

FINA200

Summer 1 2011

Case 3 - due Wednesday, June 15, 2011

Covering Chapters 9, 10, 13 and 14

PLEASE NOTE

- THIS IS AN INDIVIDUAL ASSIGNMENT.
 - YOUR SOLUTION MAY BE SUBMITTED IN ENGLISH OR FRENCH.
 - ACCEPTABLE SUBMISSION FORMATS INCLUDE WORD 2007 (.docx) or PDF. EXCEL IS NOT ACCEPTED.
 - OUTSIDE RESEARCH WILL LIKELY BE REQUIRED. PLEASE QUOTE ALL SOURCES AND DO NOT COPY AND PASTE!
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Perhaps you've been listening to conversations around the dinner table, or on your visits home, about how your parents, aunts or uncles don't have enough money to retire on. Not only did the retired and soon-to-be retired lose a portion of their personal retirement savings in RRSPs or RRIFs due to the market crash of 2009 (from which many have not recovered), but many expect that their pensions may be cut back. Consider the following situation.

I was recently asked by a client named Winifred, aged 65, to review her investment portfolio given that she had been advised that her corporate pension could be cut by as much as 30%. She wanted reassurance that her money was appropriately invested and asked the classic question, "Will I have enough?" Winifred comes from a line of long-lived women - so she stated her life expectancy at about 100+, hence her concern that she could "run out of money". She also posed a few other questions about her financial situation.

Winifred is a widow and has 3 adult children and 5 grandchildren. She lives common-law with a widower in a spiffy condo development for seniors in St. Lambert. He has two adult children who will inherit the condo and his investment assets when he dies.

Winifred has a significant portfolio of registered and non-registered assets - approximately \$200,000 in an RRSP and \$400,000 in an investment account with a bank-owned full-service broker, which she wishes to leave intact to her 3 children. She makes no withdrawals from her RRSP, but has any investment income earned on her non-registered portfolio deposited into her bank account. The overall asset allocation in her RRSP and investment portfolio is 70% fixed income, 30% equity.

Winifred has lived in Canada her entire life and moved to Montreal from Ontario two years ago. She was a senior manager in an international pharmaceutical firm before she retired. Her pension plan currently pays an indexed benefit of about \$40,000 a year.

Use the following rates for planning purposes. The forecast for inflation is 2%.

Cash and cash equivalents	2%
Fixed income	6%
Equities	8%

Question 1 (30 marks)

Assume that Winifred's pension is cut by 30%. Estimate her gross and net income in 2012 from all sources. Assume a combined federal/provincial tax rate of 35% for ease of calculation. Assume also that she receives 75% of the maximum QPP. Discuss whether the OAS clawback would apply.

In your estimation, will Winifred have enough after-tax income? Please explain.

Question 2 (15 marks)

What type of pension does Winifred have? Discuss 3 characteristics that support your point of view.

What could cause her former employer to reduce her pension by 30%?

Question 3 (15 marks)

When will Winifred have to collapse her RRSP? What options will she have with the assets held in her RRSP at that time? Identify one strength and one weakness of each option.

Question 4 (20 marks)

Winifred's portfolio contains the RBC Bond Fund. Explain this fund's load, MER, 1, 3, 5 and 10-year compound return, risk (standard deviation, not beta) and top 5 holdings. You will need to research this information. Please quote your source.

Is it an appropriate investment for Winifred, and why? (Hint: Look at its investment objectives.)

Question 5 (5 marks)

Is Winifred's overall asset allocation appropriate? Why do you think so? Please provide your reasoning.

Question 6 (15 marks)

Upon her death, Winifred's estate would be responsible for paying the capital gains tax on a deemed disposition of her assets. (Deemed disposition means we presume that all her assets were sold immediately prior to her death.) Given that Winifred wishes to pass all her assets to her children, what type of life insurance should she purchase, and why?

What other types of insurance would you recommend for Winifred? Please explain.