

# Retirement Top Up

## WHAT TO CONSIDER BEFORE RETIRING ON A PENSION



**“THE BAD NEWS IS** time flies. The good news is you’re the pilot.” That quote by time management guru Michael Altshuler keeps echoing in my mind as the prospect of retiring from my job looms in the not-so-distant future.

Until recently, I didn’t give much thought to retirement. I figured that after 20 years on the job my government pension plan would take care of me, more or less. I could look forward to a life of leisure with time to pursue all sorts of interests, from reading and travel, to gardening and golf.

Or can I?

With a mere six years to go to retirement I started wondering how practical my retirement goals are, and if I’ll be able to realize them with only my pension and modest savings. With that in mind, I started asking myself some hard questions, and then went in search of the answers:

### DO I HAVE ENOUGH INFORMATION TO RETIRE?

The answer to this was an unnerving ‘no’. As such, I visited my pension plan’s website and started rooting around for information, resources and publications. At the same time, I attended a pension information seminar to help fill in the blanks.

All the above was helpful, but I soon recognized I may not be able to retire on a pension as comfortably as I envisioned. As such, I sought the professional perspective of Spencer Pocock, Portfolio Manager at Odlum Brown Limited in Victoria.

### WHAT KIND OF PENSION DO I HAVE?

“People often don’t know what type of pension they have,” says Pocock. “All pensions — public or private — are regulated, but there are significant differences between plan types that people should understand.”

Pocock explained to me that there are generally two types of pension plan structures — defined benefit pensions and defined contribution plans.

# My job is to help you retire comfortably.

“Defined benefit pension plans are the gold standard, but are becoming less common because the employer is responsible for ensuring there is enough money in the plan to pay current and future pension liabilities to all plan members,” says Pocock. “Defined contribution plans are more common nowadays. With this type of plan pension contributions into the plan are defined, but the retirement income amount is not. Contributions are invested over time and the pension benefit at retirement is based on the assets and growth accumulated within the plan.”

## HOW IS MY PENSION CALCULATED?

I’m fortunate to have a defined benefit pension plan through my job with the B.C. Public Service. My employer promises to pay me an income for life during retirement. The payout is based on how many years I’ve worked, and how much I earned during that time, determined largely by my five highest income years.

If my pension was a defined contribution plan, however, my retirement income would be dependent upon the amounts my employer and I contributed over my working years, and the underlying portfolio returns over time.

## WHEN CAN I RETIRE?

Reaching pensionable age means you are entitled to a pension that is not reduced because of early retirement. Depending on the terms of your plan, pensionable age can be a specific age or a number of years of service, or a combination of both. It is the age at which you, as a member or former member, are entitled to receive an unreduced pension.

Early retirement certainly isn’t in the cards for me, but what about retiring once I am eligible for my full pension?

“You may be able to retire at your earliest unreduced date and collect a pension, but you may not be taking two vacations a year,” says Pocock. “Just because you can retire doesn’t necessarily

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mean you should. Retiring when you are still relatively young and able to work means lost income during your peak earning years — the years typically when debt is paid off and savings are being maximized. That’s potentially foregone money that could be saved to generate future income.”

### HOW LONG WILL MY PENSION LAST?

Generally, a defined benefit pension plan should continue paying out until the plan member (or their surviving spouse, depending on the pension option chosen) dies. A defined contribution plan, however, will only pay out until the assets are exhausted.

Most people take a conservative view of their pension plan, regarding it as a safety net managed by the plan’s administrators. Still, some people choose to trade in security for increased financial control.

“Even if a person has a defined benefit pension plan, under certain circumstances, they may choose to commute the cash value of the plan into a self-managed account rather than leaving it and taking a deferred pension,” says Pocock. “It’s a personal choice that works for some, but not for others.”

### WHAT HAPPENS IF I GET DIVORCED?

I’m happily married, and I hope it stays that way. That’s because “my” pension is not really mine at all. As it turns out, my pension is a family asset, just like our house and vehicle, which my darling husband may be entitled to a portion of should we ever part ways.

In fact, you need not even be married for your pension to be affected. Under B.C.’s Family Law Act people who live together in a marriage-like relationship for a continuous period of two years or more are considered to be spouses, and are therefore treated the same as married spouses for the purpose of dividing a pension.

Here’s hoping the romance lives on!

### WHAT HAPPENS IF I PREDECEASE MY SPOUSE?

Should I kick the bucket before my hubby, he will have to come to terms with my personal loss, but he may not have to deal with the loss of my pension.

“Your spouse will be entitled to the value of the pension benefit you earned up until your date of death,” notes Pocock. “Circumstances vary, but if you die before retiring, your spouse should be eligible to receive a pre-retirement death benefit. This may be in the form of a monthly pension or a lump-sum payment directly to their own RRSP or locked-in account. If you die after retiring, your spouse may continue to receive a monthly pension amount from your plan if you select a joint-life option upon retirement. Essentially, the larger the amount you opt to have continue to your surviving spouse, the less you will receive during your lifetime and vice versa.”

It’s not a one-way street, though. My husband works in the private sector and, though he doesn’t have a pension plan, he does significantly contribute to our household income, and he is saving for our retirement. Should he predecease me, both my life and lifestyle will be affected.

Which leads me to the next, and perhaps most important, question of all:

### HOW MUCH INCOME WILL I NEED TO RETIRE?

The answer to this question depends on what retirement looks like for each person. For some, retirement means living large; for others it is about living simply. Like most, I am somewhere in between — wanting a comfortable existence with the occasional extravagance now and again.

To be honest, I have no exact idea what it will cost to realize that from one month to the next.

“Most people neither know exactly how much they spend each month, nor how much they will need to live the lifestyle they want after they retire,” says Pocock. “To get a handle on this, I recommend clients have a financial plan prepared to help quantify and illustrate income needs in retirement, as well as where those needs will be funded from. You may think you have enough today, but there are a lot of variables to consider, and a plan helps uncover potential shortfalls or issues. A financial plan that incorporates information around pension statements and investments, as well as debts and monthly expenses will help provide clarity around a lot of unknowns.”

Then there is the matter of health concerns, which become all the more pressing with age. Most pension plans provide health benefits, but the extent of coverage varies from one plan to the next. And as unpleasant as it may be to consider, there are significant costs associated with long-term care.

“A lot of people don’t want to consider health issues until they have to,” says Pocock. “But you may need a way of replacing lost income if your spouse becomes ill, or dies, especially if you are relying on this income to fund part of your long-term plan.”

Something to also consider when nearing retirement are the costs of supporting family. As often as not, those nearing retirement are what Pocock refers to as the “sandwich generation” — those whose resources may be stretched as they concurrently support children and aging parents.

This brings me back to my original question: ‘How much will I need to retire?’

After going through the planning process there appears to be a sizeable gap between my monthly income needs in retirement and what my pension plan will deliver.

“When there are shortfalls between resources and income needs clients often have a few options they can consider,” says Pocock. “First, they can think about working longer and retiring later. Second, if possible, they can increase their regular savings amount to build their resources. Third, their investment portfolio can be rebalanced, adding more equity to try to enhance returns, but the risks have to be weighed. Lastly, they may need to re-evaluate how much they can spend during retirement to prolong the life of their resources, or simply spend less.” To that, he adds, “Only you know which of these is the right answer for you.”

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