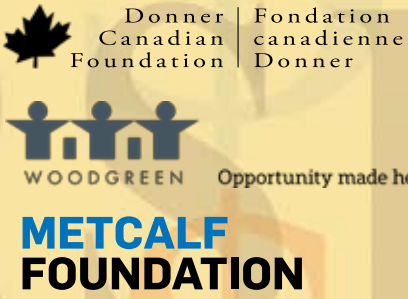
Maximizing GIS

A background paper on retirement financial planning for Canadians with very low incomes



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The purpose of this paper

This background paper is intended for people who give financial advice about retirement to low-income people. These people include:

- Financial planners and advisors
- Staff of banks and other institutions that sell financial products
- Financial writers and broadcasters
- Friends and family of low-income people who provide them with financial advice
- Community agencies that run tax clinics and other financial services for low-income people
- Organizations that design and provide training in financial literacy.

Most financial advice fails to take into account the availability of the Guaranteed Income Supplement for low-income seniors. People eligible for the GIS need very different financial advice from what is normally heard on the radio, on television, or in magazines and newspapers. Some forms of private savings reduce GIS entitlement, while others do not. ***Advising a low-income person to save within an RRSP, for example, can be very bad advice.***

Low-income people need savings and retirement strategies that won't leave them worse off in their senior years. The purpose of this paper is to educate people who help low-income adults plan for their financial future. While the income thresholds for GIS entitlement depend on family circumstances, in general, the considerations set out in this paper are relevant for singles with less than $20,000 in annual income and couples with less than $40,000.

Our aim is to put GIS planning at the centre of the pre-retirement discussion for these singles and couples. Far too many low-income people have failed to get good advice about filing their taxes and applying for a program to which they are entitled. ***The effect of this is to take millions of retirement dollars off the table for Canada's most vulnerable seniors.***

This paper provides background detail for the slide presentations and booklet that we have developed for advisors and counsellors. These materials can be

used in their own training and as an aid when advising low-income people. The topics covered are:

- I have a low income...
  Does CPP early retirement make sense for me?
- I have a low income...
  What's the smartest way to save before I turn 65?
- Retiring at 65 on a low income...
  How do I get the Guaranteed Income Supplement?
- Retiring at 65 on a low income...
  What's a smart way to save before I turn 71?

We have also developed a tool for determining Old Age Security for people who come to Canada. The rules around OAS and GIS eligibility are complex for people who have immigrated to Canada as adults or who have returned to Canada later in life. It is our hope that these tools will aid advisors helping low income people in this situation to take advantage of partial OAS combined with GIS.

The materials were field-tested with community advisors from tax clinics at WoodGreen Community Services and St. Christopher House in Toronto. Some were used in a workplace financial literacy program in Richmond, B.C.

Summary of GIS eligibility criteria and advice for low-income people

If you will be eligible for full OAS and you expect your other income will be close to or below one of these amounts:		Then this is what you should do to qualify for and maximize your Guaranteed Income Supplement (GIS):	
FAMILY STATUS	**INCOME LIMIT (at July 2012)[1]**	**BEFORE AGE 65**	**AT AGE 65, IF YOU ARE SOMEWHAT ABOVE THE INCOME LIMIT:**
Single	$16,512	• Apply for CPP early retirement as early as age 60. • Place any savings in a TFSA. • Don't place savings in an RRSP. • Consider converting RRSPs to a TFSA.	• If you have RRSP 'room', place any savings in RRSPs until age 71. • Consider borrowing to buy RRSPs until age 71. • Convert TFSAs to an RRSP to lower your income.
Couple, both getting Old Age Security (OAS)	$21,840		
Couple, only one partner getting OAS, other partner under 60	$39,600		
Couple, one partner getting OAS, other partner is 60-64	$30,576		

1. These figures change from time to time. Updated figures are available from http://www.servicecanada.gc.ca/eng/isp/oas/tabrates/tabmain.shtml

Introduction

People who are eligible for full Old Age Security[2] at age 65[3] and who have income (from sources other than OAS) below the limits shown here are eligible to apply[4] for the federal Guaranteed Income Supplement.

