Budget 2007: Old age benefits

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Turning 60 just got a little easier. The 2007 Federal Budget rolled out three key tax measures that are designed to allow retirees to ease into retirement and lower their tax burden once they're finally out of the workforce.

The key changes mentioned in the budget include raising the age limit where Canadians have to convert their RRSP to a RRIF from 69 to 71, introducing the idea of phased-in retirement, and a $1,000 increase to the age credit to $5,066. But by far the most popular measure was pension splitting, which was first introduced in October and re-introduced in Monday's budget.

Of the nearly six million Canadians who are already over the age of 60, this demographic are more likely to take advantage of this relief, explains Peter Drake, president, economic and retirement research for Fidelity Investments. The reason, he continues, is because in large measure this is the group who lived more as a traditional family, where one spouse went out and earned a living while the other likely stayed home.

"That means there are a lot of people in retirement now where the two spouses have very distinct, unequal incomes," says Drake. In after-tax money, this measure could mean between $1,000 and $8,000 in savings, depending on the client's individual circumstances. Drake warns, however, that impact of this measure will wane in time as more dual income spouses enter retirement.

Another measure that is likely to resonate with those wanting to ease into retirement is the Conservatives' phased retirement plan. Under the proposal, older workers would be able to continue working on a part-time basis, while receiving a partial pension from their employer. At the same time, while they are working, they could accrue further pension benefits.

The idea is to allow workers to work part-time, but using the pension benefits to make up the drop in income from the reduced number of hours. As noted in the budget, "specifically, the new regulations will allow employers to offer qualifying employees up to 60% of their accrued defined benefit pension."

Given the number of tax measures that will impact the way Canadians use their pensions, it will become that much more important for advisors to make sure they take a holistic view of their clients' portfolios. "Every time I sit down and I create a financial plan for a client, you take a look at what kind of planning is in place, short term and long term and a pension plan, whether it be a money purchase or a defined benefit, is one of the key questions asked," says Al Nagy, a CFP with Investors Group in Edmonton. "That's very important to look at that as one of the main stages of financial planning."

The increase in the age to move RRSP to a RRIF to 71 from 69 so far has received mixed reviews. As Ernst & Young point out in an analysis paper, taxpayers currently are required to stop contributing to their RRSPs and start a withdrawal program, usually through a RRIF, by the end of the year in which they turn age 69.

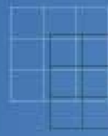
"Transition rules are also available for taxpayers who turn 70 and 71 in 2007 by allowing RRSP contributions for the 2007 and 2008 taxation year to the extent of their available deduction room," Ernst & Young notes in its budget brief. "In addition, these taxpayers can waive the minimum withdrawal requirement from their existing RRIFs for 2007 and 2008."

It's really incremental, coming at the end of the RRSP life, says Ian Russell, president of the Investment Industry Association of Canada.

Jacques F. Liwanpo, CA, CFP,

The Shops on Steeles & 404, 2900 Steeles Avenue E., Suite 207, Thornhill, Ontario. L3T 4X1

Phone: 905.881-6257 . Fax: 416.352.1501 . Email: jacques@liwanpo.com



"[The finance minister] is providing a little more relief on the RRSP front by enabling that additional three years to accumulate RRSPs," he says. "It's for people who may not have contributed as much as they should have through the working lifetime. It does provide some relief, but it is a gain on the margin."

Drake, however, thinks this measure has more potential, especially if used in concert with some of the other propels unveiled by Finance Minister Jim Flaherty on Monday. As Drake explains, the measure to give retirees an option to delay converting their RRSP to a RRIF could affect the way advisors help their clients prepare for retirement. If a client comes to an advisor and says they plan to work into retirement, depending on job security and the client's time horizon, that may mean that the portfolio might be able to be invested more aggressively it might have been if that person was in retirement starting to draw things down, he says.

"Typically we do like to suggest to our clients that they maintain their registered portfolios as long as possible because of the tax deferred nature," says Michael George, a CFP and director of wealth planning with Richardson Partners Financial in Winnipeg. If your clients don't need to draw out this fully taxed pension or need the income from a RRIF then it might help them avoid the OAS clawback. till, George feels the Conservatives missed a larger opportunity to really fix the tax system by failing to bring the tax brackets and tax rates up to where they should be given the inflationary periods that we've seen in the past.

One example, he says is RRSP limits. "I think even the RRSP limits that we've experienced in the past have not been sufficient for clients in order to fully fund retirement in that system."

Aside from the three tax measures clearly targeted at retirees, there were other gems that advisor think seniors might be able to take advantage of. While the new Registered Disability Savings Plan highlighted today doesn't have an obvious link to retirees, several advisors note that gives seniors another tool to help them ensure the financial well-being of their disabled children.

Up until now, the elderly have had limited options: insurance or setting money aside in a taxable account.

Changes to Registered Education Saving Plans, by eliminating the $4,000 annual maximum contribution level and increasing the maximum contribution to $50,000, could also be something seniors will want to take advantage of. As Graham McPhaden, a CFP with Quaile & Armstrong in Toronto notes, grandparents often make contributions to their grandchildren's RESP.

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Jacques F. Liwanpo, CA, CFP,
The Shops on Steeles & 404, 2900 Steeles Avenue E., Suite 207, Thornhill, Ontario. L3T 4X1

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