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BUSINESS

Planning is essential for security after retirement

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You've saved all your working life for retirement and built a nice nest egg. Now that you're retired, making that money last should be your goal. Hopefully, your pre-retirement planning has paid off.

“The first step to make your money last in retirement is to plan before you retire to make sure you can do so successfully and on your terms,” said Wade Chessman, certified financial planner at Chessman Wealth Strategies in Dallas. “Some of the decisions you make today, such as when to take Social Security, can have a lasting long-term impact.”

There are many similarities in managing money before and after retirement, said Tom Murphy, certified financial planner at Murphy & Sylvest in Dallas.

“The biggest difference is that pre-retirement, you are putting money into the account, while post-retirement you are taking it out,” he said. “Although this seems obvious, it has profound implications.”

And it’s those implications that should influence how you manage your money in retirement.

Build a cushion

One of your first steps should be to develop a hedge against the stock market’s ups and downs.

“If the market fluctuates in value pre-retirement, you can simply wait until it recovers, whereas in retirement when you are dependent upon income from your accounts, you cannot wait,” Murphy said. “A market downturn in the first few years of retirement can be devastating to your retirement assets since you may be forced to sell into a declining market, permanently losing value.”

Carrie Schwab-Pomerantz, senior vice president at Charles Schwab & Co., said you should keep at least a year of cash available, “especially with these volatile times.”

“Set aside enough money to cover at least one year of spending,” she said. “This is the amount that you’ll need in addition to the income you can count on, from Social Security, a pension or real estate investments.”

Murphy takes it a step further and urges planning for three years.

“It is absolutely necessary you have enough cash and assets which will not fluctuate in value to cover at least three years of needed income,” he said.

Murphy gave this example: If you need $75,000 a year to live on and you get $25,000 from Social Security benefits, then you need at least $50,000 per year for three years.

For the first year after retirement, your $50,000 should be in cash. For the second and third years, the money can be in certificates of deposit, bonds or other assets that will not fluctuate with the market.

“That way, you will know where the money will come from for you to buy groceries and cover other expenses for the first three years of retirement,” Murphy said. “Those dollars which you will not need until after the third year can be invested in a diversified portfolio with the goal of keeping up with inflation.

“It is those three years of cash and maturing assets which makes the difference,” he said. “Just be certain to replace the cash, bonds and CDs as you spend them.”

Watch your expenses

“In retirement it is crucially important to monitor your expenses and to adjust spending habits over time,” Chessman said. “Ideally, you want to develop a spending plan and begin monitoring expenses before retirement so that there are no surprises.”

Look for areas that are out of whack or where you are spending more than you thought.

“This is also a good time to look for opportunities to save money,” Chessman said. “Perhaps it is time to consider downsizing or selling your second home. There may be expenses that will be reduced or even eliminated in retirement, such as gasoline or dry cleaning. This is a good time to review your P&C [property casualty insurance] coverage, given your change in circumstances and changes in driving habits.”

Milton and Patricia Bradley, both retired, have set a goal to pay off their car and become debt-free as soon as possible.

“I don’t want to go into a much older age in debt in any particular way,” said Milton, 78, of Dallas. “When I pay that off in three or four months, I will be debt-free.”

The Bradleys typically have paid cash for major purchases, including their home.

“My home’s paid for, my other car’s paid for and the other products I own, they’re all paid for,” Milton said. “We remodeled our home about three years ago; I was able to pay for all that without going into debt.”

Delay benefits claim

To get the highest possible payout, delay claiming Social Security if you can.

“I’m a big supporter of claiming Social Security as late as possible,” said Alicia Munnell, director of the Center for Retirement Research at Boston College. “If you can work longer, that is great, and then you claim at 70 and then you get the highest possible benefit.”

If you can’t work, use a portion of your savings to live on, she said.

“If you can’t work, but you have — say — $100,000 in your 401(k), you should use some of that to postpone claiming Social Security,” Munnell said.

Tax planning

A smart strategy for withdrawing money from taxable, tax-deferred, and tax-free accounts can save retirees in taxes, says Anthony D. Criscuolo, a senior financial planner with Palisades Hudson Financial Group.

There's an order to follow when withdrawing money.

The general rule is to withdraw funds from your taxable accounts first, Criscuolo said.

That's because when you sell stocks and mutual funds that have appreciated longer than a year, you'll pay a long-term capital gains tax, which tops out at 20 percent.

Look next to tax-deferred accounts, such as traditional IRAs and 401(k) plans. Withdrawals are taxed at your ordinary income tax rate (which can be as high as 39.6 percent), so they're a less attractive source of funds, Criscuolo said.

Once you reach age 70½, you must take the annual required minimum distribution or pay a hefty excise tax.

Withdraw money last from tax-free accounts, such as a Roth IRA.

"The longer you can keep your money in them," he said, "the better."

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