Sophia and Raj decide to sell the family home: RBC® helped build their plan

Sophia and Raj love their home. For the past 25 years, it has been their castle – a place where they raised two sons and a daughter. Over the years, neighbours became friends, they upgraded their kitchen, and created a home full of memories.

But over the last five years, a few things have changed. The winters started to seem a little harder than they used to, so Sophia and Raj have gone south for the season. Upon their return home each spring, they notice things about the house that need work – the deck needs to be refinished, the roof needs replacing, and the driveway could use a fresh pave.

At the same time, they have been finding the budgeting to be a bit trickier. When they retired at age 62, both Sophia and Raj took early Canadian Pension Plan (CPP). Raj's company pension income was enough to cover day-to-day expenses, with the odd withdrawal from savings for renovations and vacations. While they both started to collect Old Age Security (OAS) at 65, with steady increases to property taxes and utility bills, it didn't feel like they got a raise! Last year, at age 68, they decided to convert their Registered Retirement Savings Plans (RRSPs) to Registered Retirement Income Funds (RRIFs) to boost cash flow.

After meeting a local real estate agent at a community event, Sophia and Raj decided to explore the idea of downsizing – selling their home and investing some of the money to boost their monthly cash flow. The idea was already on their minds after a friend's recent health scare forced a quick decision to downsize. The agent spent time talking about the advantages and disadvantages of different types of properties and suggested something they hadn't thought of before: renting. It was a lot to take in, so Sophia and Raj booked time with Tara, their RBC Financial Planner, to review their finances and understand the implications of the choices available.

The financial snapshot:

Sophia and Raj paid off their mortgage five years ago, and pay $5,000 a year (or $415 a month) in property tax plus $400 per month for heat and hydro. The agent estimates the value of their home at $650,000. A condo in the same area costs $375,000 with combined maintenance fees and taxes of $650 per month. If they prefer to rent the condo, the estimated cost is $2,100 per month.

When Sophia and Raj sell their home	
Proceeds from the sale of their home	$650,000
Less: Real estate fees & closing costs	$65,000
Available funds	$585,000

Sophia and Raj's marginal income tax rate is 30%. They expect to live another 25 years and aren't planning on setting much aside to leave as an inheritance. They've talked to their family – their children want them to enjoy what they have rather than worrying about leaving money behind. Based on all of this, they ask Tara to calculate the amount of monthly income and capital they could withdraw if the available funds earn a 4.5% rate of return. To be cautious, they ask her to arrange a lower monthly payment to begin with, and increase it by 3% every year to help keep up with inflation.

Option 1: Purchase a condo for $375,000 and invest $200,000	
Proceeds of house sale	$585,000
Condo purchase price	$375,000
Moving expenses	$10,000
Funds available to invest	**$200,000**
Condo fees & property taxes	$650/month (heat and hydro included)

Under this scenario – where they invest $200,000 at a rate of 4.5% - their additional monthly after-tax cash flow is $688 in the first year. By year 25, their monthly cash flow is $1,399.

What Option 1 Gives Them:	
Monthly cash generated in year 1 from $200,000	$688
Savings from property tax + basic house expenses	$815
Less fees + taxes on condo	($650)
Additional monthly cash in year 1	$853

Option 2: Sell the house and rent a condo for $2,100 per month	
Proceeds of house sale	$585,000
Moving expenses	$10,000
Funds available to invest	**$575,000**
Monthly rent	$2,100

Under this scenario – where they invest the full amount of their home proceeds – their additional monthly after-tax cash flow in the first year is $1,978. By year 25, it is $4,021.

What Option 2 Gives Them:	
Monthly cash generated in year 1 from $575,000	$1,978
Savings from property tax + basic house expenses	$815
Rent (includes basic housing expenses)	($2,100)
Additional monthly cash in year 1	$693

The bottom line

Both options improve cash flow for Sophia and Raj.

Purchasing the condo allows them to continue to be homeowners, with the potential for appreciation (or depreciation) in the value of the condo. This gives an extra cushion if they live longer than 25 years, and would leave an estate. While it's not critically important to them, they find it comforting. This option comes with the continued responsibilities and expenses of home ownership.

Renting the condo means never having to worry about replacing appliances or dealing with major repairs. Renting

also means that they are free to move if they don't like the building or the neighbourhood. On the flip side, it implies less control over things such as renovations and wall colour. And it means that when their income stops after 25 years, they have no further financial cushion.

The decision:

Sophia and Raj decide to buy the condo; they are confident in the neighbourhood and like the building. Raj feels strongly about home ownership but admittedly worries a bit about the condo fees. On the bright side, he looks forward to having someone else manage repairs and maintenance. The extra $853 per month will allow them to travel while still in good health, and enjoy the retirement lifestyle they worked hard to achieve.

Sophia and Raj decide to buy the condo; they are confident in the neighbourhood and like the building.

What would you do? Would your answer change if your circumstances changed? What if you or a loved one experienced health problems, a loss, or received a severance package before retirement?

Speak with an RBC Financial Planner who can review your options with you, and help you make the best decision about your financial future.

To learn more about how RBC can help you create your ideal retirement, speak to an advisor today or visit us at rbc.com/next30

Financial Planning

VPS97441

115926 (12/2016)