

A Financial Planning Perspective on Employer Sponsored Capital Accumulation Plans

Presented by: Barry Laberge CFP
Selectpath Benefits & Financial

The RIGHT Path™

May 24, 2005



CAP Responsibilities

- Plan Sponsor
- Plan Advisor
- Financial Institution
- Plan Member



The RIGHT Path™

May 24, 2005



Meeting Topics

Financial Planning and CAPs



- Importance of Plan Design
- Financial Education and Advice
- Sponsor Tools-Plan Oversight
- Member Tools-Financial Planning
- Creating Income from a Capital Accumulation Plan
- Plan Member Communication

The RIGHT Path™

May 24, 2005



The Importance of Plan Design

Plan Design impacts how the member values the Plan, how they use it, and their eventual retirement income

Plan Types: DCP, RRSP, DPSP

Rules: Contribution formula, eligibility, withdrawals

The RIGHT Path™

May 24, 2005



The Importance of Plan Design

Investment Selection

- How Many?
- What type?
- Periodic reviews of Plan Member choices

The RIGHT Path™

May 24, 2005



Plan Oversight-Sponsor Reports

1. Employee Data and Demographic Reports
2. Plan Investment Reports

Education and Advice

- Identifying the Plan Members who may require attention

Best Practices – Good Governance

- Documentation of Periodic Reviews
- Documentation of Education Strategies

The RIGHT Path™

May 24, 2005



Plan Oversight-Member Reports

Employee Data and Demographic Reports

Administration – missing enrollments, member withdrawals, terminated members. Who is on the plan? Who is not?

Education and Advice

- Members nearing retirement
- New members
- Age banding
- Individual member balance and demographic reports



The RIGHT Path™

May 24, 2005



Plan Oversight- Investment Reports

Investment Reports



Asset Mix and Fund Selection

- Low interest rate investment

(Funds in daily interest, money market, short term vs. long term G C's, maturing G C's)

The RIGHT Path™

May 24, 2005



Plan Oversight- Investment Reports

Investment Reports

Asset Mix and Fund Selection

- Plan Level Breakdown by Fund Type (Fixed Income, Balanced, Asset Allocation, Lifecycle, Equity)
- Direction of new contributions
- Plan Performance

The RIGHT Path™

May 24, 2005



Sponsor Reports: Education and Advice

Financial Planning Considerations

Investor Suitability

- Basic tenant of securities regulation: Know your Client (KYC)
- Age and risk tolerance determine the asset mix decision

Investment risk and the objective of a Retirement plan

For many plan members, the fear of short term loss leads to more conservative Fixed Income investments. The longer term risk could be a lack of growth and a resulting insufficient retirement income

The RIGHT Path™

May 24, 2005



Member Financial Planning Tools

Asset Allocation questionnaire

1. How old age are you? When do you plan to retire?

2. What kind of investor are you?

- Conservative, Moderate, Aggressive



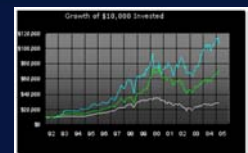
The RIGHT Path™

May 24, 2005



Plan Oversight-Investment Selection

1. Provider Investment manager reviews
2. Fund performance
3. Investment choice
4. Investment fees and expenses



The RIGHT Path™

May 24, 2005



Financial Planning Considerations

1. Creating Income from a Capital Accumulation Plan



Financial Planning Considerations

1. Plan Type – DCPP vs. RRSP and DPSP
 - Locked in versus non Locked in Funds
 Should a Capital Accumulation Plan have Defined Benefit Pension Plan restrictions?
2. Will there be sufficient capital to create income for life?
3. The Tax Incentive to Save for retirement

Financial Planning: Am I Saving Enough?

Am I saving enough?

- 6 to 10% of income is suggested (E/R and E/E)
- Comparison to CPP
- Contribution Formula-9.8% of \$37,500
- CPP Premium (E/R and E/E) - \$3,772 in 2005
- Income replacement ratio – 25% of insurable earnings



Financial Planning Considerations-How Much Should I Save for Retirement?

Money Purchase Plans Versus Defined Benefit Plans

Example:

- Ontario Municipal Employee Retirement Systems (OMERS) is a Multi-employer Defined Benefit Plan with 355,000 members
- Employee Contributions to the Plan:
 - 6% of \$41,100
 - 8.8% on earnings above \$41,100

Financial Planning: Am I saving enough?

