part of your retirement income. Let’s look at the following example of **“Stacked Annuities”**: Brad is 55 years old and plans on retiring 10 years from now. He has already accumulated 300,000 in his RRSP plan but wants to establish another layer of guaranteed income to add to the CPP and OAS pensions. He is able to contribute 20,000 per year to his RRSP. Instead of adding his annual contributions to his existing RRSP plan he purchases a registered deferred annuity every year with payments beginning at age 65. In the first year he purchases a 10 year deferred annuity, in the second year he purchases a 9 year deferred annuity etc. The following table shows the amount of income purchased based on current annuity rates.(it should be noted that current annuity rates are at a historical low point and any increases in interest rates will increase the payments)

Year	Contribution	Life Annuity Income at age 65
1	20,000	150.31/month
2	20,000	146.11/month
3	20,000	142.05/month
4	20,000	138.12/month
5	20,000	136.92/month
6	20,000	138.89/month
7	20,000	139.25/month
8	20,000	135.68/month
9	20,000	129.28/month
10	20,000	123.42/month
Total	200,000	1380.03/month

1380.03/month registered annuity payments plus CPP and OAS benefits will all provide Brad with a guaranteed lifetime income. He will still have his RRSP which he can convert to a RRIF to produce flexible income to match his lifestyle. If he used 5000 of his tax refund from his 20,000 RRSP contributions to contribute to a Tax Free Savings Account, he will have additional tax sheltered funds to complement his income.

If you want your income to last as long as you do, see a retirement **spending** specialist!