Incomes above which seniors are ineligible for the Guaranteed Income Supplement[5]	
FAMILY STATUS	**INCOME LIMIT (at July 2012)**
Single	$16,512
Couple, both getting Old Age Security (OAS)	$21,840
Couple, only one partner getting OAS, other partner under 60	$39,600
Couple, one partner getting OAS, other partner is 60-64	$30,576

These four income limits (which rise from time to time) are extremely important numbers for low-income people to think about during the five years leading up to their 65th birthday and beyond. They affect such things as:

- Deciding whether to take early retirement at age 60 under the Canada Pension Plan or any other retirement plan
- Deciding when to take out a Registered Retirement Savings Plan (RRSP) and when not to
- Deciding whether or not to put money into a Tax Free Savings Account (TFSA)
- Deciding what to do with existing RRSPs, TFSAs, and retirement income plans.

All of these decisions have a big impact on a low-income person's eligibility to collect the Guaranteed Income Supplement (GIS).

2. People who are eligible for only partial OAS are subject to higher income limits.
3. Old Age Security eligibility will continue to start at age 65 until at least 2023.
4. The federal government announced in the 2012 budget that it will put in place a proactive enrolment regime, eliminating the need for many seniors to apply for the OAS pension and GIS. This will be implemented between 2013 and 2016.
5. Adapted from http://www.servicecanada.gc.ca/eng/isp/oas/tabrates/tabmain.shtml. Updated figures are available at this web address.

Questions and answers about the GIS

1. What is the Guaranteed Income Supplement (GIS)?

According to Service Canada, "The Guaranteed Income Supplement provides additional money, on top of the Old Age Security pension, to low-income seniors living in Canada. To be eligible for the GIS benefit, you must be receiving the Old Age Security pension. It is paid monthly."[6]

People who have lived in Canada for at least ten of the 47 years between their 18th and 65th birthdays are eligible for Old Age Security (OAS).

2. How much is GIS worth to a senior?

The highest full monthly amount of GIS, combined with OAS, is currently $1,283.94 for a single person. Other tax credits and benefits can bring this amount up by about $150 a month.

These amounts are paid to people who have no other outside income except for their basic OAS payment. This is an entitlement program for seniors who are very close to poverty levels.

3. What makes the GIS different from OAS?

The big difference is the income tests that apply to each of them. For seniors receiving the full amount of OAS, there is no reduction in OAS benefits until net income reaches $67,688.

The GIS reduction, by contrast, is 50 cents on the dollar and it starts from the first dollar of countable income, which includes CPP income, other monthly income like a pension, or an RRSP cash-out. For most people, the reduction starts very quickly. For example, no GIS is available to a single senior after $16,512 in yearly income (not counting OAS).

The need for careful planning

People who have incomes low enough to qualify for GIS need to make careful plans to ensure that their income sources do not reduce their GIS entitlement or disqualify them altogether.

The careful planning we discuss here is to ensure that low-income seniors **maximize** their GIS. Most of the financial advice that is currently provided to low income seniors tends to lower GIS entitlement.

This paper discusses four retirement planning issues for low income Canadians:

1. Taking CPP early retirement benefits
2. Contributing to an RRSP or saving in a TFSA before age 65
3. Contributing to an RRSP or saving in a TFSA after age 65
4. Newcomer access to OAS and what it means for their GIS.

6. http://www.servicecanada.gc.ca/eng/isp/pub/oas/gismain.shtml

Topic 1. Taking CPP early retirement benefits

People who have paid into the Canada Pension Plan can take their pension, with reduced benefits, as early as age 60.[7] For a low-income person who may qualify for the GIS, this is often the right choice.[8]

Why? Because of the high GIS reduction. However, if a low-income senior is collecting a lower amount of CPP at age 65, there will be less GIS reduction. And in the meantime, they will have started collecting pension earlier and benefiting from the extra income.

