Another day older and deeper in debt

Tips on how retirees can get out of the hole

By Deanne Gage 06-07-11

Once upon a time, when people retired, they had paid off the mortgage and other debts. After all, who wants to carry on liabilities on a fixed income? Well, the answer today is at least half of us. A 2010 poll from Investors Group found that 56% of Canadians do not consider paying off a mortgage as a deciding factor when retiring. Furthermore, only 56% retire debt-free, down from 61% a year ago, according to a recent survey from RBC. Why has our attitude toward debt shifted so much?

About the Author
Deanne Gage is a Toronto-based writer who has specialized in personal-finance issues since 1999. A recipient of several journalism awards, including one from the Investment Funds Institute of Canada, she is also a former editor of *Advisor's Edge* and Advisor.ca. She can be reached at deannegage@gmail.com.

It's partially due to apathy and entitlement. In the case of the former, it's not uncommon for people "to fall into the trap of remortgaging to finance lifestyle expenses," says Michael Berton, a financial planner with Assante Financial Management in Vancouver. Also, since mortgages can eat up to 72% of a person's income in Vancouver, according to the recent RBC Affordability Study, it takes that much longer to pay it off. Berton tends to emphasize downsizing as a strategy to reduce, if not eliminate, debt.

Still, even in smaller, more affordable towns like Nelson, B.C., Bradley Roulston finds debt more "socially acceptable" and people buying into the notion that debt is OK as long as one's net worth increases. "That drives me crazy," says Roulston, a CFP at Healthcare Financial Group. "Though assets fluctuate in value, debts do not fluctuate. Therefore if you buy a house for $300,000 with a $250,000 mortgage, the house may go up in value but could just as likely go down. However, your debt will only go down when you pay it down."

Kurt Rosentreter, a senior financial advisor with Manulife Securities Inc. in Toronto, finds that those retiring with debt in their 60s are basing their decision to carry a mortgage on low interest rates. "If 10 years from now, we're looking at 8% interest rates, what is that going to do to the percentage of your money that has to go to servicing debt? You're at an age where you can't resume a career. It is shallow thinking and very emotional."

Kurt Rosentreter

So is praying for substantial inheritances from their elderly parents, says Berton. "It's amazing how many people bank on [inheritances] to save them," he says. "I tell people not to count on it. There may not be that much money and sometimes it goes to the church or charities."

Some who are contemplating retirement want to pay down debt but can't seem to find a way out of the situation, Rosentreter says. At the same time, they are fed up with their jobs. "They are at an age where they have been working for 25 or 30 years and are frustrated," he says "They feel they deserve to retire. My preference is for them to keep working until they are debt-free because of the cost of debt. If someone is 63 and still carrying a six-figure debt load and wants to retire, they are violating all the rules of Money 101. The problem is it's not easy to convince them."

So, Rosentreter starts number-crunching. He puts together spreadsheets that include their investments (shown at a conservative 5% rate of return), pension (if any) and benefits such as Canada Pension Plan and Old Age Security. He also gets his pre-retirees to do an accounting of their expenses and categorize them by:

- fixed core costs (payments that will not change, such as property tax and utility bills)
- variable core costs (necessary to buy but can vary the expense. For instance, spending $50 on a birthday present instead of $500)
- discretionary costs (i.e. meals and entertainment)

- luxury costs (i.e. vacations)

People need money for fixed and variable costs. If they're falling short of cash in retirement, it's the discretionary and luxury purchases that will be affected. Rosentreter's clients often tell him, "I like to spend money without worrying about what's in my bank account." He counters with this statement: "Go ahead and retire but you're going to have to pay for the mortgage for 15 more years and there's no money left for vacations and fun stuff."

He finds that's a great motivator for people to find a part-time job for "pocket change" and pay down debt. "If you dislike your job, it might just be to find something part-time without the commute," he says.

Another motivating factor is considering the next generation. What message will baby boomers send their offspring about retiring with liabilities? "It's a dangerous precedent to set for their children who will be even further behind the eight ball," Rosentreter says.

Thankfully, there is a happily-ever-after ending for one of Berton's clients whom we'll call George. George wanted to retire but had six-figure debt load. So he took drastic action. George sold his house and moved to the Middle East for three years to work as an aircraft mechanic.

Since he made four times his Canadian salary over there, George was able to wipe out his debt. He returned to Canada with substantial savings, and bought a substantially cheaper house in small-town Alberta, plus a motor home. "That was radical surgery but he was a person who was happy to travel," says Berton.