7 Steps to Retirement Planning in Canada

Description

Retirement planning is the process of preparing for the years when you're no longer working. It involves setting retirement goals, calculating how much money you need to save, and deciding how you're going to save that money.

Since retirement planning is a major multistep process for Canadians, it's best to break it into bitesize chunks. Below we'll walk you through the seven major steps of retirement planning:

1. Set a retirement goal.
2. Decide your benchmark retirement age.
3. Determine how your spending will change.
4. Calculate how much you'll need.
5. Factor in additional income.
6. Pick investment accounts.
7. Start saving.

Let's get into it.

1. Set a retirement goal

Setting a retirement goal means assigning an intention that answers one big question: What do you *want* out of retirement?

For example, your retirement goal might be:

- Living modestly in your hometown
- Traveling broadly
- Living closer to grandkids
- Going back to school
- Picking up hobbies
- Working a part-time job

- Moving abroad to another country

At this point, you don't have to set a savings number, like $1 million, or a retirement age (we'll do those later). While those numbers are important, they mean nothing if they're not attached to a retirement dream or aspiration that makes you *want* to retire. This goal will steer the ship, while also making you feel excited about the rest of your planning.

2. Decide your benchmark retirement age

Your retirement age is the year you're going to stop working full-time for income. It's important to set this age now—even if it changes—as it will help you decide how aggressively (or conservatively) you should save and invest.

In Canada, most people retire between 60 and 70. At 60, you can start receiving benefits from your Canada Pension Plan (CPP). Most wealth advisors, however, recommend waiting until you're 65 to start taking CPP payments, as the longer you wait, the bigger your CPP payments will be. In general, your CPP payments will be 36% higher if you wait until 65 to retire versus retiring at 60.[(1)]

That doesn't mean you *have* to retire between 60 and 70. You can retire when it's most convenient for you. But as you're setting your own personal benchmark, here are some ages to keep in mind:

- **Age 60:** The Canada Pension Plan (CPP) begins.
- **Age 65:** Old Age Security (OAS) and Guaranteed Income Supplement (GIS) begin.
- **Age 71:** You must convert an RRSP into an RRIF.

3. Determine how your spending will change in retirement

Most retirees spend less in retirement than the years when they were working, simply because they eliminate certain expenses when they retire. Some common expenses you may no longer have in retirement include:

- Your mortgage
- Life insurance premiums
- Commuting expenses
- Saving for retirement

You'll also encounter new expenses that you perhaps weren't expecting. For example:

- Healthcare costs
- Long-term care
- Unexpected housing costs (such as maintenance or repairs)
- Adult children who need financial help
- Expenses related to your retirement goal (such as extra traveling)

Numerous everyday expenses will also carry over, such as food, clothing, utilities, and entertainment.

Pro tip: Start with your current spending habits, then eliminate expenses you don't expect to have (such as your mortgage or retirement savings goal). Then add healthcare, expenses related to your retirement goal, and “unexpected” expenses.

4. Calculate how much you’ll need in retirement

Now that you have a good idea of how you’re spending will change, let’s get a concrete number for how *much* you’ll spend. To help you estimate how much you’ll need, you can use the following methods.

1. The 80% rule

The 80% rule says you should expect to replace around 80% of your pre-retirement income to maintain your current standard of living in retirement.

For example, if your household income is $150,000 now, you’ll need around $120,000 annually when you retire. If you expect to live for 20 years after retirement, then you would need $2.4 million in savings and investments.

2. The 4% rule

The 4% rule states that you should withdraw 4% of your savings for every year of retirement. According to this rule, if you saved $1 million, you should withdraw $40,000 of your savings per year for the next 25 years. Keep in mind, this doesn’t include your pensions, just the money you’ve saved.

3. The 10x rule

Some financial experts recommend you multiply your annual salary by 10 to get your recommended savings goal. For instance, if you made $150,000, according to this rule, you should save $1.5 million to live comfortably in retirement.