Advising a low-income person on CPP early retirement

To plan a strategy for maximizing GIS entitlement, a low-income person must realistically assess how much money they will likely receive from CPP and other sources when they turn 65. Note that in determining income for GIS purposes, Old Age Security income is not counted.

When advising a low-income person on a decision to take CPP early retirement, it is important to ask if they intend to continue working after taking early CPP. If so, they should be aware that they will have to continue making CPP contributions until age 65.

For people who are receiving social assistance, taking early CPP is not an attractive option, because the social benefits will simply be reduced dollar for dollar by the amount of CPP. At age 65, social assistance converts to CPP, OAS, and GIS, and the reductions are no longer an issue.

7. http://www.servicecanada.gc.ca/eng/isp/pub/overview/refguide11.shtml

8. This advice for low-income people was recently confirmed in a report from the C.D. Howe Institute. See: http://www.cdhowe.org/comparing-nest-eggs-how-cpp-reform-affects-retirement-choices/17887

9. http://www.moneyville.ca/article/802910--roseman-taking-cpp-early-will-be-less-attractive-under-new-rules. See also Service Canada, Learn more about your public pension benefits. Annual newsletter for beneficiaries residing in Ontario, February, 2011. Making CPP contributions becomes optional between ages 65 and 70.

Topic 2. Contributing to an RRSP or saving in a TFSA before age 65

Registered Retirement Savings Plans (RRSPs)

For a low-income person who expects to qualify for GIS when they turn 65, saving money inside an RRSP is **not** a good option. The tax advantages that are so attractive to higher-income earners have no value for a person with little or no taxable income.

RRSPs are a way of postponing taxes to a person's retirement years. For people who have higher earnings during their working lives, it makes sense to postpone taxes to the years after retirement, when income will be lower.

The opposite is true for people who have incomes low enough to qualify for GIS. Canada's low-income seniors are, on the whole, better off than working-age low-income people. After they turn 65, their incomes will go **up**, through a combination of receiving:

- Old Age Security (OAS)
- Canada Pension (CPP), and
- Guaranteed Income Supplement (GIS).

Old Age Security and Canada Pension are fully taxable. Withdrawals from an RRSP are also taxable. The year someone turns 71, he or she must transfer RRSP savings into another type of account or financial contract that provides annual income starting the following year, usually a Registered Retirement Income Fund (RRIF).

This means that after retirement, low-income seniors may find that their incomes have risen to the point where they are exposed to taxation for the first time. Moreover, seniors receiving the GIS face a 50% reduction on additional income, such as income from RRSP redemption.

For these reasons, people approaching retirement on a low income need careful planning and good advice to avoid exposing their retirement incomes to taxation and GIS reductions. Unfortunately, they're not getting it. Instead, they receive pervasive, mainstream advice about making contributions during RRSP season.

They are even encouraged to take out RRSP loans. Low-income people usually have a very hard time obtaining retail credit. But during RRSP season, loans are easy to get, because the RRSP remains with the lending institution. For a low-income person, this is like getting a car loan and leaving the vehicle on the lot.

Tax-free Savings Accounts (TFSAs)

For a low-income person who expects to qualify for GIS when they turn 65, saving money inside a TFSA is a much better option. Unlike RRSP redemptions, there is no tax on withdrawing money from a TFSA. Nor is there any tax on interest earned within the TFSA.

