Winding Down Your RRSP

Polson Bourbonniere FINANCIAL

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Choosing how to wind down your RRSP can be a complex task. There are as many different kinds of RRIFs and annuities as there are cars in your grocery store parking lot. Low interest rates, health, longevity, withdrawal rates -- not to mention the unusual market volatility of recent years – all impact your decision. But in these days, what financial matter isn't complex?

With this Guide to Your RRSP Maturity Options we want to make the job simpler. It will give you some ideas to get you thinking about what lies ahead well before you're forced to wind down your RRSP at age 71. And, by seeking advice from one of our CERTIFIED FINANCIAL PLANNERS® (CFP®) and Retirement Income Specialists, you'll be in a better position to make the choices that suit your needs.

We want you to have a Worry Free Retirement Experience™. How we do that is through a 6-step process that first identifies your needs and analyzes your existing sources of income, including pensions and investment income. From there, we build your personal Worry Free Retirement Income Plan, a blueprint to providing you with the cash flow that you need, while at the same time minimizing income tax and organizing your estate.

So, take some time to read through this Guide. Then call or e-mail us to arrange a mutually convenient appointment. We absorb the cost of our initial meeting. And, we'll make it worth your while!

RRIFs and Annuities

Let's get down to the serious business of winding down your RRSP. Think of RRIFs, LIFs, and annuities as pensions. While an actuary will tell you there are subtle distinctions, an annuity, RRIF or LIF simply pays you periodic income in retirement – just as a pension does.

You must wind down your RRSP by the end of the calendar year in which you turn age 71. But, you don't have to take income until the following year. All income is fully taxable as received, just like your pension income, or if you had withdrawn cash. There are a number of planning strategies that can help you minimize taxes, and while these are beyond the scope of this Guide, that's where one of our CFP®s will be of valuable assistance to you.

As you read on, we'll go into more detail on RRIFs and annuities individually.

Your Annuity Choices

An annuity is essentially the opposite of a mortgage. In the case of a mortgage, a financial institution provides you with a lump sum to buy your home and you repay them over a period of years, with interest. With an annuity, you provide the financial institution with a lump sum and it pays you back over a period of years – for your lifetime or to age 90 -- also with interest.

Term Certain Annuity to Age 90

Let's take a look at what is really the simplest annuity option for RRSP proceeds, the Term Certain Annuity to age 90 (TC90). Under the TC90 Annuity – also known as a fixed-term annuity to age 90 – income continues until your 90th year, and then ends.

Take the case of Tom, age 71, and his 65 year-old wife, Betty. Tom is winding down his RRSP and likes the idea of a guaranteed payout to age 90. He can choose either a 19-year or 25-year stream of payments. The income from the latter is smaller, but provides six more years of protection for Betty.

The table below shows the monthly income available in May 2014 from one major life insurance company for a $100,000 RRSP for various types of annuities for men and women aged sixty through 71. Look at the last column, "Term Certain to Age 90 – Male or Female. Since Tom is 71, the 19-year annuity would pay him $559.47 monthly. If he elects Betty's age 90, the 25-year annuity would pay him $463.35 monthly.

$100,000 Annuity (purchase ages 60 through 71)

	SINGLE LIFE		JOINT LIFE	TERM-CERTAIN
Purchase	10 Year Guarantee		10 Year Guarantee	To age 90
Age	Male	Female	Male & Female	Male & Female
60	$475.44	$447.92	$399.21	$449.98
61	$486.52	$457.18	$406.87	$463.38
62	$498.24	$466.98	$415.25	$472.15
63	$510.63	$477.35	$424.07	$481.64
64	$523.73	$488.31	$433.49	$491.84
65	$527.38	$489.55	$436.39	$503.13
66	$542.02	$501.85	$439.29	$515.34
67	$557.46	$514.85	$450.81	$528.69
68	$573.72	$528.61	$463.12	$543.35
69	$590.85	$543.16	$476.31	$559.49
70	$594.10	$543.42	$482.45	$577.35
71	$612.91	$559.72	$488.58	$593.00

The above table illustrates the monthly income from annuities that a $100,000 RRSP will provide at certain ages.

* All monthly incomes start one month after purchase date

Source: Manulife May 2014

If you are convinced you won't live beyond ninety, the term certain annuity may be for you. It provides a guaranteed payout regardless of market conditions, and no money management is required. Should you die prematurely, it will continue to your spouse until the end of the term, or if you are single, widowed, or divorced, it can be cashed in. On the flip side, as is the case with all annuities, the income payable is based on interest rates at the time the annuity is arranged, and it cannot be changed.

One important tip:

Annuity incomes vary with financial institutions so we survey the marketplace to ensure that you are getting a competitive payout from a reliable company.

Roughly 25% of all single men and women age 65 will live to age 90, but there is a 50% chance that one spouse of a couple age 65 will live to age 90. So before you settle on the TC90 annuity – or any other RRSP maturity option – consider your overall financial picture as well as your health.

Life Annuities

Over time, the life annuity has been much maligned and often misunderstood. Yet if you have a pension from your employer, it's a form of life annuity. Quite simply, the life annuity pays you an income that you cannot outlive – income lasts for your lifetime (a "single life" annuity), or for the joint lifetimes of you and your spouse should you elect to do so (a "joint & survivor" annuity).

Whether you live to age 80 or to age 105, a life annuity continues to pay. There is a common misconception that all life annuities stop on death – not necessarily so, although in its riskiest form that's the case. Known as a "straight-life" annuity, "life-only" annuity, or life annuity "with no guarantee", it's the kind that your Uncle Harry might have chosen from his company pension plan many years ago, and when he died three years later, left no income for Aunt Eleanor.