The trick with the 10x rule is to use your *ending* salary, that is, the salary you have before you retire. That may seem impossible (after all, who can know what they’ll make when they retire), but a good rule of thumb is to multiply your current salary by 2% for every year you plan on working.

Keep in mind: These rules only give you estimates, and they shouldn’t take the place of a well-thought out retirement plan. To calculate your number, you’ll need to look closely at your spending habits, pension plans, and the life you want to live in retirement.

5. Factor in any additional income you expect to receive in retirement

Fortunately, when it comes to saving for retirement, you’re not alone. The Canadian government offers several pension plans to retirees and, depending on how long you worked and your income needs, you could greatly enhance your savings.

Here are some income streams you can add to your retirement planning.

Canada Pension Plan (CCP)

The Canada Pension Plan (CCP) is a government-sponsored pension that distributes monthly payments to retirees who contributed to their CCP during their working years.

CCP distributions depend entirely on how much you contributed to the system while you were working. You can start taking distributions as early as age 60 or as late as 70, though the earlier you start receiving payouts, the lower your monthly payments will be.

Old Age Security (OAS)

Like the CCP, Old Age Security (OAS) is a government-sponsored pension. Unlike the CCP, however, OAS doesn't depend on your contributions. Basically, any Canadian citizen above age 65—or legal residents who have lived in Canada for at least 10 years—is eligible for OAS payouts.

Similar to CCP, you can choose to defer your OAS payouts to an age above 65, which will raise your monthly payments the longer you wait.

Guaranteed Income Supplement (GIS)

Canadians with low incomes may be eligible for the Guaranteed Income Supplement (GIS). In order to receive GIS payments, your income has to be lower than a certain threshold (you can find eligibility tables here), and you have to file your income tax returns every year, even if you don't expect to owe taxes.

Part-time Employment

In addition to a pension, some Canadians may wish to continue working part-time past the age of retirement. In that case, you can still have a small stream of income coming in, even if the trickle is slower.

Home Equity

Finally, your home can be a source of income, especially if you own it forthright. Downsizing to a smaller house, or moving to an area with a lower standard of living, may allow you to put a portion of your equity towards retirement.

6. Pick an investment account to save for retirement

Investing money is crucial, but *where* you invest that money is just as important to your retirement planning. The Canadian government sponsors some lucrative retirement accounts, ones that will help your money grow without tax liabilities. If you want to pay less in taxes, you'll do well to invest your money in the following accounts.

Please note. This information is provided for educational use only, and is not retirement advice. For personalized information about your situation, please consult a financial advisor.

Registered Retirement Savings Plan (RRSP)

The Registered Retirement Savings Plan (RRSP) is a tax-sheltered savings account that houses certain investments. Basically, as long as you're earning income and you're under age 69, you can open an RRSP.

The tax benefits on RRSPs are remarkable. For one, any contributions you make into an RRSP grow tax-free. So, if the investments inside your RRSP perform well, you won't have to pay taxes on your earnings. Additionally, any RRSP contributions are automatically deducted from your taxable income, which can help you reduce how much you pay in taxes every year.

RRSPs do have some restrictions, however. For one, your annual contributions cannot exceed 18% of your previous year's income, up to a maximum of $29,210 (for 2023, the limit is $30,780). Any unused contribution space, however, will be rolled over to the next year.

Finally, you will pay taxes on RRSP withdrawals in retirement. That's because your RRSP contributions are *pre-tax,* meaning money the CRA hasn't collected taxes on. When you start making withdrawals in retirement, the CRA will tax them as ordinary income.

Group Registered Retirement Savings Plan

A Group Registered Retirement Savings Plan is similar to an RRSP, except it's sponsored by your employer. Often, your employer will match your contributions (up to a certain amount, usually three to five percent), and contributions are taken directly from your paycheque.