Financial Planning Risks

1. Depletion of Capital
2. Inflation

How Long Should I Plan For? Will I Run Out of Money?

Conditional Probability of Survival at Age 65

To Age:	Female	Male
70	93.9%	92.2%
75	85.0%	81.3%
80	72.3%	65.9%
85	55.8%	45.5%
90	34.8%	23.7%
95	15.6%	7.7%
100	5.0%	1.4%

Source: Society of Actuaries RP-2000 Table with full projection.

Depletion of Capital- Living Too Long Retired Couples

ifid

A Couple Aged 65....Survival:

To Age:	At Least One...
70	99.5%
75	97.2%
80	90.6%
85	75.9%
90	50.3%
95	22.1%

Source: Society of Actuaries RP-2000 Table (with full projection)

13

Copyright © 2005 The BTD Centre

The RIGHT Path™

May 24, 2005



Financial Planning: Inflation Risk

ifid

Inflation: What Does a \$1,000 Payment, Really Buy You?

Years in Future	Realized inflation rate during each year....						
	0%	1%	2%	4%	6%	8%	10%
1	\$1,000	\$990	\$980	\$962	\$943	\$926	\$909
5	\$1,000	\$952	\$906	\$822	\$747	\$681	\$621
10	\$1,000	\$905	\$820	\$676	\$558	\$463	\$386
15	\$1,000	\$861	\$743	\$555	\$417	\$315	\$239
20	\$1,000	\$820	\$673	\$456	\$312	\$215	\$149
25	\$1,000	\$780	\$610	\$375	\$233	\$146	\$92
30	\$1,000	\$742	\$552	\$308	\$174	\$99	\$57
35	\$1,000	\$706	\$500	\$253	\$130	\$68	\$36

18

Copyright © 2005 The BTD Centre

The RIGHT Path™

May 24, 2005



The Tax Incentive to Save Marginal Tax 2005

Taxable Income Threshold	Combined Rate (includes Ontario surtax)
\$0 - \$35,595	22.05%
\$35,595 - \$71,190	31.15%
\$71,190 - \$115,739	43.41%
>\$115,739	46.41%

The RIGHT Path™

May 24, 2005



Financial Planning: Retirement Income GAP's

Retirement Income Goal
 - Projected Retirement Income
 = Retirement Income GAP



The RIGHT Path™

May 24, 2005



Achieving Financial Security- Retirement Income GAPS

	Retire at age 60	Retire at Age 65
Old Age Security	Nil	5,661
Canada Pension Plan	6,730	9,615
RPP (DC or DB)	??	??
Employer Savings Plan	??	??
Personal Investments	??	??
Total Retirement Income	??	??

Most Capital Accumulation Plan Members do not know what their retirement income will be

The RIGHT Path™

May 24, 2005



Planning for Retirement Income

Let's look at three CAP members

1. Thirty year old who saves 6% of future income
2. Forty five year old who has no other Retirement Assets and joins CAP
3. Forty five year old with \$50,000 in CAP and saves 6% of future income



The RIGHT Path™

May 24, 2005



Example – Three Members

Common variables:

- Current Income: \$40,000
- Retirement age: 65
- Inflation: 2%
- Rate of return: 5%
- Maximum CPP and OAS



The RIGHT Path™

May 24, 2005



Examples – Three Members

Retirement Income Goal:

(CAP, OAS, CPP)

- 70% replacement ratio
- \$27,600 (today's dollars)



The RIGHT Path™

May 24, 2005



Member Financial Planning Tools- Planning for Retirement Income

By using financial planning software CAP members can project their estimated retirement income.



The RIGHT Path™

May 24, 2005



Example #1: The Thirty Year Old – How much do I need to save?

Current Income: \$40,000

Current investments: nil

Retirement Income Goal:

Replacement Ratio: 60 to 70% of final earnings

Income objective: \$24K to \$28K



1. How much do I need to save per year?
2. How much capital do I need to have?

The RIGHT Path™

May 24, 2005



The Thirty Year Old – How much to save? What will I have in the future?