Even more important, there is no reduction of the GIS. This is what the federal government says about TFSAs and the GIS:[10]

> ***No Impact on Income-Tested Benefits***
>
> *Neither income earned in a TFSA nor withdrawals will affect your eligibility for federal income-tested benefits and credits, such as the Guaranteed Income Supplement and the Canada Child Tax Benefit. This will improve incentives for people with low and modest incomes to save.*

The federal government's website gives this case study as an example:

> ***Benefits for Low-and Modest-Income Canadians***
>
> *Alexandre and Patricia, a modest-income couple, expect to receive the Guaranteed Income Supplement (GIS) in addition to Old Age Security and Canada Pension Plan benefits when they retire. They have saved for a number of years in their TFSAs and now earn $2,000 a year in interest income from their TFSA savings. Neither this income, nor any TFSA withdrawals, will affect the GIS benefits (or any other federal income-tested benefits and credits) they expect to receive. If this $2,000 were earned on an unregistered basis, it would reduce their GIS benefits by $1,000."*

Giving advice about RRSPs and TFSAs before age 65

When advising a low-income person about saving for retirement, recommend saving within a TFSA rather than in an RRSP. If the person is already contributing to an RRSP, suggest that they redirect these contributions to a TFSA. They may also wish to consider 'melting down' their existing RRSP. This simply means withdrawing the money over a period of years in a way that is planned and structured to minimize tax now and maximize their entitlement to GIS in the future.

10. http://www.tfsa.gc.ca/tfsapamphlet-eng.html

Topic 3. Contributing to an RRSP after age 65

As we have seen, contributing to an RRSP before the age of 65 has no real benefit for very low-income people. But for people whose incomes are a little over the GIS eligibility limit, or who are eligible for only a partial supplement, contributing to an RRSP *at age 65* might make a lot of sense.

Here's why:

Old Age Security and the GIS begin at age 65. But people can keep contributing to RRSPs until they turn 71. Contributing to an RRSP effectively lowers a person's income for purposes of GIS eligibility.

If a 65-year old with a very modest income happens to have some RRSP 'room' (shown on page two of the Notice of Assessment they receive after filing their tax return), they can contribute enough money to an RRSP to allow them access, or more access, to GIS.

For some seniors, this strategy might justify borrowing modestly to take out an RRSP. The increased income from the GIS would enable them to repay the debt.

This strategy is only effective until a senior turns 71, the last year to contribute to an RRSP. At that point, RRSPs must be transferred to a type of account or financial contract that will provide annual income starting the following year. In the best-case scenario, this income would offset the loss of GIS income.

An example: Mary

When Mary turned 65, she had a yearly income (excluding OAS) of $18,000. This was made up of CPP and a modest pension. She was also eligible for full OAS.

Mary's income was too high to be eligible for GIS. But Mary still had $60,000 in RRSP 'room'. That was because she couldn't afford to put money into an RRSP when she was working.

Each year, from age 65 to 71, Mary took out a $10,000 RRSP loan at low interest. The RRSP contribution reduced her taxable income to zero. It also made her eligible for the GIS supplement.

Mary got partial GIS ($346.76 a month).[11] To pay back her loans, she used this money, plus other savings and part of her RRIF money after she turned 71.

Mary knows that she will pay higher taxes on her income after she turns 71, because she will be getting money from her RRIF. But the taxes will be far less than the extra funds she has been able to access for the last 6 years.

Mary also knows that she will not qualify for the GIS after she turns 71. This is because her income will be too high and she can no longer make RRSP contributions.

However, Mary collected $24,966.72 in GIS income for six years. This is money she would never have received if she had not taken out the RRSP. And during those years, Mary saved on taxes.

A checklist for advising on RRSPs at age 65

Taking out an RRSP is a strategy that benefits only a limited group of low-income seniors. Use this checklist to decide if an RRSP might be good advice for your client:

- ☑ Is your client between the ages of 65 and 70?[12]
- ☑ Are they eligible for Old Age Security? (Eligibility for GIS hinges on eligibility for OAS. If they are not eligible, please see Topic 4: GIS for newcomers.)
- ☑ Do they need further deductions from their income to be eligible for GIS, or to maximize GIS? (Do not count current income from OAS or GIS.)
- ☑ Do they have RRSP 'room' showing on their income tax statement?
- ☑ Do they have access to money to contribute to the RRSP, or can they access an RRSP loan through their bank?

