# Income Solutions For Life

Canadians today are enjoying a healthier and more active retirement than their parents' generation. We are living longer than ever and, in some cases, may spend as much time in retirement as they did working. How you turn your savings into retirement income can have a significant impact on your retirement lifestyle. One of the biggest risks you'll face during this stage of your life is longevity risk - the risk you'll outlive your income.

## How can annuities help?

A life annuity can help to lessen your longevity risk by providing a guaranteed source of income for life. This income can be used to meet expenses or provide a strong foundation for your portfolio, freeing up the balance to be invested in the most efficient manner.

**What is an annuity?**

An annuity is like a mortgage payment that works in reverse. Instead of borrowing money, you invest money with a financial institution and in exchange you receive regular income payments - payments that contain both interest and principal. But unlike a mortgage that would typically end after a specific period, payments from an annuity can be guaranteed for the rest of your life.

## How else can annuities help?

Beyond providing guaranteed income for you for the rest of your life (or for you and your spouse's life) no matter how long you live, an annuity can also:

- Protect you against fluctuations in the market - you'll always know what your income will be no matter what the markets do
- Protect you against inflation - you can index your annuity so that your income increases each year by a set amount
- Provide a guaranteed stream of income for:
    - You and your spouse - your income can be based on two people's lives to guarantee income for your spouse after you're gone
    - You and your beneficiaries - payment guarantees ensure a specific amount is paid to you or your beneficiaries, no matter what happens
- Offer tax advantages - for non-registered funds, partial tax-deferral is available for your income. For clients over 65, the interest portion of your annuity income will generally qualify for the Pension Income Amount Tax Credit.

**Types of Annuities**

A **Single Life** annuity provides income for as long as the annuitant is living. A **Joint and Survivor Life** annuity provides income for the lifetimes of two people. A **Term Certain** annuity provides income for a specified period.

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## Annuity Pros and Cons

| Con | Pro |
|---|---|
| I lose control of my assets | ▪ You gain a guaranteed stream of income that will last your lifetime and won't be affected by market fluctuations<br>▪ You can simplify a part of your portfolio – a single lump sum investment can provide financial security without the need for ongoing investment decisions |
| My beneficiaries will get nothing from my annuity | ▪ A Joint and Survivor annuity will provide payments to the surviving spouse<br>▪ You can choose from several payment guarantee options that can ensure income will continue to your spouse or other designated beneficiaries<br>▪ The cash refund option will provide a lump sum payment to your beneficiary that is equal to the difference between your original investment and income you have already received<br>▪ The installment refund option will continue payments to your beneficiary until the total amount of payments equals your original premium<br>▪ Back up your initial deposit with life insurance, if you can qualify |
| My annuity income won't keep up with inflation | ▪ You can index your annuity so your income increases each year |
| Interest rates are low right now and I'll get locked into low income payments | ▪ Annuities generate a consistent income for the length of the portfolio owner's life that may be more difficult to achieve with other investment options<br>▪ An annuity payment may appear moderate now but as it continues, steadily, year in, year out, regardless of market fluctuations, the total amount paid to you will add up and generate an attractive return on your initial purchase. For example, a 65-year-old-male who purchases a $100,000 single life annuity can expect to receive approximately $176,400 in payments before he dies at age 90, providing him with an annual return of 7.06%*<br>▪ You don't have to annuitize your whole portfolio or a large part of it now. Annuitize a small portion of your portfolio now to guarantee some income and consider annuitizing more of it later if the rates become more attractive |

## How much should I annuitize?

The answer to "how much" you should annuitize depends on your income needs and your resources. To help you with this decision you could prepare a cash flow analysis (your advisor can help you with this) to determine what you think your expenses will be and what sources of income you have to meet those expenses.

Break your expenses into "essential" living expenses such as housing, food and medical and "lifestyle" expenses such as vacations or hobbies. You should then consider matching your essential expenses with income that is guaranteed for life such as the Canada Pension or Old Age Security and matching your lifestyle expenses with your sources of income from your managed investments. This way you can ensure your critical expenses are always covered leaving you with more flexibility for the balance of your income sources.

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## Cash Flow Analysis

**Expenses**

| *Essential expenses per month* | *Lifestyle expenses per month* |
|---|---|
| Housing - Rent | Clothing |
| Utilities | Entertainment |
| Health Insurance | Travel/Vacation |
| Other | Other |
| **Total monthly essential expenses** | **Total monthly lifestyle expenses** |

**Sources of Income**

| *Monthly income guaranteed for life* | *Income from other investments* |
|---|---|
| CPP | RRSP |
| OAS | LIRA |
| Employer Defined Benefit Pension | Employer Defined Contribution Pension |
| | Non-registered investments |
| **Total guaranteed income** | **Total non-guaranteed investments** |

After matching your expenses to your income you may have income left over that you could spend or perhaps reinvest. However, if you find a gap, you may need to consider reducing your expenses or increasing your income. If the gap is between your "guaranteed" income and your essential expenses or you are concerned your income won't keep up with your expenses, you might want to consider an annuity.

## Balancing Your Portfolio

An annuity can help you build a well-balanced retirement income portfolio. With your essential expenses looked after, you may feel more comfortable increasing your exposure to the financial markets to try to achieve addition gains.

## When should I annuitize?

You should purchase an annuity whenever you need it to meet your needs. If your primary concern is income, you should consider purchasing an annuity when you retire. If maximizing your return on your investment is key and you feel you can afford to wait, consider waiting until you are older to annuitize. The older you are when you buy an annuity the higher the income you will receive.

*Calculations as of February 2007 for a non-registered, single life annuity with a 10-year guarantee period.



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