Fortunately, with qualified advice from a CERTIFIED FINANCIAL PLANNER® (CFP®) or Chartered Life Underwriter (CLU), few people choose this type of life annuity these days. In fact, most single or joint life annuities include a guaranteed minimum number of payments. Have a look under age 71 on the above Annuity Table for representative incomes at various ages.

Based on $100,000 from an RRSP, a male age 71 would receive a monthly income of approximately $646.55 (October 2011), assuming a Single Life annuity with a 10 year guarantee. (The corresponding income for a female age 71 would be $597.83 monthly -- lower because women of the same age are expected to live longer than men). This version of the single life annuity pays as long as the male is alive, but if he passes away before receiving 10 years of payments, the balance would continue to his spouse, or be paid out to other beneficiaries or his estate. If he dies after the 10 year guarantee period expires, the annuity would end.

"Guarantee" periods can range from 3 years to your age 90, but remember that the "life" annuity pays for your lifetime. The guarantee period is added to provide some form of residual benefit. The longer the guarantee period the lower the income received.

When a joint life annuity is arranged with RRSP proceeds, income simply continues as long as one spouse is alive. So, if Bob and Carol are both aged 71, and Bob decides to annuitize his $100,000 RRSP, he will receive approximately $518.74 (October 2011) as shown on the above table. Let's say that Bob lives for 8 years, and Carol survives him for another 12 years, income continues until Carol passes away. And, since they elected a 10-year guarantee, if both die before receiving a minimum of 10 years' payments, their beneficiaries or estate will benefit. Here again, the guarantee period can range from zero to age 90 of the youngest spouse. Think of the guarantee period as a warranty. It serves to ensure that some of your money ends up in the hands of your beneficiaries or estate, and doesn't go to the insurance company.

Variations on a Theme

When you bought your last car, you may have agonized over the many options available – colour, engine size, sunroof, and a host of other features. As you've read above, annuities, like cars, also come in a variety of models. What you should also be aware of is that they also come with several options to choose from.

While exploring all variations of annuities is beyond the scope of this article, you should know that the following are some of the more common ones that are available. Whether they fit in your particular situation is something that you'll need to assess based on your personal needs.

- indexed annuities that increase at a guaranteed rate or with the Consumer Price Index.
- Impaired annuities that factor in your reduced life expectancy if you have a serious health problem.
- Cash Refund annuities that return the unused portion of your original investment if you die before your capital is returned.
- Deferred annuities where your initial payment is postponed until the next calendar year.

View an annuity as a final decision. Once you have made your final decision there is no turning back. Annuity incomes are based on your age at the time of purchase, the insurance company's expenses, and long-term interest rates. They also vary from company to company at any one point in time. Not only should you advisor be able to give you advice on which option works best for you, he or she should also be able to shop the annuity market and deal with a range of companies.

RRIFs: The Basics

Let's take a look at the most popular RRSP maturity option in recent years, the Registered Retirement Income Fund (RRIF).

Surprisingly enough, the RRIF has been around since 1978, but didn't gain in popularity until 1986 when significant changes expanded its flexibility. Like an annuity, a RRIF is arranged with RRSP proceeds. Your RRSP can simply be converted to a RRIF at any time before the end of the calendar year of your 71st birthday. Existing assets in your RRSP can be moved into the RRIF, or you can take a different tack based on the requirement to make mandatory withdrawals each year.

The "RRIF Minimum Percentages" table below shows the percentage that you must withdraw from your RRIF each year, based on your age and RRIF value at December 31st of the previous year. For example, a 71-year old who has $100,000 in a RRIF on December 31st of this year, would have to withdraw a minimum of 7.38%, or $7,380, next year. Your payout can be structured at whatever frequency that you wish – monthly, quarterly, semi-annually, and annually – just as long as you take out at least the legislated minimum or more every year.

Age (yours or spouse's) at Jan. 1	Minimum % Factor	Age (yours or spouse's) at Jan. 1	Minimum % Factor
65	4.00%	80	8.75%
66	4.17%	81	8.99%
67	4.35%	82	9.27%
68	4.55%	83	9.58%
69	4.76%	84	9.93%
70	5.00%	85	10.33%
71	7.38%	86	10.97%
72	7.48%	87	11.33%
73	7.59%	88	11.96%
74	7.71%	89	12.71%
75	7.85%	90	13.62%
76	7.99%	91	14.73%
77	8.15%	92	16.12%
78	8.33%	93	17.92%
79	8.53%	94+	20.0%

Source: Canada Revenue Agency

The key feature of a RRIF is its flexibility. While all income received is 100% taxable, you do have the ability to increase your withdrawals from year-to-year, if needed. Secondly, and most importantly to the majority of retired Canadians, is that you have the ability to control your money by continuing to manage it. This brings about a whole range of factors that you need to consider when using a RRIF, not the least of which is the age-old choice between risk and guarantees. “Risk” means different things to each of us. For some, its’ market risk -- the volatility associated with equity markets, something that has been a fact of life in recent years. For others, it’s the “risk” of exhausting capital too soon – running out of money while still enjoying good health.

With a RRIF, your investment alternatives boil down to any authorized investments for RRSPs and RRIFs – the more common ones being stocks, bonds, GICs, money market instruments, mutual funds and exchange-traded funds (ETFs). The choices can be somewhat daunting, and require close attention to the nuances of structuring cash flow, and your overall income objectives.

Summary

So, when winding down your RRSP, whether you are considering an annuity, RRIF, or both, there is a need to have a Worry Free Retirement Income Plan, as well as a Worry Free Asset Allocation Plan -- money to meet your lifestyle needs, and an investment blueprint to ensure that you can sleep at night. Remember, there are enough things in life to worry about. Money doesn’t have to be one of them. Let us show you how. That’s why we developed the Worry Free Retirement Experience™

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