11. Http://www.servicecanada.gc.ca/eng/isp/oas/tabrates/tab1-22.shtml

12. Technically, a person could begin this strategy at age 64, so that income reported during the year they turn 65 is already lowered. Advisors must be careful not to counsel this strategy too soon, however, for people receiving social assistance or provincial disability benefits. The RRSP might be viewed as a disqualifying asset.

Topic 4. GIS for newcomers

Eligibility for the Guaranteed Income Supplement hinges on eligibility for Old Age Security. A person receives **full** OAS if they have lived in Canada at least 40 of the 47 years between their 18th and 65th birthdays.

For people who do not meet this criterion, the rules are more complicated. Under these rules, however, many low income people could qualify for a combination of partial OAS plus GIS — the equivalent of receiving full OAS.[13]

Newcomers can get **partial** OAS if they have lived at least 10 years in Canada. If their income is low, this means that they may also be eligible for **full** GIS. Moreover, low-income newcomers with only partial OAS can get a higher GIS amount through a special, extra GIS increment.[14] This means that for this group, income limits for GIS eligibility are sometimes higher than the limits shown in the table on page 4.

Fifty-three countries have reciprocal social security agreements with Canada.[15] These agreements allow partial OAS eligibility after one year of residence. The amount of combined OAS and GIS increases gradually over the next 10 years of residence.

Other factors that have an impact on GIS for newcomers include money received from a state pension plan in the country of their birth or another country where they worked before coming to Canada.

Would the strategies in this paper work for someone with less than 10 years of residence?

For low-income people who have lived less than 10 years in Canada and who qualify for partial Old Age Security under a reciprocal agreement, GIS entitlements grow gradually, at the rate of one tenth (10%) of the benefit for each year of residence.[16] The tables in the Appendix explain how GIS payments grow over a ten-year period and give a breakdown of the OAS and GIS components after ten years.

Since the GIS entitlements are initially very small, the amount of income it would take to reduce the GIS to zero is also very low. To qualify for GIS, the senior would have to have very little or no outside income. This would mean that the RRSP strategy after age 65, for example, may not be worth using.

However, the strategies around early retirement and saving within a TFSA are very relevant to this group. Any person who anticipates a very low income after retirement should do everything they can to maximize their GIS entitlement.

13. For an overview of the rules, see http://www.servicecanada.gc.ca/eng/isp/oas/oasoverview.shtml.

14. See http://www.servicecanada.gc.ca/eng/isp/oas/oasoverview.shtml: "If a person is receiving a partial Old Age Security pension, the maximum Guaranteed Income Supplement may be increased by the difference between that partial pension and the full Old Age Security pension."

15. More than 150 countries do not. The list of countries that have reciprocal agreements is available at: http://www.servicecanada.gc.ca/eng/isp/ibfa/socsectoc.shtml.

Afterword: Why does most financial advice ignore GIS planning?

There are a number of reasons why low-income people don't get the advice they need to plan their retirement. First, most financial advice is directed at people who have average or higher incomes. These people expect their incomes to drop after retirement. People who are on social assistance, however, can expect a modest gain in their standard of living after age 65. This is because provincial disability and social assistance programs for working-age adults tend to provide lower incomes than Canada's social security entitlement programs for senior citizens.

The financial planning required for someone whose income rises at age 65 is very different from the planning needed for a person whose income goes down. For example, in their pre-senior years, low income people often have income sources like social assistance or disability payments, which are not taxable. When they become senior citizens, they receive new benefits like OAS and CPP, both of which **are** taxable. Middle and high-income people tend to pay less in tax once they reach 65. The opposite is true for many low-income people turning 65.

Most financial advisors are unfamiliar with the workings of income security programs that benefit lower-income Canadians, perhaps because they don't deal with them as often. The Guaranteed Income Supplement is an entitlement program, as opposed to a tax credit program. It is not directly linked to the sale of a financial product, as is the RRSP. Hence, financial institutions have less incentive to train their staff to give sound retirement advice to low-income people. Moreover, many advisors believe they should not be counselling people to arrange their affairs in such a way as to take advantage of entitlements.

