



Retirement

2009 Edition

# FOCUS

## Top RRSP limit continues to rise

*You will be able to put an extra \$1,000 into your RRSP for 2009 if your earned income for 2008 is at least \$116,667.*

Each January the maximum dollar limit goes up by \$1,000 under a multi-year schedule that runs to 2010. After that, plans call for the top limit to be indexed to growth in the average national wage.

As the accompanying table shows, the top limit for is \$20,000 for 2008 and \$21,000 for 2009. That means those with earnings of about two and a half times the average wage can save for retirement on a fully tax-sheltered basis.

### RRSP contribution ceilings

Tax year	RRSP Room*	If earned income in the prior year was at least
2008	\$20,000	\$111,111
2009	\$21,000	\$116,667
2010	\$22,000	\$122,222
2011	Indexed to growth in average national wage	

\* Assumes no membership in an employer-sponsored pension plan or DPSP

The annual \$1,000 increase only affects the RRSP ceiling. Your RRSP limit is still based on 18% of earned income for the prior year, minus the "pension adjustment" reported by your employer on your T4 tax slip if you belong to a pension plan or deferred profit-sharing plan. Earned income includes salary, employee profit sharing income, business income, rental income and taxable alimony/maintenance payments. Disability pensions from the Canada Pension Plan or Quebec Pension Plan count too, but not regular CPP or QPP retirement benefits. Earned income for RRSP purposes is then reduced by business losses, rental losses, union dues, tax-deductible employment expenses and any deductible alimony/maintenance you've paid.

If you contribute at the start of the year, see the RRRSP Deduction Limit Worksheet in Canada Revenue Agency publication T4040, available at [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca). If you contribute later in the year or monthly, you might wait for CRA to calculate your limit from the numbers on the 2008 tax return due by April 30. This will then be reported in the Notice of Assessment sent after your tax return has been processed.

If you own an incorporated business, you might wish to have your accountant review how much compensation you take as salary and bonus, and how much as dividends. Salary and bonus create RRSP room; dividends do not.

Pension limits are also rising. The maximum contribution to a defined contribution pension plan was \$21,000 for 2008 and will rise to \$22,000 for 2009. RRSP limits lag pension limits by one year to give employers time to report the pension adjustments that reduce RRSP room for plan members.

Defined benefit pension limits are going up too, but are calculated differently. Those retiring in 2009 can be paid as much as \$2,444 for each year of service. So, someone with 30 years of credit could be paid a pension of \$73,320 plus inflation indexing, if any. That's the maximum allowed by law. Whether you get that much will depend on the pension plan's rules and the earnings base on which the pension is calculated. As with the top RRSP limit, the defined benefit limit has been rising annually. After 2009 it will be indexed to growth in the average national wage.

# RRSP & TFSA: What should go where?

*Question: Should the new tax-free savings account (TFSA) be used to hold fixed income securities or equities? Answer: Yes.*

The TFSA is the most flexible tax-sheltered savings and investment program ever introduced by government. As of January 1, each Canadian aged 18 or older can deposit \$5,000 annually into a special account whose earnings will face no tax at all. This contribution limit will be periodically adjusted for inflation. Significantly, you can withdraw money from the TFSA to meet a spending requirement and then return it to the tax shelter in the following year when you have spare cash. This revolving aspect will make the account very handy for every Canadian without regard to wealth, age or station in life.

The TFSA will be particularly useful as an RRSP supplement for high-income savers who can afford to set aside more retirement money that the RRSP/pension system allows. It will also be valuable in retirement income planning because the tax-free withdrawals can create cash flow without reducing income-tested government benefits such as the age credit and Old Age Security payments.

### Level playing field

Normally, outside a sheltered plan, taxation is a major factor in deciding how to invest. Interest and dividends on shares of foreign companies are fully taxed while capital gains and dividends on shares of Canadian companies are tax-advantaged. The TFSA removes this distinction, so it can be invested entirely based on risk-return analysis. This means the optimal way to coordinate asset allocation between your RRSP and TFSA will depend on your personal situation.

At first glance, the TFSA tax shelter would therefore be ideal for interest-bearing vehicles such as bonds that would otherwise be fully taxed – especially strip bonds. Normally, it's inadvisable to hold strips outside an RRSP or RRIF because you must pay tax on the rising value even though you receive no cash until maturity. Since there is no tax to worry about, the TFSA makes it possible to hold strips outside your registered retirement plan. This enables people to save up on a predictable basis for a big expense. Suppose you dream of foreign travel for your first year of full-time retirement. You could earmark the TFSA for that purpose and every year buy a strip that will mature right when you will need the money. You will know in advance how quickly your money will grow and how much you will have when you are ready to hit the road.

On the other hand, you might find it better to keep interest-bearing securities

in your RRSP and use the TFSA for equities that are expected to outperform. This way, the greater accumulation will face no tax on withdrawal. Here's an illustration. Suppose you put \$5,000 into a strip bond that will compound at 6% a year for 20 years and \$5,000 into an equity mutual fund that's expected to average 8% annually over the same period. Both investments are then liquidated and withdrawn as cash with the RRSP withdrawal taxed at 48%.