Results (using Financial Planning Software) Retirement Income Goals

Replacement Ratio- 69%

Income: \$27,600

Current investments: nil

Amount to save for retirement to meet income objective:

- 6% of income, or,
- \$2,400 per year, increasing with inflation

	Today's Dollars	Future Dollars
Projected Assets at Retirement age 65	\$155,000	\$311,000

The RIGHT Path™

May 24, 2005



Income Assumptions

Capital of \$155,000 is converted to a lifetime annuity

- Annuity interest rate assumed is 5.5%
- Income is level and paid for life
- Other income options available
- Life Income Funds (Locked in Funds)
- Registered Retirement Income Funds

The RIGHT Path™

May 24, 2005



Example #1 - The Thirty Year Old Sources of Retirement Income

Income In Today's Dollars	Retire at Age 65	Breakdown by source
OAS	5,661	20%
CPP (max)	9,615	35%
Employer RRSP	12,332	45%
Total Income	27,608	100%

- The Thirty year old who saves 6% of his income accumulates about \$150,000 at age 65
- \$150,000 creates \$1,000 per month of lifetime retirement income (in today's dollars)

The RIGHT Path™

May 24, 2005



Example 2 - The Forty Five Year Old

Retirement Income Goal :

Replacement Ratio: 69% of final earnings

Income objective: \$27,600

Existing Investments: *nil*

Amount to save for retirement to meet income objective

- 14% of income or,
- \$5,700 per year, increasing with inflation

To create the same retirement income as the person who starts at age 30, the forty-five year old needs to save 2.4 times more per year.

The RIGHT Path™

May 24, 2005



Example 3 - The Forty Five Year Old

Retirement Income Goal

Replacement Ratio: 69% of final earnings

Income objective: \$27,600

Current investments: \$50,000

Amount to save for retirement to meet income objective

- 6% of income
- \$2,400 per year, increasing with inflation

- The forty-five years old who starts with \$50,000 and saves 6% of future income accumulates \$150,000 at age 65.
- \$150,000 creates \$1,000 per month of lifetime retirement income (in today's dollars)

The RIGHT Path™

May 24, 2005



Communication Strategies

1. The Merits of a Capital Accumulation Plan
2. Plan Member Responsibilities as outlined in CAP Guidelines

The RIGHT Path™

May 24, 2005



Communicating the Merits of a Capital Accumulation Plan

Why participate in an Employer Sponsored Plan?

Income Tax Savings:

Reduce income tax payable now; earn tax sheltered growth; withdraw funds when in a lower tax bracket.

Immediate Tax Savings:

Employer can withhold less tax when there is a CAP contribution. There is no need to wait for a tax refund. Compounding starts immediately.

The RIGHT Path™

May 24, 2005



Communicating the Merits of a Capital Accumulation Plan

The Convenience of Payroll Deduction

- Saving money can be a challenge. A payroll deduction makes it easy and affordable.
- Let's say a person contributed \$75 per pay (\$2,000 per year) to their Employer Sponsored Group RRSP. For a person in a 33% marginal tax bracket, the "after tax cost" is only \$50 per pay.

The Advantage of Early Investing

- Starting early and staying invested are the first steps towards building a retirement "nest egg". The magic of compound interest takes care of the rest.

Sources of Retirement Income

- Government pensions provide the first \$6,000 to \$15,000. A registered savings plan adds the next layer of income.

The RIGHT Path™

May 24, 2005



Communicating the Merits of a Capital Accumulation Plan

Financial Planning Strategies

A Registered Savings Plan is a financial planning tool that has changing uses throughout a person's lifetime.

- *Buying a first home*- Funds can be accumulated and used towards the purchase of a first home.
- *Emergency Fund*- A source of additional income when it is needed most.
- *Income Splitting*- A Spousal RRSP is a means for one spouse to pay less tax by transferring funds to a spouse with lower taxable income.
- *Retiring Early*- RRSP's can create an income bridge until Old Age Security commences at age 65.
- *Pension for Life*- RRSP's can be converted into various types of income streams. A Lifetime Annuity is one option that most closely resembles pension income. A person retiring today at age 65 needs about \$150,000 in their RRSP to create a guaranteed income of \$1,000 per month.

The RIGHT Path™

May 24, 2005



Your Responsibilities as a Plan Member

- Make sure you understand how your plan works
- Take advantage of the information and tools made available to you to help you make your investment decisions
- Decide whether you should obtain investment advice

The RIGHT Path™

May 24, 2005



Your Responsibilities as a Plan Member

- Make the actual investment decisions
- Check to see how your investments are performing
- Revisit your investment strategy at least annually

The RIGHT Path™

May 24, 2005



Communication Strategies

Make the most of what retirement has to offer by taking full advantage of your group plan

The RIGHT Path™

May 24, 2005



CAP Seminar



Thank You

The RIGHT Path™

May 24, 2005

