Prepping for the Critical Retirement Years

BY JOSEPH H. GUYTON

Whether you are a C-suite executive, a sole proprietor or an entrepreneur, many of the issues you will want to evaluate about retirement are the same: income, market risk and the strategies that surround them. If you own your business, there will be additional challenges related to your orderly exit and the creation of income streams from what is likely your largest single asset, the business.

Over the years, you planned for retirement in several ways: saving in a retirement plan, investing your savings, buying a second home and paying down debt. You may have a specific date in mind, and you probably don't have an answer to the question, "I have all these plans, but how does this actually work?"

Here are some tips for the last stretch of your plan to answer that question:

Know Your Lifestyle

Have a good sense of what you will need to maintain your desired lifestyle on an inflation-adjusted basis. Surveys show that people are routinely off in their estimates by 20 percent. In addition, you might want to consider the impact of your age and health on your financial needs.

Some advisors break retirement into three phases. "Go-Go" is when every day is Saturday, and you travel and spend potentially more money than when you worked. The "Slow-Go" are the later years when you are still quite active but simply do less. And the "No-Go" are the elderly years when you may simplify your life. Each of these phases can justify a reduction in your inflation-adjusted cash flow needs.

Balance Your Assets

Everyone has some mix of taxable versus tax-deferred versus tax-free assets. Most people prefer to have tax-free assets, such as municipal bonds, Roth accounts, and life insurance. However, people generally accumulate the bulk of their wealth in taxable assets such as stocks, bonds, business interests and particularly tax-deferred assets like 401(k), IRA and real estate. While everyone is different, an ideal mix of assets would have a balance among these three categories.

Your assets can also be defined by their purpose. They generally fall under three categories: protection, sufficiency and surplus.

Protection assets are contractually based and are used to shift risk via a legal contract to another party. These include homeowner's, auto, term life and disability insurance.

Sufficiency assets are also contractually based. They are used to generate a guaranteed income over time. Many people like having a significant portion of their income in retirement that can be guaranteed. These assets include guaranteed pension plans, bank CDs, bonds held to maturity and annuities.

Surplus assets are market based. What you get to spend is the residual value of the asset as determined by a market. They are not typically guaranteed and can go up or down. Examples of these assets are stocks, real estate, your business, 401(k) retirement plans and their equivalents.

While many people want guaranteed income in retirement, they tend to accumulate their wealth in surplus assets where there is more risk and potentially more reward. This imbalance is attributable to several causes: the decline of guaranteed pension plans, the rise in 401(k)-type plans, and a lack of education on how to generate a guaranteed income in retirement.

A Plan for Spending

It's not enough to estimate how much you need to retire. You should also develop a plan for how to use it. Each year you will need a certain amount to live. It may be delivered by several components: part-time income, Social Security, investment income, a pension and rental income, among others.

You need to consider how to mix and match these sources on a tax and risk efficient basis.

Make sure your plan is flexible and well balanced. What if you have unforeseen ex-

penses? Can you get a lump sum from a low risk account to meet the need? What if the market goes down? Will you want to make a withdrawal? Checking your plan for flexibility will help you prepare for a variety of circumstances.

You must also protect your financial plan by having adequate umbrella liability, life insurance and long-term care insurance. Be sure all estate planning documents are up to date as it is important to minimize the potential threats to your wealth and retirement. A professional review of your protection strategy is important.

Action Items

• Develop a detailed inventory of your assets so that everything is in one place and easy to find.

• Develop a model for your income that includes all the different sources: 401(k), pension, Social Security, non-qualified deferred compensation plans, rent, sale of business, consulting income, royalties, etc. Any one or all of these might contribute to your total living need in any one year. It is important to prioritize the use of these income streams as well as their risk and tax efficiency. You should use this model to evaluate various scenarios such as: What if my income need is different? What if I need long term care? What if I have to pay for a wedding? What if the market declines?

• Review your Social Security record and benefits and understand your options. Depending on when you choose to start drawing benefits, the amount you will receive differs. For example, you may be able to collect at age 62, but you will receive a reduced benefit. If you wait beyond your full eligibility age and start taking benefits at age 70, your guaranteed payment for life will be larger.

• Review your insurance coverage including umbrella liability that protects your assets from claims of creditors, which is critical in a litigious time. Also check your life insurance, which often expires when people retire because it was provided through an employer plan with contractual reductions, or it was purchased with a limited guarantee period. Life insurance may be used as a mechanism to replace the "nest egg," recover unforeseeable costs for a survivor or to create an estate for heirs. Long term care insurance can be used to protect your assets for a survivor in the event that extra care is needed.

• Be sure all your estate planning documents including power of attorney, health care proxy, wills and trusts are up to date.

• Review beneficiary designations on retirement plans, insurance policies and annuities to be sure they are correct and represent your wishes.

• Check your asset allocation, paying special attention to your risk exposure. A large drop in the market can be a quick way to derail your long-term plan. Be sure that you have a good balance in your sufficiency and surplus assets.

By using these tips and action items, you can begin to get a sense of how your retirement will play out and how comfortable it is likely to be. It is worth the extra effort to be sure that your lifetime of hard work and savings will allow you to transition to the next phase of life on your terms. ■

Joseph H. Guyton is principal of the Guyton Group in Portsmouth. He can be reached at 603-766-9200. For more information, visit guytongroup.net.