<u>Retirement Readiness</u> -- contributed by Sandra D. Adams, CFP®

As a financial planner, I am often asked by clients "When will I know that I am ready to retire?" That can be a tricky question, because there are two sides to being ready for the next phase of your life – the technical side and the personal side. While certainly you need to be financially secure for the next decades of your life, you also need to be comfortable with the transition from your life as a career individual to what you now wish to become in your next phase – and that is not as easy as it sounds.

From a financial-readiness perspective, there are some widely-known retirement "targets" that get thrown around by clients (especially those that are new to working with us):

- "When I have $1 million in assets saved, I will be ready to retire."
- "When I am eligible to collect Social Security, I will be ready to retire."
- "When I am eligible to collect my company pension OR I have reached my XX anniversary with my company, I will be ready to retire."
- "When I am eligible to receive Medicare, I will be ready to retire."

The real answer is, some or all of these may be true for you, and some or all of these may be false. Every client situation is different and no general guideline can determine whether or not you are financially ready to retire. Unfortunately, it is far more complicated than that. There are numerous financial factors that go into determining financial readiness. Let's take a deeper look into the issues.

<u>Financial Readiness Issues:</u>

- **Retirement Savings**:

  Determining whether or not you have enough saved is dependent on several factors:

  - What might your other retirement income sources be (Social Security, Pensions, etc.)
  - How much income will you need (what are your fixed costs versus lifestyle wants in retirement), and
  - What are your longevity expectations (how long might you expect to live based on health, family history, etc.—expect it will be longer than you think!).

  For some folks, expecting to spend 75% to 85% of what they spent pre-retirement is entirely realistic. For others who expect to travel more, purchase a second home, or who simply have higher lifestyle expectations, setting a lower income need expectation would not be realistic at all. It makes sense to envision what retirement looks like for you and what real costs might be so that the income numbers you are using in your planning make real sense.

  Once you have determine IF you have enough saved (or are on track to have enough saved), you need to be aware of what types of accounts the savings are in. Most folks have been well trained to funnel all of their retirement savings into the pre-tax 401(k)/403(b) plans; not only does this provide the biggest tax savings currently, but it makes it easy to save because you never see the money and it goes directly into the retirement savings account unnoticed. Unfortunately, you can easily find yourself heading into retirement with nothing but tax-deferred retirement savings and nothing else. What does this mean? It means that every dollar you need to take from investments in retirement is taxed at ordinary income tax rates on the way out. These tax deferred accounts are restricted until age 59 ½ without penalty and at age 701/2 it is subject to Required Minimum Distributions. Ultimately, having only tax deferred investments limits your tax flexibility going into retirement, and we are always uncertain as to what tax rates will look like in the future. *We find that our most successful retirees have a good mix of tax deferred, tax free (ROTH) and after tax investment accounts*.

- **Debt:** Related to retirement savings and income needs, being as debt free as possible by the time you reach retirement is ideal. This frees up your retirement income to be used for "wants" not "needs". In addition, since most debt pre-retirement is mortgage debt, reducing or eliminating that debt frees up home equity to be leveraged in retirement, when and if needed. *We find that our most successful retirees go into retirement debt free.*

- **Retirement Income:** A large part to being retirement ready is understanding your retirement income sources, options and strategies and using them to your best advantage.
  - **Pensions:** You many have the option to take a lump sum or various monthly pension payments over your lifetime and possibly over your spouse's lifetime either in full or in some percentage of your full payment. When it comes to pensions options, there is no way to give an across-the-board answer as to which option or options are better. Every plan has different options and not all plans are structured the same. It makes sense to analyze each plan and each option based on your own individual situation to see what option is best for you. *We find that our most successful retirees that have taken the lifetime pension option have some spousal benefit of at least 65% or more*.
  - **Social Security:** While many are under the false impression that because you are allowed to take Social Security benefits as early as age 62, they should, we might recommend otherwise. For most individuals now approaching Social Security claiming age, Full Retirement Age for claiming Social Security is now age 66 and delaying benefits until age 70 results in an 8% per year increase in benefits. Knowing and understanding the Social Security benefits, rules and strategies that can be employed, especially for married couples, to ensure the largest lifetime benefit can be an added supplement to long-term retirement income. *We find that our most successful married couples in retirement employ a strategy where the lower Social Security earner draws at Full Retirement age while the higher Social Security earner waits to draw at age 70, insuring the highest possible Social Security benefit for the spouse that lives the longest.*
- **Investments:** Preparing for retirement involves making appropriate adjustments to your investment strategy. While you may have been a more aggressive investor when you were younger and were accumulating assets towards retirement, now that it is time to think seriously about the next phase of life, it makes sense to reduce the risk of the portfolio and adjust your allocation according. You should work with your financial planner to adjust your asset allocation to one that is appropriate for your new

goals and time horizon. *We find that our most successful retirees tend to have asset allocations ranging from 40% Bond/60% Stock to 50% Bond/50% Stock.*

- **Insurance:**
    - For those retiring before age 65 (Medicare eligibility) and without retiree healthcare, finding health insurance to bridge them to Medicare is a must. You may be able to continue on your employer sponsored healthcare via COBRA for some time, You may be able to enroll as a spousal dependent on your spouse's employer coverage (if they are still working or have retiree health insurance) or get health insurance through the health insurance exchange (Affordable Care Act).
    - Retirement readiness does require addressing the issue of Long Term Care funding. How will you pay for long term care expenses, if/when you should need them? Will you buy insurance – traditional long term care insurance or hybrid long term care insurance? Will you utilize an existing life insurance vehicle that has options for paying for long term care? Or will you self-fund the risk? Having a plan, no matter what your choice, is something that must be done before retirement.
- **Estate Planning:** While not exactly monetary, having your estate planning documents (Durable Powers of Attorney, Wills and possibly Trust or Trusts in place) updated prior to retirement is a good idea. Part of this is making sure accounts are titled properly, beneficiaries are updated, and account holdings/locations and management are as simplified as possible going into your last phase of life. If you have been put into the position of assisting your older adult parents with managing their financial affairs, you will understand the importance of doing this for yourself (and your own children who may one day be assisting you!).

Once you have determined your *financial retirement readiness*, you need to determine your *personal retirement readiness,* which may be even more difficult for many folks. Why? Many have spent the majority of their lifetimes to this point building careers that established them with titles, credentials and stature. They built reputations, networks, social and business circles and were well respected because of the work that they have done. And now they are moving from that phase of their lives to another and that means starting over. What will they be now? What will their lives mean? And to whom?

Until you are ready to start the next phase of your life knowing your purpose – what you want to wake up for every day – you are likely not ready for retirement. Those that have not given the thought to their mission, values, and their "why" for their next phase will be left feeling lost and will likely fail at retirement and find themselves wanting to go back to their former lives. Or will be those retirees that struggle with depression, anxiety, or cannot get out of their spouse's way in retirement and find themselves the victim of the high rate of gray divorce.

How can you find your purpose?

- Ask yourself what is most important to you? (family, friends, spirituality, charity,etc)
- Ask yourself what are your life priorities? (family, health, knowledge, etc.)
- Ask yourself what you want to let go of and what you want to give yourself to.

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- Realize that the rest of your life can be the best of your life if you embrace it with an open mind and enthusiasm.
- Consider reading the book "Purposeful Retirement" by Hyrum Smith if you need more help!

"Am I ready to retire?" It is not a simple question and there is no simple answer. It may take months or years to answer all of the questions and make all of the preparations. If you think that retirement is in your not too distant future, the time is NOW to start planning. Don't let retirement sneak up on you…be Retirement Ready!

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