GOOD LIVING: FINANCIAL PLANNING FOR THE HEALTHY, WEALTHY AND WISE.

Planning for the end of employment

Even the financially comfortable can benefit from foresight

When employment income stops, a material and emotional shift is required to begin living off investments and pensions. Even financially comfortable retirees need a clearer picture of what life after work will look like.

"For years, we're trained to save for the time we eventually retire," says Berkshire Securities Inc. investment advisor Heather Borrelli. "Suddenly the question is: have we put enough aside to afford to stop working? Unless we have the luxury of a defined benefit pension plan, retirement means we won't have a regular paycheque. Fewer and fewer Canadians are covered by defined benefit pension plans, so the issue of affordability must be carefully examined before taking that big step."

According to a 2005 Statistics Canada study, says Ms. Borrelli, over 8 per cent of retirees return to the workforce for financial reasons. "To ensure you're not among those who are forced to return to employment," she says, "don't wait until you're staring retirement in the face. Your advisor's job is to help you complete this analysis – and to raise the questions you need to ask yourself."

For a clearer picture of income and expenses in retirement, pre-retirees need to begin by focusing on expenses. "Identify how much you think you are currently spending, as a first step," says Ms. Borrelli. "Then put yourself through a reality check. For example, if you think that you spend $3,000 per month, and your annual after tax income is $50,000, this means you should be able to save $14,000 per year. Are you really adding this much to your savings on an annual basis? If your statements don't reflect this, you need to revisit your spending estimates."

Once pre-retirement expenses have been tested, it is important to be equally realistic about how they'll change in retirement. "One of the (traditional) rules of thumb is that expenses decrease by 25 per cent, but in reviewing the retirement experiences of my clients, I feel that's the farthest thing from the truth. Most of my clients are busier in retirement than ever, and spend more time enjoying their favourite hobbies and travelling."

Ms. Borrelli suggests erring on the side of caution. "There are always exceptions, but it is safer to assume that you will need sufficient sources of income to replace your paycheque. Furthermore, regular expenses like municipal and school taxes are constantly increasing, often faster than the overall cost of living."

Another consideration that's sometimes overlooked is the loss of employment benefits beyond the paycheque, such as health care and life insurance benefits. "It is important to clarify these details with your human resources department. The added cost of health care expenses, the expense of joining a private plan, and life insurance premiums may need to be included in the tabulation of expenses," she says.

The next step, of course, is to calculate your sources of income as well as the impact that taxes will have on your net income, something a financial advisor can help you explore in detail.

Another common retirement stage pitfall is the tendency to take on major expenses: with more time on their hands, many retirees decide it's time to buy an RV, remodel the cottage or kitchen, take an extended trip or start a business. But it is very important to make these decisions within the context of the overall financial plan, because any one of them has the potential to derail an otherwise solid retirement strategy.

"The best way to plan for any major project is to budget for it prior to retirement," says Ms. Borrelli. "Building contingencies for potential unexpected costs into your financial plan will help you with your decision process as well as indicate whether or not you can afford the extra expense. Major projects can take on a life of their own, and almost always cost more than anticipated. I have yet to hear about a renovation completed within the original budget or time frame."

All major plans can also benefit from a rigorous reality check. "One of my clients wanted to buy a RV for his retirement, but before making that financial commitment, I advised him to rent one for six months and try the lifestyle on for size. That trial period gave him and his wife a clear picture of the expenses involved in living this lifestyle as well as maintaining their vehicle. Four months into their experiment, they had blown their six-month budget and were ready to reconsider the original plan." ■

PHOTO: CHRISTINNE MUSCHI

Berkshire Securities Inc. investment advisors Heather Borrelli and Maggie Borowiec say that it's important for people approaching retirement to begin planning for the transition by making the distinction between the working years and the retirement phase. "Your needs will change and your financial plan should evolve to reflect that," says Ms. Borowiec.

Less room for mistakes makes planning critical

Conservative financial planning is critical in the retirement years simply because there is less room for mistakes.

"You don't have the luxury of time to make up for negative surprises. Making the distinction between the working years and the retirement phase is one of the greatest oversights in planning. Your needs will change and your financial plan should evolve to reflect that," says Berkshire Securities Inc. investment advisor Maggie Borowiec.

As an example of this premise in action, imagine two hypothetical investments: one has an average annual return of 6 per cent, the other 8 per cent. If the only other difference between the two is volatility, which one would you choose?

While the investment yielding 8 per cent seems like the obvious favourite, you might be surprised at the impact the additional volatility has on your portfolio. See the chart below for an illustration.

Ready, steady

Imagine a choice between two hypothetical investments: one has an average annual return of 6 per cent, the other 8 per cent. If the only other difference between the two is volatility, which one would you choose?

AN INVESTOR HAS $100,000 AND WITHDRAWS $5,000 AT THE END OF EACH YEAR

YEAR	INVESTMENT "A" RETURNS (average = 6%)	YEAR-END MARKET VALUES	INVESTMENT "B" RETURNS (average = 8%)	YEAR-END MARKET VALUES
1	6%	$101,000	-45%	$50,000
2	6%	$102,060	-11%	$39,500
3	6%	$103,184	7%	$37,265
4	6%	$104,375	65%	$56,487
5	6%	$105,637	70%	$91,028

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