The TFSA: Finally an incentive for the poor to save

With the introduction of the Tax Free Savings Account (TFSA), the poor finally have a good way to save and a reason to purchase financial products. Social assistance programs emphasize means testing and asset stripping, not saving. But the TFSA has been explicitly structured to "improve incentives for people with low and modest incomes to save" without penalties.[17]

Education for those who advise low-income people on taxes and retirement planning has lagged behind this development. It is our hope that this paper will lead to more discussion and a better understanding of what low-income Canadians need to know in order to become more financially literate and more financially secure.

16. This includes immigrants whose sponsorship agreement has broken down because the sponsor dies, is imprisoned for more than six months, is convicted of abusing the sponsored person, or is in personal bankruptcy.

17. http://www.tfsa.gc.ca/tfsapamphlet-eng.html

Appendix

These tables show the OAS and GIS payment structure for single people who, at age 65:

- have been in Canada for less than 10 years
- have met the one-year residency requirement
- are not sponsored and
- come from a country that has a social security agreement with Canada.

The numbers illustrate what would happen for single seniors who have **no other income**. The numbers would vary for seniors with small incomes from other sources.

OAS and GIS payment structure for low-income single people who are eligible to apply after one year of residency

TABLE ONE

This table shows the amounts of OAS and GIS a senior receives during the first 10 years after they qualify to apply. They get more money each year until they reach the tenth year.

Age at arrival in Canada (with no prior residency)	Portion of OAS paid at 65	Portion of GIS paid at 65	Monthly OAS/GIS combined (figures as of July 2012)[18]
64	One fortieth	One tenth	**$140.66**
63	Two fortieths	Two tenths	**$278.58**
62	Three fortieths	Three tenths	**$413.78**
61	Four fortieths	Four Tenths	**$546.26**
60	Five fortieths	Five tenths	**$676.02**
59	Six fortieths	Six tenths	**$803.05**
58	Seven fortieths	Seven Tenths	**$927.36**
57	Eight fortieths	Eight tenths	**$1,048.94**
56	Nine fortieths	Nine tenths	**$1,167.80**
55	Ten fortieths	Ten tenths	**$1,283.94**

TABLE TWO

Calculating the amounts in Table One

This table shows the calculation of OAS and GIS for a senior newcomer with no income, corresponding to the amounts in Table One. The mix of OAS and GIS is determined by the number of years of residency the person had at the time they turned 65.

The ratio of OAS to GIS is of interest because OAS is taxable and GIS is not. In addition, OAS can be received regardless of sponsorship agreements that prohibit receipt of GIS.

It is also worth noting that a senior with some other income and a high ratio of GIS to OAS is tax advantaged over a senior with a low ratio of GIS to OAS.

Years of residency on turning 65	OAS Based on 1/40 of full OAS for each year in Canada	Regular GIS	Extra GIS payment	Total (OAS + GIS Maximum)
1	$13.62	10% of $738.96	10% of $531.36	$140.66
2	$27.24	20% of $738.96	20% of $517.74	$278.58
3	$40.86	30% of $738.96	30% of $504.12	$413.78
4	$54.48	40% of $738.96	40% of $490.50	$546.26
5	$68.10	50% of $738.96	50% of $476.88	$676.02
6	$81.72	60% of $738.96	60% of $463.26	$803.05
7	$95.34	70% of $738.96	70% of $449.64	$927.36
8	$108.96	80% of $738.96	80% of $436.02	$1,048.94
9	$122.58	90% of $738.96	90% of $422.40	$1,167.80
10	$136.20	100% of $738.96	100% of $408.78	$1,283.94

18. To obtain updated figures for Tables 1 and 2, visit http://openpolicyontario.com.

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