If your employer offers a match, always take the match! You don't want to leave money sitting on the table.

Tax-Free Savings Account (TFSA)

The Tax-Free Savings Account (TFSA) is another tax-advantaged retirement account. Like the RRSP, money invested in a TFSA grows tax-free. But, unlike the RRSP, TFSA withdrawals *aren't* taxed. That's because you invest after-tax dollars into your TFSA: you've already paid taxes, so the CRA won't make you pay them again, no matter how much your underlying investments earn.

Like RRSPs, TFSAs have contribution limits. For 2022, the annual contribution limit is $6,000 (it's expected to rise to $6,500 in 2023). Additionally, TFSAs have a total contribution limit, which is currently set at $75,500. That means if you open a TFSA today, you can contribute a grand total of $75,500 over the entire life of the account.

Please note: This information is provided for educational use only, and is not tax advice. For tax information that is personalized to your situation, please consult a tax advisor.

7. Start saving for retirement

When you've finally calculated how much you'll need in retirement, you'll typically have a moment of panic. Your ideal retirement number will often be in the hundred thousands, possibly millions (depending on your age and how much you've already saved), which is probably way higher than anything you've saved before.

While that number can be daunting, don't let it discourage you. The key is to save money over a long period of time, rather than all at once, and if you set your finances up right, saving money won't be a challenge. Here are some things you can do to set your retirement plan up for success.

Build a savings goal into your budget

It's one thing to throw money at retirement accounts in random spurts. It's quite another to save consistently every month over a long period of time.

In order to guarantee you're always saving money, build your budget around a specific savings goal, one that ensures you'll hit your retirement planning goals. Treat this savings goal like a fixed expense.

In other words, if your budget doesn't match up with your income, adjust variable expenses, such as groceries or entertainment, before you touch your savings goal.

Building a savings goal into your budget is more proactive than the more common "leftover" approach: spend money for a month, then put whatever is leftover into savings. This loose approach to saving money almost never works, as the temptation to spend almost always trumps the goal of saving money.

Maintain an emergency fund

Most Canadians want to save for retirement. But every time they start, a surprise expense pops up and derails their plans.

That's where the emergency fund comes in. Maintaining an emergency fund ensures you can always cover unexpected expenses without depending on high-interest debt, such as credit cards and personal loans. It also prevents the temptation to dip in your investment or retirement accounts, which can easily lead to early withdrawal penalties, taxes, and fees.

Though any emergency fund is better than none, most experts agree you're better off with three to six months of emergency savings. This will help you not only cover big pop-up expenses, such as medical bills, but also stay afloat if you or your spouse lost your jobs.

Pay down high-interest debt

If you’re loaded with high-interest debt, work on paying it off first before you start saving for retirement. High-interest debt can become extremely expensive over the long-run. In fact, in some cases, you may pay more on high-interest debt than you would earn on investments over the same period.

While you don’t have to be completely debt-free before you start saving for retirement, you should aim to eliminate high-interest debt as quickly as possible.

Set up automatic savings

One method to save consistently is to set up automatic transfers between your chequing and savings accounts. You can schedule to have a certain amount pulled from your chequing on the same day every month — possibly the day you get paid — such that you’re consistently saving money.

If you have direct deposit, you could set up automatic savings a different way. Just ask your employer to send a portion of your paycheque to a separate savings account. In this way, you eliminate the temptation to spend money that you really should have saved.

Retirement planning starts today

Every Canadian should start saving for their retirement as soon as they can. Your money will never have as much growth potential as it does today, and the younger you start investing, the more earning potential you’ll have.

If retirement planning still feels elusive, you can always seek help from a certified financial planner. These financial experts can help you make retirement plans, hit savings goals, and possibly even help you manage your investments.

PP NOTIFY USER

1. cleona
2. metienne
3. tmfbwelch

Date
2025/09/03
Date Created
2021/07/20
Author
sporrello