As you can see, the equity fund's stronger growth generates more money for use in retirement, and the ability to access that greater accumulation tax-free means you'll have more money to spend.

RRSP holds	TFSA holds	Tax on RRSP withdrawal	Net income: RRSP + TFSA
Strip Bond	Equity Fund	\$7,697	\$31,643
Equity Fund	Strip Bond	\$11,186	\$28,154

We suggest that you sit down with your Investment Advisor and see how the TFSA can best be incorporated into your retirement planning given your personal situation.

### Be aware of wrinkles

But there is a potential pitfall for those investing in U.S. stocks that pay dividends. As we mentioned earlier, the federal and provincial governments fully tax foreign dividends, just like interest. The RRSP and TFSA both avoid Canadian tax, but there is a difference in foreign withholding tax on those dividends. Under a cross-border treaty, U.S. dividends paid to an RRSP or RRIF are not subject to U.S. withholding tax. Currently, this shield does not cover U.S. dividends paid to a TFSA, and changing that might take years. So, in choosing the right account for U.S. shares, weigh the potential capital appreciation against the impact of having to pay withholding tax on dividends.

Here's yet another wrinkle. People in generous defined benefit pension plans get hardly any RRSP contribution room because their "pension adjustments" are so high. (The pension adjustment reported on your T4 slip reduces RRSP room to balance tax-sheltered savings opportunities among those with good pension plans and those without.) These people can use the TFSA as a pseudo RRSP with \$5,000 of annual contribution room. Normally, those with defined benefit pensions – especially generous ones – can assume above-average

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## CIPF & CDIC : Covering your assets

The failure of several major U.S. and European financial institutions this year has led many investors to wonder if their NBF accounts are protected.

National Bank Financial is a member of the Canadian Investor Protection Fund (CIPF), which is an industry-sponsored fund established in 1969 to protect clients in situations where a member investment dealer became insolvent. It now has more than 200 member dealers.

In several respects, CIPF resembles the more familiar Canada Deposit Insurance Corporation (CDIC) that insures bank deposits. But CIPF coverage is more extensive.

Like CDIC, CIPF protection applies only in the rare event that an investment dealer fails. There have been just 17 such cases in nearly 40 years and CIPF has had to pay a total of only \$36 million, net of recoveries, for claims and expenses. This fairly small amount was all that was needed to ensure that no client suffered a financial loss over this period as a result of the insolvency of their brokerage firm. That's because investment dealers are tightly regulated, which includes regulations to ensure that fully-paid securities are available to be returned to clients in the event of an insolvency. Furthermore, in the past, financially sound dealers have taken over the accounts of troubled ones in situations of impending bankruptcy.

As with CDIC, you pay no fee for this protection. National Bank Financial and the other members finance the organization to provide investors with peace of mind.

### Coverage limits

While CDIC coverage is capped at \$100,000 per person per member institution, CIPF

coverage limit is ten times higher: \$1 million for any combination of cash and securities. And, this is multiplied for those with both general and retirement accounts. Most investors have \$2 million in coverage \$1 million for the combined value of regular cash and margin accounts plus \$1 million for the combined value of RRSP, RRIF, LIRA and LIF accounts.

Some clients are covered for more than \$2 million since Registered Education Savings Plans enjoy separate coverage, as do accounts for trusts, personal holding companies, partnerships and unincorporated associations and organizations.

It is unlikely that even those with accounts above the coverage limit incur a loss, because any claim to CIPF is determined after the assets recovered by the bankruptcy trustee, such as securities (segregated and non-segregated), cash, firm inventories, etc. are returned on a pro-rata basis to client accounts. Non-client creditors only share in these assets after client claims are satisfied.

### Only dealer failure

Please note that CIPF coverage applies only if a dealer becomes insolvent and is unable to return all its clients' cash and securities to them. CIPF does not cover fluctuations in account values and trading losses. Nor does it cover the failure of a company whose stock you own or a default on a bond.

For more information, ask your NBF investment advisor for the CIPF client brochure or visit [www.cipf.ca](http://www.cipf.ca).

### What about GICs in my RRSP or other brokerage account?

Each GIC is entitled to the same CDIC coverage that would apply had it been purchased directly from the issuing institution. Suppose your RRSP holds a \$90,000 GIC from one bank and a \$90,000 GIC from another, both banks are CDIC members and both GICs are eligible deposits. Your money is fully protected if either bank fails, or both do. If other institutions do not take over the banks that issued the GICs, CDIC will make payment to your RRSP. CIPF would not be involved.

## RRSP & TFSA: What should go where? (continued from page 2)

investment risk with their own savings since the pension plan guarantees a set level of retirement income for life. So, defined benefit pension plan members might consider using their TFSAs to hold equities.

A final point: there has been a trend in which provincial medicare plans shift more and more health care spending to individuals. Similarly, it has been getting harder and more costly for retired snowbirds to buy out-of-Canada health insurance for long winter sojourns down south. These trends show no sign of letup. So, you might consider using your TFSA as a

health care spending plan. Those still in accumulation mode could then favour equities with stronger growth potential while those in retirement might favour laddered bonds or GICs that protect capital, provide reasonable growth, and make some money accessible at least once a year.

As you can see, there is no simple answer to the question we posed at the outset. It all depends on your personal situation. So, we encourage you to discuss this in detail with your NBF investment advisor.

# Worried about the market? Get a checkup

2008 was a very tough year for investors and many Canadians are understandably worried about their retirement planning. Are you among them?

We suggest that you look beyond the day-to-day noise of the overall market and focus instead your unique situation. Ask your National Bank Financial investment advisor for a review of your portfolio's performance in relation to your retirement funding plan. You might be pleasantly surprised, or at least relieved. Consider:

- *The multi-year performance of your portfolio is what matters.* Before 2008 Canadian stocks enjoyed five years of very strong returns. So this part of your portfolio may well have been far ahead of plan. Adding 2008's performance to that of prior years, where do you stand in terms of the average annual return on which your planning was based?
- *Most NBF clients have balanced portfolios that hold bonds as well as stocks.* While the stock market has suffered heavy losses this year, bond performance has generally been slightly positive. We typically recommend a balanced portfolio for that reason – the value of diversification.
- *Many clients hold strip bonds in their RRSPs.* While the market value of a strip fluctuates daily, investors who hold to maturity know exactly how much each strip will pay and its average compound annual growth rate.
- *The foreign exchange value of the Canadian dollar has fallen in relation to the U.S. dollar and other major currencies.* While this means a mid-winter vacation down south might cost more, it also means that when performance is expressed in terms of Canadian dollars, foreign stocks and equity mutual funds have done better than the performance based on their home currencies. For example, at press time the S&P 500 Total Return Index had lost 33% since January 1 when valued in U.S. dollars but 17.5% when valued in Canadian dollars.

As you can see, there are many factors to consider. That's why we recommend arranging a portfolio and retirement plan review. Hopefully, you will find you are in good shape. But what if you have some catching up to do? There are four ways to get back on track; use any or all.

- *Save more.* If you have always maximized your RRSP contributions, the new tax-free savings account (TFSA) offers \$5,000 of additional tax sheltering. And beyond that, your NBF investment advisor can present an array of vehicles that are not tax-sheltered but are tax-advantaged or tax-efficient.

- *Take less.* In other words, reconsider the retirement lifestyle you have envisioned to see if you can reduce your income need and still live comfortably. Depending on how far you are from retirement, the new tax-free savings account might be able to provide a fair-sized amount of tax-free income, reducing the pre-tax income need you previously assumed. Remember too that the pension income splitting provision implemented for 2007 can mean substantial tax savings on pension income and RRIF withdrawals for many couples. So, if you have not yet factored this into your plan, you are now able to reduce the pre-tax income target you previously set.
- *Earn more.* On your investments, that is. This might be difficult in today's environment unless you are willing to assume more risk. Consult your Investment Advisor.
- *Work longer.* Putting in a few more years of full-time work or including part-time or seasonal work in your retirement lifestyle plan can make a big difference in how much retirement capital you will need.

Your NBF investment advisor has retirement projection software that makes it easy to see the impact of mixing and matching these alternatives. Call today for an appointment.

# Tax- deductible contributions past 71

■ Here's a year-end tax break for those who turned 71 in 2008 and still  
■ draw income from a business, director's fees, rental property or royalties.  
■

You cannot have an RRSP after the year in which you turn 71. But you can still make tax-deductible RRSP contributions to your spouse's RRSP, providing you have a spouse who's younger. But what if you don't?

Consider the age-71 top-up, a strategy that rests on three points:

- The RRSP system runs on a one-year lag. Income earned this year generates contribution room for next year – even though you will then be too old to use it.
- You can put money into your RRSP right up to the last day of the year in which you turn 71.
- The 1% penalty for over-contributing is levied monthly.

Suppose you earned \$100,000 this year and have used all RRSP room available in the past. Your earned income for 2008 will generate \$18,000 of tax-deductible contribution room for 2009. Since you

will not be allowed to contribute after this year, you could put \$18,000 into your RRSP in December as a deliberate over-contribution. You will be charged \$180 in tax (1% of 18,000 – corresponding to the one month you are in the situation of having over-contributed to your RRSP), but the penalty meter will click off on January 1 when the system creates the \$18,000 in room for 2009. In effect, the December deposit becomes an advance contribution.

The \$180 penalty buys you an \$18,000 deduction for your 2009 tax return – and you will have that much more retirement money tax-sheltered.

What if you have already converted your RRSP to a RRIF? Simply open a new RRSP in December, make the over-contribution and have the money rolled from this plan to your RRIF before year's end. If you prefer, your National Bank Financial investment advisor can do all the steps at once.



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